



REGIONAL COURSES IN INTERNATIONAL LAW

Bangkok, Thailand
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STUDY MATERIALS PART VII

Codification Division of the United Nations Office of Legal Affairs

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REGIONAL COURSES
IN INTERNATIONAL LAW

Bangkok, Thailand
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INTERNATIONAL TRADE LAW
PROFESSOR MAKANE MBENGUE

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**Agreement Establishing the World Trade
Organization, 1994**

AGREEMENT ESTABLISHING THE WORLD TRADE ORGANIZATION

The *Parties* to this Agreement,

Recognizing that their relations in the field of trade and economic endeavour should be conducted with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, and expanding the production of and trade in goods and services, while allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development,

Recognizing further that there is need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development,

Being desirous of contributing to these objectives by entering into reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international trade relations,

Resolved, therefore, to develop an integrated, more viable and durable multilateral trading system encompassing the General Agreement on Tariffs and Trade, the results of past trade liberalization efforts, and all of the results of the Uruguay Round of Multilateral Trade Negotiations,

Determined to preserve the basic principles and to further the objectives underlying this multilateral trading system,

Agree as follows:

Article I

Establishment of the Organization

The World Trade Organization (hereinafter referred to as "the WTO") is hereby established.

Article II

Scope of the WTO

1. The WTO shall provide the common institutional framework for the conduct of trade relations among its Members in matters related to the agreements and associated legal instruments included in the Annexes to this Agreement.

2. The agreements and associated legal instruments included in Annexes 1, 2 and 3 (hereinafter referred to as "Multilateral Trade Agreements") are integral parts of this Agreement, binding on all Members.

3. The agreements and associated legal instruments included in Annex 4 (hereinafter referred to as "Plurilateral Trade Agreements") are also part of this Agreement for those Members that have

accepted them, and are binding on those Members. The Plurilateral Trade Agreements do not create either obligations or rights for Members that have not accepted them.

4. The General Agreement on Tariffs and Trade 1994 as specified in Annex 1A (hereinafter referred to as "GATT 1994") is legally distinct from the General Agreement on Tariffs and Trade, dated 30 October 1947, annexed to the Final Act Adopted at the Conclusion of the Second Session of the Preparatory Committee of the United Nations Conference on Trade and Employment, as subsequently rectified, amended or modified (hereinafter referred to as "GATT 1947").

Article III

Functions of the WTO

1. The WTO shall facilitate the implementation, administration and operation, and further the objectives, of this Agreement and of the Multilateral Trade Agreements, and shall also provide the framework for the implementation, administration and operation of the Plurilateral Trade Agreements.

2. The WTO shall provide the forum for negotiations among its Members concerning their multilateral trade relations in matters dealt with under the agreements in the Annexes to this Agreement. The WTO may also provide a forum for further negotiations among its Members concerning their multilateral trade relations, and a framework for the implementation of the results of such negotiations, as may be decided by the Ministerial Conference.

3. The WTO shall administer the Understanding on Rules and Procedures Governing the Settlement of Disputes (hereinafter referred to as the "Dispute Settlement Understanding" or "DSU") in Annex 2 to this Agreement.

4. The WTO shall administer the Trade Policy Review Mechanism (hereinafter referred to as the "TPRM") provided for in Annex 3 to this Agreement.

5. With a view to achieving greater coherence in global economic policy-making, the WTO shall cooperate, as appropriate, with the International Monetary Fund and with the International Bank for Reconstruction and Development and its affiliated agencies.

Article IV

Structure of the WTO

1. There shall be a Ministerial Conference composed of representatives of all the Members, which shall meet at least once every two years. The Ministerial Conference shall carry out the functions of the WTO and take actions necessary to this effect. The Ministerial Conference shall have the authority to take decisions on all matters under any of the Multilateral Trade Agreements, if so requested by a Member, in accordance with the specific requirements for decision-making in this Agreement and in the relevant Multilateral Trade Agreement.

2. There shall be a General Council composed of representatives of all the Members, which shall meet as appropriate. In the intervals between meetings of the Ministerial Conference, its functions shall be conducted by the General Council. The General Council shall also carry out the functions assigned to it by this Agreement. The General Council shall establish its rules of procedure and approve the rules of procedure for the Committees provided for in paragraph 7.

3. The General Council shall convene as appropriate to discharge the responsibilities of the Dispute Settlement Body provided for in the Dispute Settlement Understanding. The Dispute Settlement Body may have its own chairman and shall establish such rules of procedure as it deems necessary for the fulfilment of those responsibilities.

4. The General Council shall convene as appropriate to discharge the responsibilities of the Trade Policy Review Body provided for in the TPRM. The Trade Policy Review Body may have its own chairman and shall establish such rules of procedure as it deems necessary for the fulfilment of those responsibilities.

5. There shall be a Council for Trade in Goods, a Council for Trade in Services and a Council for Trade-Related Aspects of Intellectual Property Rights (hereinafter referred to as the "Council for TRIPS"), which shall operate under the general guidance of the General Council. The Council for Trade in Goods shall oversee the functioning of the Multilateral Trade Agreements in Annex 1A. The Council for Trade in Services shall oversee the functioning of the General Agreement on Trade in Services (hereinafter referred to as "GATS"). The Council for TRIPS shall oversee the functioning of the Agreement on Trade-Related Aspects of Intellectual Property Rights (hereinafter referred to as the "Agreement on TRIPS"). These Councils shall carry out the functions assigned to them by their respective agreements and by the General Council. They shall establish their respective rules of procedure subject to the approval of the General Council. Membership in these Councils shall be open to representatives of all Members. These Councils shall meet as necessary to carry out their functions.

6. The Council for Trade in Goods, the Council for Trade in Services and the Council for TRIPS shall establish subsidiary bodies as required. These subsidiary bodies shall establish their respective rules of procedure subject to the approval of their respective Councils.

7. The Ministerial Conference shall establish a Committee on Trade and Development, a Committee on Balance-of-Payments Restrictions and a Committee on Budget, Finance and Administration, which shall carry out the functions assigned to them by this Agreement and by the Multilateral Trade Agreements, and any additional functions assigned to them by the General Council, and may establish such additional Committees with such functions as it may deem appropriate. As part of its functions, the Committee on Trade and Development shall periodically review the special provisions in the Multilateral Trade Agreements in favour of the least-developed country Members and report to the General Council for appropriate action. Membership in these Committees shall be open to representatives of all Members.

8. The bodies provided for under the Plurilateral Trade Agreements shall carry out the functions assigned to them under those Agreements and shall operate within the institutional framework of the WTO. These bodies shall keep the General Council informed of their activities on a regular basis.

Article V

Relations with Other Organizations

1. The General Council shall make appropriate arrangements for effective cooperation with other intergovernmental organizations that have responsibilities related to those of the WTO.

2. The General Council may make appropriate arrangements for consultation and cooperation with non-governmental organizations concerned with matters related to those of the WTO.

Article VI

The Secretariat

1. There shall be a Secretariat of the WTO (hereinafter referred to as "the Secretariat") headed by a Director-General.

2. The Ministerial Conference shall appoint the Director-General and adopt regulations setting out the powers, duties, conditions of service and term of office of the Director-General.

3. The Director-General shall appoint the members of the staff of the Secretariat and determine their duties and conditions of service in accordance with regulations adopted by the Ministerial Conference.

4. The responsibilities of the Director-General and of the staff of the Secretariat shall be exclusively international in character. In the discharge of their duties, the Director-General and the staff of the Secretariat shall not seek or accept instructions from any government or any other authority external to the WTO. They shall refrain from any action which might adversely reflect on their position as international officials. The Members of the WTO shall respect the international character of the responsibilities of the Director-General and of the staff of the Secretariat and shall not seek to influence them in the discharge of their duties.

Article VII

Budget and Contributions

1. The Director-General shall present to the Committee on Budget, Finance and Administration the annual budget estimate and financial statement of the WTO. The Committee on Budget, Finance and Administration shall review the annual budget estimate and the financial statement presented by the Director-General and make recommendations thereon to the General Council. The annual budget estimate shall be subject to approval by the General Council.

2. The Committee on Budget, Finance and Administration shall propose to the General Council financial regulations which shall include provisions setting out:

(a) the scale of contributions apportioning the expenses of the WTO among its Members; and

(b) the measures to be taken in respect of Members in arrears.

The financial regulations shall be based, as far as practicable, on the regulations and practices of GATT 1947.

3. The General Council shall adopt the financial regulations and the annual budget estimate by a two-thirds majority comprising more than half of the Members of the WTO.

4. Each Member shall promptly contribute to the WTO its share in the expenses of the WTO in accordance with the financial regulations adopted by the General Council.

Article VIII

Status of the WTO

1. The WTO shall have legal personality, and shall be accorded by each of its Members such legal capacity as may be necessary for the exercise of its functions.
2. The WTO shall be accorded by each of its Members such privileges and immunities as are necessary for the exercise of its functions.
3. The officials of the WTO and the representatives of the Members shall similarly be accorded by each of its Members such privileges and immunities as are necessary for the independent exercise of their functions in connection with the WTO.
4. The privileges and immunities to be accorded by a Member to the WTO, its officials, and the representatives of its Members shall be similar to the privileges and immunities stipulated in the Convention on the Privileges and Immunities of the Specialized Agencies, approved by the General Assembly of the United Nations on 21 November 1947.
5. The WTO may conclude a headquarters agreement.

Article IX

Decision-Making

1. The WTO shall continue the practice of decision-making by consensus followed under GATT 1947.¹ Except as otherwise provided, where a decision cannot be arrived at by consensus, the matter at issue shall be decided by voting. At meetings of the Ministerial Conference and the General Council, each Member of the WTO shall have one vote. Where the European Communities exercise their right to vote, they shall have a number of votes equal to the number of their member States² which are Members of the WTO. Decisions of the Ministerial Conference and the General Council shall be taken by a majority of the votes cast, unless otherwise provided in this Agreement or in the relevant Multilateral Trade Agreement.³
2. The Ministerial Conference and the General Council shall have the exclusive authority to adopt interpretations of this Agreement and of the Multilateral Trade Agreements. In the case of an interpretation of a Multilateral Trade Agreement in Annex 1, they shall exercise their authority on the basis of a recommendation by the Council overseeing the functioning of that Agreement. The decision to adopt an interpretation shall be taken by a three-fourths majority of the Members. This paragraph shall not be used in a manner that would undermine the amendment provisions in Article X.
3. In exceptional circumstances, the Ministerial Conference may decide to waive an obligation imposed on a Member by this Agreement or any of the Multilateral Trade Agreements, provided that

¹The body concerned shall be deemed to have decided by consensus on a matter submitted for its consideration, if no Member, present at the meeting when the decision is taken, formally objects to the proposed decision.

²The number of votes of the European Communities and their member States shall in no case exceed the number of the member States of the European Communities.

³Decisions by the General Council when convened as the Dispute Settlement Body shall be taken only in accordance with the provisions of paragraph 4 of Article 2 of the Dispute Settlement Understanding.

any such decision shall be taken by three fourths⁴ of the Members unless otherwise provided for in this paragraph.

- (a) A request for a waiver concerning this Agreement shall be submitted to the Ministerial Conference for consideration pursuant to the practice of decision-making by consensus. The Ministerial Conference shall establish a time-period, which shall not exceed 90 days, to consider the request. If consensus is not reached during the time-period, any decision to grant a waiver shall be taken by three fourths⁴ of the Members.
- (b) A request for a waiver concerning the Multilateral Trade Agreements in Annexes 1A or 1B or 1C and their annexes shall be submitted initially to the Council for Trade in Goods, the Council for Trade in Services or the Council for TRIPS, respectively, for consideration during a time-period which shall not exceed 90 days. At the end of the time-period, the relevant Council shall submit a report to the Ministerial Conference.
4. A decision by the Ministerial Conference granting a waiver shall state the exceptional circumstances justifying the decision, the terms and conditions governing the application of the waiver, and the date on which the waiver shall terminate. Any waiver granted for a period of more than one year shall be reviewed by the Ministerial Conference not later than one year after it is granted, and thereafter annually until the waiver terminates. In each review, the Ministerial Conference shall examine whether the exceptional circumstances justifying the waiver still exist and whether the terms and conditions attached to the waiver have been met. The Ministerial Conference, on the basis of the annual review, may extend, modify or terminate the waiver.
5. Decisions under a Plurilateral Trade Agreement, including any decisions on interpretations and waivers, shall be governed by the provisions of that Agreement.

Article X

Amendments

1. Any Member of the WTO may initiate a proposal to amend the provisions of this Agreement or the Multilateral Trade Agreements in Annex 1 by submitting such proposal to the Ministerial Conference. The Councils listed in paragraph 5 of Article IV may also submit to the Ministerial Conference proposals to amend the provisions of the corresponding Multilateral Trade Agreements in Annex 1 the functioning of which they oversee. Unless the Ministerial Conference decides on a longer period, for a period of 90 days after the proposal has been tabled formally at the Ministerial Conference any decision by the Ministerial Conference to submit the proposed amendment to the Members for acceptance shall be taken by consensus. Unless the provisions of paragraphs 2, 5 or 6 apply, that decision shall specify whether the provisions of paragraphs 3 or 4 shall apply. If consensus is reached, the Ministerial Conference shall forthwith submit the proposed amendment to the Members for acceptance. If consensus is not reached at a meeting of the Ministerial Conference within the established period, the Ministerial Conference shall decide by a two-thirds majority of the Members whether to submit the proposed amendment to the Members for acceptance. Except as provided in paragraphs 2, 5 and 6, the provisions of paragraph 3 shall apply to the proposed amendment, unless the Ministerial Conference decides by a three-fourths majority of the Members that the provisions of paragraph 4 shall apply.
2. Amendments to the provisions of this Article and to the provisions of the following Articles shall take effect only upon acceptance by all Members:

⁴A decision to grant a waiver in respect of any obligation subject to a transition period or a period for staged implementation that the requesting Member has not performed by the end of the relevant period shall be taken only by consensus.

Article IX of this Agreement;
 Articles I and II of GATT 1994;
 Article II:1 of GATS;
 Article 4 of the Agreement on TRIPS.

3. Amendments to provisions of this Agreement, or of the Multilateral Trade Agreements in Annexes IA and IC, other than those listed in paragraphs 2 and 6, of a nature that would alter the rights and obligations of the Members, shall take effect for the Members that have accepted them upon acceptance by two thirds of the Members and thereafter for each other Member upon acceptance by it. The Ministerial Conference may decide by a three-fourths majority of the Members that any amendment made effective under this paragraph is of such a nature that any Member which has not accepted it within a period specified by the Ministerial Conference in each case shall be free to withdraw from the WTO or to remain a Member with the consent of the Ministerial Conference.
4. Amendments to provisions of this Agreement or of the Multilateral Trade Agreements in Annexes IA and IC, other than those listed in paragraphs 2 and 6, of a nature that would not alter the rights and obligations of the Members, shall take effect for all Members upon acceptance by two thirds of the Members.
5. Except as provided in paragraph 2 above, amendments to Parts I, II and III of GATS and the respective annexes shall take effect for the Members that have accepted them upon acceptance by two thirds of the Members and thereafter for each Member upon acceptance by it. The Ministerial Conference may decide by a three-fourths majority of the Members that any amendment made effective under the preceding provision is of such a nature that any Member which has not accepted it within a period specified by the Ministerial Conference in each case shall be free to withdraw from the WTO or to remain a Member with the consent of the Ministerial Conference. Amendments to Parts IV, V and VI of GATS and the respective annexes shall take effect for all Members upon acceptance by two thirds of the Members.
6. Notwithstanding the other provisions of this Article, amendments to the Agreement on TRIPS meeting the requirements of paragraph 2 of Article 71 thereof may be adopted by the Ministerial Conference without further formal acceptance process.
7. Any Member accepting an amendment to this Agreement or to a Multilateral Trade Agreement in Annex 1 shall deposit an instrument of acceptance with the Director-General of the WTO within the period of acceptance specified by the Ministerial Conference.
8. Any Member of the WTO may initiate a proposal to amend the provisions of the Multilateral Trade Agreements in Annexes 2 and 3 by submitting such proposal to the Ministerial Conference. The decision to approve amendments to the Multilateral Trade Agreement in Annex 2 shall be made by consensus and these amendments shall take effect for all Members upon approval by the Ministerial Conference. Decisions to approve amendments to the Multilateral Trade Agreement in Annex 3 shall take effect for all Members upon approval by the Ministerial Conference.
9. The Ministerial Conference, upon the request of the Members parties to a trade agreement, may decide exclusively by consensus to add that agreement to Annex 4. The Ministerial Conference, upon the request of the Members parties to a Plurilateral Trade Agreement, may decide to delete that Agreement from Annex 4.
10. Amendments to a Plurilateral Trade Agreement shall be governed by the provisions of that Agreement.

Article XI
Original Membership

1. The contracting parties to GATT 1947 as of the date of entry into force of this Agreement, and the European Communities, which accept this Agreement and the Multilateral Trade Agreements and for which Schedules of Concessions and Commitments are annexed to GATT 1994 and for which Schedules of Specific Commitments are annexed to GATS shall become original Members of the WTO.
 2. The least-developed countries recognized as such by the United Nations will only be required to undertake commitments and concessions to the extent consistent with their individual development, financial and trade needs or their administrative and institutional capabilities.
- Article XII*
Accession
1. Any State or separate customs territory possessing full autonomy in the conduct of its external commercial relations and of the other matters provided for in this Agreement and the Multilateral Trade Agreements may accede to this Agreement, on terms to be agreed between it and the WTO. Such accession shall apply to this Agreement and the Multilateral Trade Agreements annexed thereto.
 2. Decisions on accession shall be taken by the Ministerial Conference. The Ministerial Conference shall approve the agreement on the terms of accession by a two-thirds majority of the Members of the WTO.
 3. Accession to a Plurilateral Trade Agreement shall be governed by the provisions of that Agreement.

Article XIII

*Non-Applcation of Multilateral Trade Agreements
 between Particular Members*

1. This Agreement and the Multilateral Trade Agreements in Annexes 1 and 2 shall not apply as between any Member and any other Member if either of the Members, at the time either becomes a Member, does not consent to such application.
2. Paragraph 1 may be invoked between original Members of the WTO which were contracting parties to GATT 1947 only where Article XXXV of that Agreement had been invoked earlier and was effective as between those contracting parties at the time of entry into force for them of this Agreement.
3. Paragraph 1 shall apply between a Member and another Member which has acceded under Article XII only if the Member not consenting to the application has so notified the Ministerial Conference before the approval of the agreement on the terms of accession by the Ministerial Conference.
4. The Ministerial Conference may review the operation of this Article in particular cases at the request of any Member and make appropriate recommendations.
5. Non-application of a Plurilateral Trade Agreement between parties to that Agreement shall be governed by the provisions of that Agreement.

Article XIV

Acceptance, Entry into Force and Deposit

1. This Agreement shall be open for acceptance, by signature or otherwise, by contracting parties to GATT 1947, and the European Communities, which are eligible to become original Members of the WTO in accordance with Article XI of this Agreement. Such acceptance shall apply to this Agreement and the Multilateral Trade Agreements annexed hereto. This Agreement and the Multilateral Trade Agreements annexed hereto shall enter into force on the date determined by Ministers in accordance with paragraph 3 of the Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations and shall remain open for acceptance for a period of two years following that date unless the Ministers decide otherwise. An acceptance following the entry into force of this Agreement shall enter into force on the 30th day following the date of such acceptance.

2. A Member which accepts this Agreement after its entry into force shall implement those concessions and obligations in the Multilateral Trade Agreements that are to be implemented over a period of time starting with the entry into force of this Agreement as if it had accepted this Agreement on the date of its entry into force.

3. Until the entry into force of this Agreement, the text of this Agreement and the Multilateral Trade Agreements shall be deposited with the Director-General to the CONTRACTING PARTIES to GATT 1947. The Director-General shall promptly furnish a certified true copy of this Agreement and the Multilateral Trade Agreements, and a notification of each acceptance thereof, to each government and the European Communities having accepted this Agreement. This Agreement and the Multilateral Trade Agreements, and any amendments thereto, shall, upon the entry into force of this Agreement, be deposited with the Director-General of the WTO.

4. The acceptance and entry into force of a Plurilateral Trade Agreement shall be governed by the provisions of that Agreement. Such Agreements shall be deposited with the Director-General to the CONTRACTING PARTIES to GATT 1947. Upon the entry into force of this Agreement, such Agreements shall be deposited with the Director-General of the WTO.

Article XV

Withdrawal

1. Any Member may withdraw from this Agreement. Such withdrawal shall apply both to this Agreement and the Multilateral Trade Agreements and shall take effect upon the expiration of six months from the date on which written notice of withdrawal is received by the Director-General of the WTO.

2. Withdrawal from a Plurilateral Trade Agreement shall be governed by the provisions of that Agreement.

Article XVI

Miscellaneous Provisions

1. Except as otherwise provided under this Agreement or the Multilateral Trade Agreements, the WTO shall be guided by the decisions, procedures and customary practices followed by the CONTRACTING PARTIES to GATT 1947 and the bodies established in the framework of GATT 1947.

2. To the extent practicable, the Secretariat of GATT 1947 shall become the Secretariat of the WTO, and the Director-General to the CONTRACTING PARTIES to GATT 1947, until such time as the Ministerial Conference has appointed a Director-General in accordance with paragraph 2 of Article VI of this Agreement, shall serve as Director-General of the WTO.

3. In the event of a conflict between a provision of this Agreement and a provision of any of the Multilateral Trade Agreements, the provision of this Agreement shall prevail to the extent of the conflict.

4. Each Member shall ensure the conformity of its laws, regulations and administrative procedures with its obligations as provided in the annexed Agreements.

5. No reservations may be made in respect of any provision of this Agreement. Reservations in respect of any of the provisions of the Multilateral Trade Agreements may only be made to the extent provided for in those Agreements. Reservations in respect of a provision of a Plurilateral Trade Agreement shall be governed by the provisions of that Agreement.

6. This Agreement shall be registered in accordance with the provisions of Article 102 of the Charter of the United Nations.

DONE at Marrakesh this fifteenth day of April one thousand nine hundred and ninety-four, in a single copy, in the English, French and Spanish languages, each text being authentic.

Explanatory Notes:

The terms "country" or "countries" as used in this Agreement and the Multilateral Trade Agreements are to be understood to include any separate customs territory Member of the WTO.

In the case of a separate customs territory Member of the WTO, where an expression in this Agreement and the Multilateral Trade Agreements is qualified by the term "national", such expression shall be read as pertaining to that customs territory, unless otherwise specified.

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- Agreement on Agriculture
- Agreement on the Application of Sanitary and Phytosanitary Measures
- Agreement on Textiles and Clothing
- Agreement on Technical Barriers to Trade
- Agreement on Trade-Related Investment Measures
- Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994
- Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994
- Agreement on Preshipment Inspection
- Agreement on Rules of Origin
- Agreement on Import Licensing Procedures
- Agreement on Subsidies and Countervailing Measures
- Agreement on Safeguards

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ANNEX 3

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ANNEX 4

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- Agreement on Government Procurement
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General Agreement on Tariffs and Trade, 1947
(now incorporated into GATT 1994)

THE GENERAL AGREEMENT ON TARIFFS AND TRADE

("GATT 1947")

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The Governments of the COMMONWEALTH OF AUSTRALIA, the KINGDOM OF BELGIUM, the UNITED STATES OF BRAZIL, BURMA, CANADA, CEYLON, the REPUBLIC OF CHILE, the REPUBLIC OF CHINA, the REPUBLIC OF CUBA, the CZECHOSLOVAK REPUBLIC, the FRENCH REPUBLIC, INDIA, LEBANON, the GRAND-DUCHY OF LUXEMBURG, the KINGDOM OF THE NETHERLANDS, NEW ZEALAND, the KINGDOM OF NORWAY, PAKISTAN, SOUTHERN RHODESIA, SYRIA, the UNION OF SOUTH AFRICA, the UNITED KINGDOM OF GREAT BRITAIN AND NORTHERN IRELAND, and the UNITED STATES OF AMERICA:

Recognizing that their relations in the field of trade and economic endeavour should be conducted with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, developing the full use of the resources of the world and expanding the production and exchange of goods,

Being desirous of contributing to these objectives by entering into reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international commerce,

Have through their Representatives agreed as follows:

PART I

Article I: General Most-Favoured-Nation Treatment

1. With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation or imposed on the international transfer of payments for imports or exports, and with respect to the method of levying such duties and charges, and with respect to all rules and formalities in connection with importation and exportation, and with respect to all matters referred to in paragraphs 2 and 4 of Article III,* any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties.
2. The provisions of paragraph 1 of this Article shall not require the elimination of any preferences in respect of import duties or charges which do not exceed the levels provided for in paragraph 4 of this Article and which fall within the following descriptions:
 - (a) Preferences in force exclusively between two or more of the territories listed in Annex A, subject to the conditions set forth therein;
 - (b) Preferences in force exclusively between two or more territories which on July 1, 1939, were connected by common sovereignty or relations of protection or suzerainty and which are listed in Annexes B, C and D, subject to the conditions set forth therein;
 - (c) Preferences in force exclusively between the United States of America and the Republic of Cuba;
 - (d) Preferences in force exclusively between neighbouring countries listed in Annexes E and F.
3. The provisions of paragraph 1 shall not apply to preferences between the countries formerly a part of the Ottoman Empire and detached from it on July 24, 1923, provided such preferences are approved under paragraph 5¹ of Article XXV, which shall be applied in this respect in the light of paragraph 1 of Article XXIX.
4. The margin of preference* on any product in respect of which a preference is permitted under paragraph 2 of this Article but is not specifically set forth as a maximum margin of preference in the appropriate Schedule annexed to this Agreement shall not exceed:
 - (a) in respect of duties or charges on any product described in such Schedule, the difference between the most-favoured-nation and preferential rates provided for therein; if no preferential rate is provided for, the preferential rate shall for the purposes of this paragraph be taken to be that in force on April 10, 1947, and, if no most-favoured-nation rate is provided for, the margin shall not exceed the difference between the most-favoured-nation and preferential rates existing on April 10, 1947;
 - (b) in respect of duties or charges on any product not described in the appropriate Schedule, the difference between the most-favoured-nation and preferential rates existing on April 10, 1947.

In the case of the contracting parties named in Annex G, the date of April 10, 1947, referred to in sub-paragraph (a) and (b) of this paragraph shall be replaced by the respective dates set forth in that

¹ The authentic text erroneously reads "subparagraph 5 (a)".

Annex.

Article II: Schedules of Concessions

1. (a) Each contracting party shall accord to the commerce of the other contracting parties treatment no less favourable than that provided for in the appropriate Part of the appropriate Schedule annexed to this Agreement.
- (b) The products described in Part I of the Schedule relating to any contracting party, which are the products of territories of other contracting parties, shall, on their importation into the territory to which the Schedule relates, and subject to the terms, conditions or qualifications set forth in that Schedule, be exempt from ordinary customs duties in excess of those set forth and provided therein. Such products shall also be exempt from all other duties or charges of any kind imposed on or in connection with the importation in excess of those imposed on the date of this Agreement or those directly and mandatorily required to be imposed thereafter by legislation in force in the importing territory on that date.
- (c) The products described in Part II of the Schedule relating to any contracting party which are the products of territories entitled under Article I to receive preferential treatment upon importation into the territory to which the Schedule relates shall, on their importation into such territory, and subject to the terms, conditions or qualifications set forth in that Schedule, be exempt from ordinary customs duties in excess of those set forth and provided for in Part II of that Schedule. Such products shall also be exempt from all other duties or charges of any kind imposed on or in connection with importation in excess of those imposed on the date of this Agreement or those directly or mandatorily required to be imposed thereafter by legislation in force in the importing territory on that date. Nothing in this Article shall prevent any contracting party from maintaining its requirements existing on the date of this Agreement as to the eligibility of goods for entry at preferential rates of duty.
2. Nothing in this Article shall prevent any contracting party from imposing at any time on the importation of any product:
 - (a) a charge equivalent to an internal tax imposed consistently with the provisions of paragraph 2 of Article III* in respect of the like domestic product or in respect of an article from which the imported product has been manufactured or produced in whole or in part;
 - (b) any anti-dumping or countervailing duty applied consistently with the provisions of Article VI*;
 - (c) fees or other charges commensurate with the cost of services rendered.
3. No contracting party shall alter its method of determining dutiable value or of converting currencies so as to impair the value of any of the concessions provided for in the appropriate Schedule annexed to this Agreement.
4. If any contracting party establishes, maintains or authorizes, formally or in effect, a monopoly of the importation of any product described in the appropriate Schedule annexed to this Agreement, such monopoly shall not, except as provided for in that Schedule or as otherwise agreed between the parties which initially negotiated the concession, operate so as to afford protection on the average in excess of the amount of protection provided for in that Schedule. The provisions of this paragraph shall not limit the use by contracting parties of any form of assistance to domestic producers permitted by other provisions of this Agreement.*
5. If any contracting party considers that a product is not receiving from another contracting

party the treatment which the first contracting party believes to have been contemplated by a concession provided for in the appropriate Schedule annexed to this Agreement, it shall bring the matter directly to the attention of the other contracting party. If the latter agrees that the treatment contemplated was that claimed by the first contracting party, but declares that such treatment cannot be accorded because a court or other proper authority has ruled to the effect that the product involved cannot be classified under the tariff laws of such contracting party so as to permit the treatment contemplated in this Agreement, the two contracting parties, together with any other contracting parties substantially interested, shall enter promptly into further negotiations with a view to a compensatory adjustment of the matter.

6. (a) The specific duties and charges included in the Schedules relating to contracting parties members of the International Monetary Fund, and margins of preference in specific duties and charges maintained by such contracting parties, are expressed in the appropriate currency at the par value accepted or provisionally recognized by the Fund at the date of this Agreement. Accordingly, in case this par value is reduced consistently with the Articles of Agreement of the International Monetary Fund by more than twenty per centum, such specific duties and charges and margins of preference may be adjusted to take account of such reduction; *provided* that the CONTRACTING PARTIES (*i.e.*, the contracting parties acting jointly as provided for in Article XXV) concur that such adjustments will not impair the value of the concessions provided for in the appropriate Schedule or elsewhere in this Agreement, due account being taken of all factors which may influence the need for, or urgency of, such adjustments.

(b) Similar provisions shall apply to any contracting party not a member of the Fund, as from the date on which such contracting party becomes a member of the Fund or enters into a special exchange agreement in pursuance of Article XV.

7. The Schedules annexed to this Agreement are hereby made an integral part of Part I of this Agreement.

PART II

Article III: National Treatment on Internal Taxation and Regulation*

1. The contracting parties recognize that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products, and internal quantitative regulations requiring the mixture, processing or use of products in specified amounts or proportions, should not be applied to imported or domestic products so as to afford protection to domestic production.*
2. The products of the territory of any contracting party imported into the territory of any other contracting party shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products. Moreover, no contracting party shall otherwise apply internal taxes or other internal charges to imported or domestic products in a manner contrary to the principles set forth in paragraph 1.*
3. With respect to any existing internal tax which is inconsistent with the provisions of paragraph 2, but which is specifically authorized under a trade agreement, in force on April 10, 1947, in which the import duty on the taxed product is bound against increase, the contracting party imposing the tax shall be free to postpone the application of the provisions of paragraph 2 to such tax until such time as it can obtain release from the obligations of such trade agreement in order to permit the increase of such duty to the extent necessary to compensate for the elimination of the protective element of the tax.

4. The products of the territory of any contracting party imported into the territory of any other contracting party shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use. The provisions of this paragraph shall not prevent the application of differential internal transportation charges which are based exclusively on the economic operation of the means of transport and not on the nationality of the product.

5. No contracting party shall establish or maintain any internal quantitative regulation relating to the mixture, processing or use of products in specified amounts or proportions which requires, directly or indirectly, that any specified amount or proportion of any product which is the subject of the regulation must be supplied from domestic sources. Moreover, no contracting party shall otherwise apply internal quantitative regulations in a manner contrary to the principles set forth in paragraph 1.*

6. The provisions of paragraph 5 shall not apply to any internal quantitative regulation in force in the territory of any contracting party on July 1, 1939, April 10, 1947, or March 24, 1948, at the option of that contracting party; *Provided* that any such regulation which is contrary to the provisions of paragraph 5 shall not be modified to the detriment of imports and shall be treated as a customs duty for the purpose of negotiation.

7. No internal quantitative regulation relating to the mixture, processing or use of products in specified amounts or proportions shall be applied in such a manner as to allocate any such amount or proportion among external sources of supply.

8. (a) The provisions of this Article shall not apply to laws, regulations or requirements governing the procurement by governmental agencies of products purchased for governmental purposes and not with a view to commercial resale or with a view to use in the production of goods for commercial sale.

(b) The provisions of this Article shall not prevent the payment of subsidies exclusively to domestic producers, including payments to domestic producers derived from the proceeds of internal taxes or charges applied consistently with the provisions of this Article and subsidies effected through governmental purchases of domestic products.

9. The contracting parties recognize that internal maximum price control measures, even though conforming to the other provisions of this Article, can have effects prejudicial to the interests of contracting parties supplying imported products. Accordingly, contracting parties applying such measures shall take account of the interests of exporting contracting parties with a view to avoiding to the fullest practicable extent such prejudicial effects.

10. The provisions of this Article shall not prevent any contracting party from establishing or maintaining internal quantitative regulations relating to exposed cinematograph films and meeting the requirements of Article IV.

Article IV: Special Provisions relating to Cinematograph Films

If any contracting party establishes or maintains internal quantitative regulations relating to exposed cinematograph films, such regulations shall take the form of screen quotas which shall conform to the following requirements:

(a) Screen quotas may require the exhibition of cinematograph films of national origin during a specified minimum proportion of the total screen time actually utilized, over a specified period of not less than one year, in the commercial exhibition of all films of whatever

origin, and shall be computed on the basis of screen time per theatre per year or the equivalent thereof;

(b) With the exception of screen time reserved for films of national origin under a screen quota, screen time including that released by administrative action from screen time reserved for films of national origin, shall not be allocated formally or in effect among sources of supply;

(c) Notwithstanding the provisions of sub-paragraph (b) of this Article, any contracting party may maintain screen quotas conforming to the requirements of sub-paragraph (a) of this Article which reserve a minimum proportion of screen time for films of a specified origin other than that of the contracting party imposing such screen quotas; *Provided* that no such minimum proportion of screen time shall be increased above the level in effect on April 10, 1947;

(d) Screen quotas shall be subject to negotiation for their limitation, liberalization or elimination.

Article V: Freedom of Transit

1. Goods (including baggage), and also vessels and other means of transport, shall be deemed to be in transit across the territory of a contracting party when the passage across such territory, with or without trans-shipment, warehousing, breaking bulk, or change in the mode of transport, is only a portion of a complete journey beginning and terminating beyond the frontier of the contracting party across whose territory the traffic passes. Traffic of this nature is termed in this article "traffic in transit".

2. There shall be freedom of transit through the territory of each contracting party, via the routes most convenient for international transit, for traffic in transit to or from the territory of other contracting parties. No distinction shall be made which is based on the flag of vessels, the place of origin, departure, entry, exit or destination, or on any circumstances relating to the ownership of goods, of vessels or of other means of transport.

3. Any contracting party may require that traffic in transit through its territory be entered at the proper custom house, but, except in cases of failure to comply with applicable customs laws and regulations, such traffic coming from or going to the territory of other contracting parties shall not be subject to any unnecessary delays or restrictions and shall be exempt from customs duties and from all transit duties or other charges imposed in respect of transit, except charges for transportation or those commensurate with administrative expenses entailed by transit or with the cost of services rendered.

4. All charges and regulations imposed by contracting parties on traffic in transit to or from the territories of other contracting parties shall be reasonable, having regard to the conditions of the traffic.

5. With respect to all charges, regulations and formalities in connection with transit, each contracting party shall accord to traffic in transit to or from the territory of any other contracting party treatment no less favourable than the treatment accorded to traffic in transit to or from any third country.*

6. Each contracting party shall accord to products which have been in transit through the territory of any other contracting party treatment no less favourable than that which would have been accorded to such products had they been transported from their place of origin to their

destination without going through the territory of such other contracting party. Any contracting party shall, however, be free to maintain its requirements of direct consignment existing on the date of this Agreement, in respect of any goods in regard to which such direct consignment is a requisite condition of eligibility for entry of the goods at preferential rates of duty or has relation to the contracting party's prescribed method of valuation for duty purposes.

7. The provisions of this Article shall not apply to the operation of aircraft in transit, but shall apply to air transit of goods (including baggage).

Article VI: Anti-dumping and Countervailing Duties

1. The contracting parties recognize that dumping, by which products of one country are introduced into the commerce of another country at less than the normal value of the products, is to be condemned if it causes or threatens material injury to an established industry in the territory of a contracting party or materially retards the establishment of a domestic industry. For the purposes of this Article, a product is to be considered as being introduced into the commerce of an importing country at less than its normal value, if the price of the product exported from one country to another

(a) is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country, or,

(b) in the absence of such domestic price, is less than either

- (i) the highest comparable price for the like product for export to any third country in the ordinary course of trade, or
- (ii) the cost of production of the product in the country of origin plus a reasonable addition for selling cost and profit.

Due allowance shall be made in each case for differences in conditions and terms of sale, for differences in taxation, and for other differences affecting price comparability.*

2. In order to offset or prevent dumping, a contracting party may levy on any dumped product an anti-dumping duty not greater in amount than the margin of dumping in respect of such product. For the purposes of this Article, the margin of dumping is the price difference determined in accordance with the provisions of paragraph 1.*

3. No countervailing duty shall be levied on any product of the territory of any contracting party imported into the territory of another contracting party in excess of an amount equal to the estimated bounty or subsidy determined to have been granted, directly or indirectly, on the manufacture, production or export of such product in the country of origin or exportation, including any special subsidy to the transportation of a particular product. The term "countervailing duty" shall be understood to mean a special duty levied for the purpose of offsetting any bounty or subsidy bestowed, directly, or indirectly, upon the manufacture, production or export of any merchandise.*

4. No product of the territory of any contracting party imported into the territory of any other contracting party shall be subject to anti-dumping or countervailing duty by reason of the exemption of such product from duties or taxes borne by the like product when destined for consumption in the country of origin or exportation, or by reason of the refund of such duties or taxes.

5. No product of the territory of any contracting party imported into the territory of any other contracting party shall be subject to both anti-dumping and countervailing duties to compensate for the same situation of dumping or export subsidization.

6. (a) No contracting party shall levy any anti-dumping or countervailing duty on the importation of any product of the territory of another contracting party unless it determines that the effect of the dumping or subsidization, as the case may be, is such as to cause or threaten material injury to an established domestic industry, or is such as to retard materially the establishment of a domestic industry.

(b) The CONTRACTING PARTIES may waive the requirement of sub-paragraph (a) of this paragraph so as to permit a contracting party to levy an anti-dumping or countervailing duty on the importation of any product for the purpose of offsetting dumping or subsidization which causes or threatens material injury to an industry in the territory of another contracting party exporting the product concerned to the territory of the importing contracting party. The CONTRACTING PARTIES shall waive the requirements of sub-paragraph (a) of this paragraph, so as to permit the levying of a countervailing duty, in cases in which they find that a subsidy is causing or threatening material injury to an industry in the territory of another contracting party exporting the product concerned to the territory of the importing contracting party.*

(c) In exceptional circumstances, however, where delay might cause damage which would be difficult to repair, a contracting party may levy a countervailing duty for the purpose referred to in sub-paragraph (b) of this paragraph without the prior approval of the CONTRACTING PARTIES; *Provided* that such action shall be reported immediately to the CONTRACTING PARTIES and that the countervailing duty shall be withdrawn promptly if the CONTRACTING PARTIES disapprove.

7. A system for the stabilization of the domestic price or of the return to domestic producers of a primary commodity, independently of the movements of export prices, which results at times in the sale of the commodity for export at a price lower than the comparable price charged for the like commodity to buyers in the domestic market, shall be presumed not to result in material injury within the meaning of paragraph 6 if it is determined by consultation among the contracting parties substantially interested in the commodity concerned that:

- (a) the system has also resulted in the sale of the commodity for export at a price higher than the comparable price charged for the like commodity to buyers in the domestic market, and
- (b) the system is so operated, either because of the effective regulation of production, or otherwise, as not to stimulate exports unduly or otherwise seriously prejudice the interests of other contracting parties.

Article VII: Valuation for Customs Purposes

1. The contracting parties recognize the validity of the general principles of valuation set forth in the following paragraphs of this Article, and they undertake to give effect to such principles, in respect of all products subject to duties or other charges* or restrictions on importation and exportation based upon or regulated in any manner by value. Moreover, they shall, upon a request by another contracting party review the operation of any of their laws or regulations relating to value for customs purposes in the light of these principles. The CONTRACTING PARTIES may request from contracting parties reports on steps taken by them in pursuance of the provisions of this Article.

2. (a) The value for customs purposes of imported merchandise should be based on the actual value of the imported merchandise on which duty is assessed, or of like merchandise, and should not be based on the value of merchandise of national origin or on arbitrary or fictitious values.*

(b) "Actual value" should be the price at which, at a time and place determined by the legislation of the country of importation, such or like merchandise is sold or offered for sale in the ordinary course of trade under fully competitive conditions. To the extent to which the price of such

or like merchandise is governed by the quantity in a particular transaction, the price to be considered should uniformly be related to either (i) comparable quantities, or (ii) quantities not less favourable to importers than those in which the greater volume of the merchandise is sold in the trade between the countries of exportation and importation.*

(c) When the actual value is not ascertainable in accordance with sub-paragraph (b) of this paragraph, the value for customs purposes should be based on the nearest ascertainable equivalent of such value.*

3. The value for customs purposes of any imported product should not include the amount of any internal tax, applicable within the country of origin or export, from which the imported product has been exempted or has been or will be relieved by means of refund.

4. (a) Except as otherwise provided for in this paragraph, where it is necessary for the purposes of paragraph 2 of this Article for a contracting party to convert into its own currency a price expressed in the currency of another country, the conversion rate of exchange to be used shall be based, for each currency involved, on the par value as established pursuant to the Articles of Agreement of the International Monetary Fund or on the rate of exchange recognized by the Fund, or on the par value established in accordance with a special exchange agreement entered into pursuant to Article XV of this Agreement.

(b) Where no such established par value and no such recognized rate of exchange exist, the conversion rate shall reflect effectively the current value of such currency in commercial transactions.

(c) The CONTRACTING PARTIES, in agreement with the International Monetary Fund, shall formulate rules governing the conversion by contracting parties of any foreign currency in respect of which multiple rates of exchange are maintained consistently with the Articles of Agreement of the International Monetary Fund. Any contracting party may apply such rules in respect of such foreign currencies for the purposes of paragraph 2 of this Article as an alternative to the use of par values. Until such rules are adopted by the CONTRACTING PARTIES, any contracting party may employ, in respect of any such foreign currency, rules of conversion for the purposes of paragraph 2 of this Article which are designed to reflect effectively the value of such foreign currency in commercial transactions.

(d) Nothing in this paragraph shall be construed to require any contracting party to alter the method of converting currencies for customs purposes which is applicable in its territory on the date of this Agreement, if such alteration would have the effect of increasing generally the amounts of duty payable.

5. The bases and methods for determining the value of products subject to duties or other charges or restrictions based upon or regulated in any manner by value should be stable and should be given sufficient publicity to enable traders to estimate, with a reasonable degree of certainty, the value for customs purposes.

*Article VIII: Fees and Formalities connected with Importation and Exportation**

1. (a) All fees and charges of whatever character (other than import and export duties and other than taxes within the purview of Article III) imposed by contracting parties on or in connection with importation or exportation shall be limited in amount to the approximate cost of services rendered and shall not represent an indirect protection to domestic products or a taxation of imports or exports for fiscal purposes.

(b) The contracting parties recognize the need for reducing the number and diversity of

fees and charges referred to in sub-paragraph (a).

(c) The contracting parties also recognize the need for minimizing the incidence and complexity of import and export formalities and for decreasing and simplifying import and export documentation requirements.*

2. A contracting party shall, upon request by another contracting party or by the CONTRACTING PARTIES, review the operation of its laws and regulations in the light of the provisions of this Article.

3. No contracting party shall impose substantial penalties for minor breaches of customs regulations or procedural requirements. In particular, no penalty in respect of any omission or mistake in customs documentation which is easily rectifiable and obviously made without fraudulent intent or gross negligence shall be greater than necessary to serve merely as a warning.

4. The provisions of this Article shall extend to fees, charges, formalities and requirements imposed by governmental authorities in connection with importation and exportation, including those relating to:

- (a) consular transactions, such as consular invoices and certificates;
- (b) quantitative restrictions;
- (c) licensing;
- (d) exchange control;
- (e) statistical services;
- (f) documents, documentation and certification;
- (g) analysis and inspection; and
- (h) quarantine, sanitation and fumigation.

Article IX: Marks of Origin

1. Each contracting party shall accord to the products of the territories of other contracting parties treatment with regard to marking requirements no less favourable than the treatment accorded to like products of any third country.

2. The contracting parties recognize that, in adopting and enforcing laws and regulations relating to marks of origin, the difficulties and inconveniences which such measures may cause to the commerce and industry of exporting countries should be reduced to a minimum, due regard being had to the necessity of protecting consumers against fraudulent or misleading indications.

3. Whenever it is administratively practicable to do so, contracting parties should permit required marks of origin to be affixed at the time of importation.

4. The laws and regulations of contracting parties relating to the marking of imported products shall be such as to permit compliance without seriously damaging the products, or materially reducing their value, or unreasonably increasing their cost.

5. As a general rule, no special duty or penalty should be imposed by any contracting party for failure to comply with marking requirements prior to importation unless corrective marking is unreasonably delayed or deceptive marks have been affixed or the required marking has been intentionally omitted.

6. The contracting parties shall co-operate with each other with a view to preventing the use of trade names in such manner as to misrepresent the true origin of a product, to the detriment of such distinctive regional or geographical names of products of the territory of a contracting party as

are protected by its legislation. Each contracting party shall accord full and sympathetic consideration to such requests or representations as may be made by any other contracting party regarding the application of the undertaking set forth in the preceding sentence to names of products which have been communicated to it by the other contracting party.

Article X: Publication and Administration of Trade Regulations

1. Laws, regulations, judicial decisions and administrative rulings of general application, made effective by any contracting party, pertaining to the classification or the valuation of products for customs purposes, or to rates of duty, taxes or other charges, or to requirements, restrictions or prohibitions on imports or exports or on the transfer of payments therefor, or affecting their sale, distribution, transportation, insurance, warehousing, inspection, exhibition, processing, mixing or other use, shall be published promptly in such a manner as to enable governments and traders to become acquainted with them. Agreements affecting international trade policy which are in force between the government or a governmental agency of any contracting party and the government or governmental agency of any other contracting party shall also be published. The provisions of this paragraph shall not require any contracting party to disclose confidential information which would impede law enforcement or otherwise be contrary to the public interest or would prejudice the legitimate commercial interests of particular enterprises, public or private.

2. No measure of general application taken by any contracting party effecting an advance in a rate of duty or other charge on imports under an established and uniform practice, or imposing a new or more burdensome requirement, restriction or prohibition on imports, or on the transfer of payments therefor, shall be enforced before such measure has been officially published.

3. (a) Each contracting party shall administer in a uniform, impartial and reasonable manner all its laws, regulations, decisions and rulings of the kind described in paragraph 1 of this Article.

(b) Each contracting party shall maintain, or institute as soon as practicable, judicial, arbitral or administrative tribunals or procedures for the purpose, *inter alia*, of the prompt review and correction of administrative action relating to customs matters. Such tribunals or procedures shall be independent of the agencies entrusted with administrative enforcement and their decisions shall be implemented by, and shall govern the practice of, such agencies unless an appeal is lodged with a court or tribunal of superior jurisdiction within the time prescribed for appeals to be lodged by importers; *Provided* that the central administration of such agency may take steps to obtain a review of the matter in another proceeding if there is good cause to believe that the decision is inconsistent with established principles of law or the actual facts.

(c) The provisions of sub-paragraph (b) of this paragraph shall not require the elimination or substitution of procedures in force in the territory of a contracting party on the date of this Agreement which in fact provide for an objective and impartial review of administrative action even though such procedures are not fully or formally independent of the agencies entrusted with administrative enforcement. Any contracting party employing such procedures shall, upon request, furnish the CONTRACTING PARTIES with full information thereon in order that they may determine whether such procedures conform to the requirements of this sub-paragraph.

Article XI: General Elimination of Quantitative Restrictions*

1. No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences or other measures, shall be instituted or maintained by any contracting party on the importation of any product of the territory of any other contracting party or on the exportation or sale for export of any product destined for the territory of any other contracting party.

2. The provisions of paragraph 1 of this Article shall not extend to the following:

- (a) Export prohibitions or restrictions temporarily applied to prevent or relieve critical shortages of foodstuffs or other products essential to the exporting contracting party;
- (b) Import and export prohibitions or restrictions necessary to the application of standards or regulations for the classification, grading or marketing of commodities in international trade;
- (c) Import restrictions on any agricultural or fisheries product, imported in any form,* necessary to the enforcement of governmental measures which operate:
 - (i) to restrict the quantities of the like domestic product permitted to be marketed or produced, or, if there is no substantial domestic production of the like product, of a domestic product for which the imported product for which the imported product can be directly substituted; or
 - (ii) to remove a temporary surplus of the like domestic product, or, if there is no substantial domestic production of the like product, of a domestic product for which the imported product can be directly substituted, by making the surplus available to certain groups of domestic consumers free of charge or at prices below the current market level; or
 - (iii) to restrict the quantities permitted to be produced of any animal product the production of which is directly dependent, wholly or mainly, on the imported commodity, if the domestic production of that commodity is relatively negligible.

Any contracting party applying restrictions on the importation of any product pursuant to sub-paragraph (c) of this paragraph shall give public notice of the total quantity or value of the product permitted to be imported during a specified future period and of any change in such quantity or value. Moreover, any restrictions applied under (i) above shall not be such as will reduce the total of imports relative to the total of domestic production, as compared with the proportion which might reasonably be expected to rule between the two in the absence of restrictions. In determining this proportion, the contracting party shall pay due regard to the proportion prevailing during a previous representative period and to any special factors* which may have affected or may be affecting the trade in the product concerned.

Article XII: Restrictions to Safeguard the Balance of Payments*

1. Notwithstanding the provisions of paragraph 1 of Article XI, any contracting party, in order to safeguard its external financial position and its balance of payments, may restrict the quantity or value of merchandise permitted to be imported, subject to the provisions of the following paragraphs of this Article.

2. (a) Import restrictions instituted, maintained or intensified by a contracting party under this Article shall not exceed those necessary:

- (i) to forestall the imminent threat of, or to stop, a serious decline in its monetary reserves, or
- (ii) in the case of a contracting party with very low monetary reserves, to achieve a reasonable rate of increase in its reserves.

Due regard shall be paid in either case to any special factors which may be affecting the reserves of such contracting party or its need for reserves, including, where special external credits or other

resources are available to it, the need to provide for the appropriate use of such credits or resources.

(b) Contracting parties applying restrictions under sub-paragraph (a) of this paragraph shall progressively relax them as such conditions improve, maintaining them only to the extent that the conditions specified in that sub-paragraph still justify their application. They shall eliminate the restrictions when conditions would no longer justify their institution or maintenance under that sub-paragraph.

3. (a) Contracting parties undertake, in carrying out their domestic policies, to pay due regard to the need for maintaining or restoring equilibrium in their balance of payments on a sound and lasting basis and to the desirability of avoiding an uneconomic employment of productive resources. They recognize that, in order to achieve these ends, it is desirable so far as possible to adopt measures which expand rather than contract international trade.

(b) Contracting parties applying restrictions under this Article may determine the incidence of the restrictions on imports of different products or classes of products in such a way as to give priority to the importation of those products which are more essential.

(c) Contracting parties applying restrictions under this Article undertake:

(i) to avoid unnecessary damage to the commercial or economic interests of any other contracting party;*

(ii) not to apply restrictions so as to prevent unreasonably the importation of any description of goods in minimum commercial quantities the exclusion of which would impair regular channels of trade; and

(iii) not to apply restrictions which would prevent the importations of commercial samples or prevent compliance with patent, trade mark, copyright, or similar procedures.

(d) The contracting parties recognize that, as a result of domestic policies directed towards the achievement and maintenance of full and productive employment or towards the development of economic resources, a contracting party may experience a high level of demand for imports involving a threat to its monetary reserves of the sort referred to in paragraph 2 (a) of this Article. Accordingly, a contracting party otherwise complying with the provisions of this Article shall not be required to withdraw or modify restrictions on the ground that a change in those policies would render unnecessary restrictions which it is applying under this Article.

4. (a) Any contracting party applying new restrictions or raising the general level of its existing restrictions by a substantial intensification of the measures applied under this Article shall immediately after instituting or intensifying such restrictions (or, in circumstances in which prior consultation is practicable, before doing so) consult with the CONTRACTING PARTIES as to the nature of its balance of payments difficulties, alternative corrective measures which may be available, and the possible effect of the restrictions on the economies of other contracting parties.

(b) On a date to be determined by them,* the CONTRACTING PARTIES shall review all restrictions still applied under this Article on that date. Beginning one year after that date, contracting parties applying import restrictions under this Article shall enter into consultations of the type provided for in sub-paragraph (c) of this paragraph with the CONTRACTING PARTIES annually.

(c) (i) If, in the course of consultations with a contracting party under sub-paragraph (a) or (b) above, the CONTRACTING PARTIES find that the restrictions are not consistent with provisions of this Article or with those of Article XIII (subject to the provisions of Article XIV), they shall

indicate the nature of the inconsistency and may advise that the restrictions be suitably modified.

(ii) If, however, as a result of the consultations, the CONTRACTING PARTIES determine that the restrictions are being applied in a manner involving an inconsistency of a serious nature with the provisions of this Article or with those of Article XIII (subject to the provisions of Article XIV) and that damage to the trade of any contracting party is caused or threatened thereby, they shall so inform the contracting party applying the restrictions and shall make appropriate recommendations for securing conformity with such provisions within the specified period of time. If such contracting party does not comply with these recommendations within the specified period, the CONTRACTING PARTIES may release any contracting party the trade of which is adversely affected by the restrictions from such obligations under this Agreement towards the contracting party applying the restrictions as they determine to be appropriate in the circumstances.

(d) The CONTRACTING PARTIES shall invite any contracting party which is applying restrictions under this Article to enter into consultations with them at the request of any contracting party which can establish a *prima facie* case that the restrictions are inconsistent with the provisions of this Article or with those of Article XIII (subject to the provisions of Article XIV) and that its trade is adversely affected thereby. However, no such invitation shall be issued unless the CONTRACTING PARTIES have ascertained that direct discussions between the contracting parties concerned have not been successful. If, as a result of the consultations with the CONTRACTING PARTIES, no agreement is reached and they determine that the restrictions are being applied inconsistently with such provisions, and that damage to the trade of the contracting party initiating the procedure is caused or threatened thereby, they shall recommend the withdrawal or modification of the restrictions. If the restrictions are not withdrawn or modified within such time as the CONTRACTING PARTIES may prescribe, they may release the contracting party initiating the procedure from such obligations under this Agreement towards the contracting party applying the restrictions as they determine to be appropriate in the circumstances.

(e) In proceeding under this paragraph, the CONTRACTING PARTIES shall have due regard to any special external factors adversely affecting the export trade of the contracting party applying the restrictions.*

(f) Determinations under this paragraph shall be rendered expeditiously and, if possible, within sixty days of the initiation of the consultations.

5. If there is a persistent and widespread application of import restrictions under this Article, indicating the existence of a general disequilibrium which is restricting international trade, the CONTRACTING PARTIES shall initiate discussions to consider whether other measures might be taken, either by those contracting parties the balance of payments of which are under pressure or by those the balance of payments of which are tending to be exceptionally favourable, or by any appropriate intergovernmental organization, to remove the underlying causes of the disequilibrium. On the invitation of the CONTRACTING PARTIES, contracting parties shall participate in such discussions.

Article XIII*: Non-discriminatory Administration of Quantitative Restrictions

1. No prohibition or restriction shall be applied by any contracting party on the importation of any product of the territory of any other contracting party or on the exportation of any product destined for the territory of any other contracting party, unless the importation of the like product of all third countries or the exportation of the like product to all third countries is similarly prohibited or restricted.

2. In applying import restrictions to any product, contracting parties shall aim at a distribution of trade in such product approaching as closely as possible the shares which the various contracting

parties might be expected to obtain in the absence of such restrictions and to this end shall observe the following provisions:

- (d) Wherever practicable, quotas representing the total amount of permitted imports (whether allocated among supplying countries or not) shall be fixed, and notice given of their amount in accordance with paragraph 3 (b) of this Article;
- (h) In cases in which quotas are not practicable, the restrictions may be applied by means of import licences or permits without a quota;
- (c) Contracting parties shall not, except for purposes of operating quotas allocated in accordance with sub-paragraph (d) of this paragraph, require that import licences or permits be utilized for the importation of the product concerned from a particular country or source;
- (d) In cases in which a quota is allocated among supplying countries the contracting party applying the restrictions may seek agreement with respect to the allocation of shares in the quota with all other contracting parties having a substantial interest in supplying the product concerned. In cases in which this method is not reasonably practicable, the contracting party concerned shall allot to contracting parties having a substantial interest in supplying the product shares based upon the proportions, supplied by such contracting parties during a previous representative period, of the total quantity or value of imports of the product, due account being taken of any special factors which may have affected or may be affecting the trade in the product. No conditions or formalities shall be imposed which would prevent any contracting party from utilizing fully the share of any such total quantity or value which has been allotted to it, subject to importation being made within any prescribed period to which the quota may relate.*

3. (a) In cases in which import licences are issued in connection with import restrictions, the contracting party applying the restrictions shall provide, upon the request of any contracting party having an interest in the trade in the product concerned, all relevant information concerning the administration of the restrictions, the import licences granted over a recent period and the distribution of such licences among supplying countries; *Provided* that there shall be no obligation to supply information as to the names of importing or supplying enterprises.

(b) In the case of import restrictions involving the fixing of quotas, the contracting party applying the restrictions shall give public notice of the total quantity or value of the product or products which will be permitted to be imported during a specified future period and of any change in such quantity or value. Any supplies of the product in question which were *en route* at the time at which public notice was given shall not be excluded from entry; *Provided* that they may be counted so far as practicable, against the quantity permitted to be imported in the period in question, and also, where necessary, against the quantities permitted to be imported in the next following period or periods; and *Provided* further that if any contracting party customarily exempts from such restrictions products entered for consumption or withdrawn from warehouse for consumption during a period of thirty days after the day of such public notice, such practice shall be considered full compliance with this sub-paragraph.

(c) In the case of quotas allocated among supplying countries, the contracting party applying the restrictions shall promptly inform all other contracting parties having an interest in supplying the product concerned of the shares in the quota currently allocated, by quantity or value, to the various supplying countries and shall give public notice thereof.

4. With regard to restrictions applied in accordance with paragraph 2 (d) of this Article or under paragraph 2 (c) of Article XI, the selection of a representative period for any product and the appraisal of any special factors* affecting the trade in the product shall be made initially by the

contracting party applying the restriction; *Provided* that such contracting party shall, upon the request of any other contracting party having a substantial interest in supplying that product or upon the request of the CONTRACTING PARTIES, consult promptly with the other contracting party or the CONTRACTING PARTIES regarding the need for an adjustment of the proportion determined or of the base period selected, or for the reappraisal of the special factors involved, or for the elimination of conditions, formalities or any other provisions established unilaterally relating to the allocation of an adequate quota or its unrestricted utilization.

5. The provisions of this Article shall apply to any tariff quota instituted or maintained by any contracting party, and, in so far as applicable, the principles of this Article shall also extend to export restrictions.

Article XIV^a: Exceptions to the Rule of Non-discrimination*

1. A contracting party which applies restrictions under Article XII or under Section B of Article XVIII may, in the application of such restrictions, deviate from the provisions of Article XIII in a manner having equivalent effect to restrictions on payments and transfers for current international transactions which that contracting party may at that time apply under Article VIII or XIV of the Articles of Agreement of the International Monetary Fund, or under analogous provisions of a special exchange agreement entered into pursuant to paragraph 6 of Article XV.*

2. A contracting party which is applying import restrictions under Article XII or under Section B of Article XVIII may, with the consent of the CONTRACTING PARTIES, temporarily deviate from the provisions of Article XIII in respect of a small part of its external trade where the benefits to the contracting party or contracting parties concerned substantially outweigh any injury which may result to the trade of other contracting parties.*

3. The provisions of Article XIII shall not preclude a group of territories having a common quota in the International Monetary Fund from applying against imports from other countries, but not among themselves, restrictions in accordance with the provisions of Article XII or of Section B of Article XVIII on condition that such restrictions are in all other respects consistent with the provisions of Article XIII.

4. A contracting party applying import restrictions under Article XII or under Section B of Article XVIII shall not be precluded by Articles XI to XV or Section B of Article XVIII of this Agreement from applying measures to direct its exports in such a manner as to increase its earnings of currencies which it can use without deviation from the provisions of Article XIII.

5. A contracting party shall not be precluded by Articles XI to XV, inclusive, or by Section B of Article XVIII, of this Agreement from applying quantitative restrictions:

- (a) having equivalent effect to exchange restrictions authorized under Section 3 (b) of Article VII of the Articles of Agreement of the International Monetary Fund, or
- (b) under the preferential arrangements provided for in Annex A of this Agreement, pending the outcome of the negotiations referred to therein.

Article XV: Exchange Arrangements

1. The CONTRACTING PARTIES shall seek co-operation with the International Monetary Fund to the end that the CONTRACTING PARTIES and the Fund may pursue a co-ordinated policy with regard to exchange questions within the jurisdiction of the Fund and questions of quantitative restrictions and other trade measures within the jurisdiction of the CONTRACTING PARTIES.

2. In all cases in which the CONTRACTING PARTIES are called upon to consider or deal with problems concerning monetary reserves, balances of payments or foreign exchange arrangements, they shall consult fully with the International Monetary Fund. In such consultations, the CONTRACTING PARTIES shall accept all findings of statistical and other facts presented by the Fund relating to foreign exchange, monetary reserves and balances of payments, and shall accept the determination of the Fund as to whether action by a contracting party in exchange matters is in accordance with the Articles of Agreement of the International Monetary Fund, or with the terms of a special exchange agreement between that contracting party and the CONTRACTING PARTIES. The CONTRACTING PARTIES in reaching their final decision in cases involving the criteria set forth in paragraph 2 (a) of Article XII or in paragraph 9 of Article XVIII, shall accept the determination of the Fund as to what constitutes a serious decline in the contracting party's monetary reserves, a very low level of its monetary reserves or a reasonable rate of increase in its monetary reserves, and as to the financial aspects of other matters covered in consultation in such cases.

3. The CONTRACTING PARTIES shall seek agreement with the Fund regarding procedures for consultation under paragraph 2 of this Article.

4. Contracting parties shall not, by exchange action, frustrate* the intent of the provisions of this Agreement, nor, by trade action, the intent of the provisions of the Articles of Agreement of the International Monetary Fund.

5. If the CONTRACTING PARTIES consider, at any time, that exchange restrictions on payments and transfers in connection with imports are being applied by a contracting party in a manner inconsistent with the exceptions provided for in this Agreement for quantitative restrictions, they shall report thereon to the Fund.

6. Any contracting party which is not a member of the Fund shall, within a time to be determined by the CONTRACTING PARTIES after consultation with the Fund, become a member of the Fund, or, failing that, enter into a special exchange agreement with the CONTRACTING PARTIES. A contracting party which ceases to be a member of the Fund shall forthwith enter into a special exchange agreement with the CONTRACTING PARTIES. Any special exchange agreement entered into by a contracting party under this paragraph shall thereupon become part of its obligations under this Agreement.

7. (a) A special exchange agreement between a contracting party and the CONTRACTING PARTIES under paragraph 6 of this Article shall provide to the satisfaction of the CONTRACTING PARTIES that the objectives of this Agreement will not be frustrated as a result of action in exchange matters by the contracting party in question.

(b) The terms of any such agreement shall not impose obligations on the contracting party in exchange matters generally more restrictive than those imposed by the Articles of Agreement of the International Monetary Fund on members of the Fund.

8. A contracting party which is not a member of the Fund shall furnish such information within the general scope of section 5 of Article VIII of the Articles of Agreement of the International Monetary Fund as the CONTRACTING PARTIES may require in order to carry out their functions under this Agreement.

9. Nothing in this Agreement shall preclude:

(a) the use by a contracting party of exchange controls or exchange restrictions in accordance with the Articles of Agreement of the International Monetary Fund or with that contracting party's special exchange agreement with the CONTRACTING PARTIES, or

(b) the use by a contracting party of restrictions or controls in imports or exports, the sole effect of which, additional to the effects permitted under Articles XI, XII, XIII and XIV, is to make effective such exchange controls or exchange restrictions.

*Article XVI**: Subsidies

Section A - Subsidies in General

1. If any contracting party grants or maintains any subsidy, including any form of income or price support, which operates directly or indirectly to increase exports of any product from, or to reduce imports of any product into, its territory, it shall notify the CONTRACTING PARTIES in writing of the extent and nature of the subsidization, of the estimated effect of the subsidization on the quantity of the affected product or products imported into or exported from its territory and of the circumstances making the subsidization necessary. In any case in which it is determined that serious prejudice to the interests of any other contracting party is caused or threatened by any such subsidization, the contracting party granting the subsidy shall, upon request, discuss with the other contracting party or parties concerned, or with the CONTRACTING PARTIES, the possibility of limiting the subsidization.

Section B - Additional Provisions on Export Subsidies*

2. The contracting parties recognize that the granting by a contracting party of a subsidy on the export of any product may have harmful effects for other contracting parties, both importing and exporting, may cause undue disturbance to their normal commercial interests, and may hinder the achievement of the objectives of this Agreement.

3. Accordingly, contracting parties should seek to avoid the use of subsidies on the export of primary products. If, however, a contracting party grants directly or indirectly any form of subsidy which operates to increase the export of any primary product from its territory, such subsidy shall not be applied in a manner which results in that contracting party having more than an equitable share of world export trade in that product, account being taken of the shares of the contracting parties in such trade in the product during a previous representative period, and any special factors which may have affected or may be affecting such trade in the product.*

4. Further, as from 1 January 1958 or the earliest practicable date thereafter, contracting parties shall cease to grant either directly or indirectly any form of subsidy on the export of any product other than a primary product which subsidy results in the sale of such product for export at a price lower than the comparable price charged for the like product to buyers in the domestic market. Until 31 December 1957 no contracting party shall extend the scope of any such subsidization beyond that existing on 1 January 1955 by the introduction of new, or the extension of existing, subsidies.*

5. The CONTRACTING PARTIES shall review the operation of the provisions of this Article from time to time with a view to examining its effectiveness, in the light of actual experience, in promoting the objectives of this Agreement and avoiding subsidization seriously prejudicial to the trade or interests of contracting parties.

Article XVII: State Trading Enterprises

1. (a) Each contracting party undertakes that if it establishes or maintains a State enterprise, wherever located, or grants to any enterprise, formally or in effect, exclusive or special privileges,* such enterprise shall, in its purchases or sales involving either imports or exports, act in a manner consistent with the general principles of non-discriminatory treatment prescribed in this Agreement for governmental measures affecting imports or exports by private traders.

(b) The provisions of sub-paragraph (a) of this paragraph shall be understood to require that such enterprises shall, having due regard to the other provisions of this Agreement, make any such purchases or sales solely in accordance with commercial considerations,* including price, quality, availability, marketability, transportation and other conditions of purchase or sale, and shall afford the enterprises of the other contracting parties adequate opportunity, in accordance with customary business practice, to compete for participation in such purchases or sales.

(c) No contracting party shall prevent any enterprise (whether or not an enterprise described in sub-paragraph (a) of this paragraph) under its jurisdiction from acting in accordance with the principles of sub-paragraphs (a) and (b) of this paragraph.

2. The provisions of paragraph 1 of this Article shall not apply to imports of products for immediate or ultimate consumption in governmental use and not otherwise for resale or use in the production of goods* for sale. With respect to such imports, each contracting party shall accord to the trade of the other contracting parties fair and equitable treatment.

3. The contracting parties recognize that enterprises of the kind described in paragraph 1 (a) of this Article might be operated so as to create serious obstacles to trade; thus negotiations on a reciprocal and mutually advantageous basis designed to limit or reduce such obstacles are of importance to the expansion of international trade.*

4. (a) Contracting parties shall notify the CONTRACTING PARTIES of the products which are imported into or exported from their territories by enterprises of the kind described in paragraph 1 (a) of this Article.

(b) A contracting party establishing, maintaining or authorizing an import monopoly of a product, which is not the subject of a concession under Article II, shall, on the request of another contracting party having a substantial trade in the product concerned, inform the CONTRACTING PARTIES of the import mark-up* on the product during a recent representative period, or, when it is not possible to do so, of the price charged on the resale of the product.

(c) The CONTRACTING PARTIES may, at the request of a contracting party which has reason to believe that its interest under this Agreement are being adversely affected by the operations of an enterprise of the kind described in paragraph 1 (a), request the contracting party establishing, maintaining or authorizing such enterprise to supply information about its operations related to the carrying out of the provisions of this Agreement.

(d) The provisions of this paragraph shall not require any contracting party to disclose confidential information which would impede law enforcement or otherwise be contrary to the public interest or would prejudice the legitimate commercial interests of particular enterprises.

Article XVIII: Governmental Assistance to Economic Development*

1. The contracting parties recognize that the attainment of the objectives of this Agreement will be facilitated by the progressive development of their economies, particularly of those contracting parties the economies of which can only support low standards of living* and are in the early stages of development.*

2. The contracting parties recognize further that it may be necessary for those contracting parties, in order to implement programmes and policies of economic development designed to raise the general standard of living of their people, to take protective or other measures affecting imports, and that such measures are justified in so far as they facilitate the attainment of the objectives of this Agreement. They agree, therefore, that those contracting parties should enjoy additional facilities to

enable them (a) to maintain sufficient flexibility in their tariff structure to be able to grant the tariff protection required for the establishment of a particular industry* and (b) to apply quantitative restrictions for balance of payments purposes in a manner which takes full account of the continued high level of demand for imports likely to be generated by their programmes of economic development.

3. The contracting parties recognize finally that, with those additional facilities which are provided for in Sections A and B of this Article, the provisions of this Agreement would normally be sufficient to enable contracting parties to meet the requirements of their economic development. They agree, however, that there may be circumstances where no measure consistent with those provisions is practicable to permit a contracting party in the process of economic development to grant the governmental assistance required to promote the establishment of particular industries* with a view to raising the general standard of living of its people. Special procedures are laid down in Sections C and D of this Article to deal with those cases.

4. (a) Consequently, a contracting party, the economy of which can only support low standards of living* and is in the early stages of development,* shall be free to deviate temporarily from the provisions of the other Articles of this Agreement, as provided in Sections A, B and C of this Article.

(b) A contracting party, the economy of which is in the process of development, but which does not come within the scope of sub-paragraph (a) above, may submit applications to the CONTRACTING PARTIES under Section D of this Article.

5. The contracting parties recognize that the export earnings of contracting parties, the economies of which are of the type described in paragraph 4 (a) and (b) above and which depend on exports of a small number of primary commodities, may be seriously reduced by a decline in the sale of such commodities. Accordingly, when the exports of primary commodities by such a contracting party are seriously affected by measures taken by another contracting party, it may have resort to the consultation provisions of Article XXII of this Agreement.

6. The CONTRACTING PARTIES shall review annually all measures applied pursuant to the provisions of Sections C and D of this Article.

Section A

7. (a) If a contracting party coming within the scope of paragraph 4 (a) of this Article considers it desirable, in order to promote the establishment of a particular industry* with a view to raising the general standard of living of its people, to modify or withdraw a concession included in the appropriate Schedule annexed to this Agreement, it shall notify the CONTRACTING PARTIES to this effect and enter into negotiations with any contracting party with which such concession was initially negotiated, and with any other contracting party determined by the CONTRACTING PARTIES to have a substantial interest therein. If agreement is reached between such contracting parties concerned, they shall be free to modify or withdraw concessions under the appropriate Schedules to this Agreement in order to give effect to such agreement, including any compensatory adjustments involved.

(b) If agreement is not reached within sixty days after the notification provided for in sub-paragraph (a) above, the contracting party which proposes to modify or withdraw the concession may refer the matter to the CONTRACTING PARTIES which shall promptly examine it. If they find that the contracting party which proposes to modify or withdraw the concession has made every effort to reach an agreement and that the compensatory adjustment offered by it is adequate, that contracting party shall be free to modify or withdraw the concession if, at the same time, it gives effect to the compensatory adjustment. If the CONTRACTING PARTIES do not find that the

compensation offered by a contracting party proposing to modify or withdraw the concession is adequate, but find that it has made every reasonable effort to offer adequate compensation, that contracting party shall be free to proceed with such modification or withdrawal. If such action is taken, any other contracting party referred to in sub-paragraph (a) above shall be free to modify or withdraw substantially equivalent concessions initially negotiated with the contracting party which has taken the action.*

Section B

8. The contracting parties recognize that contracting parties coming within the scope of paragraph 4 (a) of this Article tend, when they are in rapid process of development, to experience balance of payments difficulties arising mainly from efforts to expand their internal markets as well as from the instability in their terms of trade.

9. In order to safeguard its external financial position and to ensure a level of reserves adequate for the implementation of its programme of economic development, a contracting party coming within the scope of paragraph 4 (a) of this Article may, subject to the provisions of paragraphs 10 to 12, control the general level of its imports by restricting the quantity or value of merchandise permitted to be imported; *Provided* that the import restrictions instituted, maintained or intensified shall not exceed those necessary:

- (a) to forestall the threat of, or to stop, a serious decline in its monetary reserves, or
- (b) in the case of a contracting party with inadequate monetary reserves, to achieve a reasonable rate of increase in its reserves.

Due regard shall be paid in either case to any special factors which may be affecting the reserves of the contracting party or its need for reserves, including, where special external credits or other resources are available to it, the need to provide for the appropriate use of such credits or resources.

10. In applying these restrictions, the contracting party may determine their incidence on imports of different products or classes of products in such a way as to give priority to the importation of those products which are more essential in the light of its policy of economic development; *Provided* that the restrictions are so applied as to avoid unnecessary damage to the commercial or economic interests of any other contracting party and not to prevent unreasonably the importation of any description of goods in minimum commercial quantities the exclusion of which would impair regular channels of trade; and *Provided* further that the restrictions are not so applied as to prevent the importation of commercial samples or to prevent compliance with patent, trade mark, copyright or similar procedures.

11. In carrying out its domestic policies, the contracting party concerned shall pay due regard to the need for restoring equilibrium in its balance of payments on a sound and lasting basis and to the desirability of assuring an economic employment of productive resources. It shall progressively relax any restrictions applied under this Section as conditions improve, maintaining them only to the extent necessary under the terms of paragraph 9 of this Article and shall eliminate them when conditions no longer justify such maintenance; *Provided* that no contracting party shall be required to withdraw or modify restrictions on the ground that a change in its development policy would render unnecessary the restrictions which it is applying under this Section.*

12. (a) Any contracting party applying new restrictions or raising the general level of its existing restrictions by a substantial intensification of the measures applied under this Section, shall immediately after instituting or intensifying such restrictions (or, in circumstances in which prior consultation is practicable, before doing so) consult with the CONTRACTING PARTIES as to the nature of its balance of payments difficulties, alternative corrective measures which may be available, and

the possible effect of the restrictions on the economies of other contracting parties.

(b) On a date to be determined by them* the CONTRACTING PARTIES shall review all restrictions still applied under this Section on that date. Beginning two years after that date, contracting parties applying restrictions under this Section shall enter into consultations of the type provided for in sub-paragraph (a) above with the CONTRACTING PARTIES at intervals of approximately, but not less than, two years according to a programme to be drawn up each year by the CONTRACTING PARTIES; *Provided* that no consultation under this sub-paragraph shall take place within two years after the conclusion of a consultation of a general nature under any other provision of this paragraph.

(c) (i) If, in the course of consultations with a contracting party under sub-paragraph (a) or (b) of this paragraph, the CONTRACTING PARTIES find that the restrictions are not consistent with the provisions of this Section or with those of Article XIII (subject to the provisions of Article XIV), they shall indicate the nature of the inconsistency and may advise that the restrictions be suitably modified.

(ii) If, however, as a result of the consultations, the CONTRACTING PARTIES determine that the restrictions are being applied in a manner involving an inconsistency of a serious nature with the provisions of this Section or with those of Article XIII (subject to the provisions of Article XIV) and that damage to the trade of any contracting party is caused or threatened thereby, they shall so inform the contracting party applying the restrictions and shall make appropriate recommendations for securing conformity with such provisions within a specified period. If such contracting party does not comply with these recommendations within the specified period, the CONTRACTING PARTIES may release any contracting party the trade of which is adversely affected by the restrictions from such obligations under this Agreement towards the contracting party applying the restrictions as they determine to be appropriate in the circumstances.

(d) The CONTRACTING PARTIES shall invite any contracting party which is applying restrictions under this Section to enter into consultations with them at the request of any contracting party which can establish a *prima facie* case that the restrictions are inconsistent with the provisions of this Section or with those of Article XIII (subject to the provisions of Article XIV) and that its trade is adversely affected thereby. However, no such invitation shall be issued unless the CONTRACTING PARTIES have ascertained that direct discussions between the contracting parties concerned have not been successful. If, as a result of the consultations with the CONTRACTING PARTIES no agreement is reached and they determine that the restrictions are being applied inconsistently with such provisions, and that damage to the trade of the contracting party initiating the procedure is caused or threatened thereby, they shall recommend the withdrawal or modification of the restrictions. If the restrictions are not withdrawn or modified within such time as the CONTRACTING PARTIES may prescribe, they may release the contracting party initiating the procedure from such obligations under this Agreement towards the contracting party applying the restrictions as they determine to be appropriate in the circumstances.

(e) If a contracting party against which action has been taken in accordance with the last sentence of sub-paragraph (c) (ii) or (d) of this paragraph, finds that the release of obligations authorized by the CONTRACTING PARTIES adversely affects the operation of its programme and policy of economic development, it shall be free, not later than sixty days after such action is taken, to give written notice to the Executive Secretary¹ to the CONTRACTING PARTIES of its intention to withdraw from this Agreement and such withdrawal shall take effect on the sixtieth day following the day on which the notice is received by him.

¹ By the Decision of 23 March 1965, the CONTRACTING PARTIES changed the title of the head of the GATT secretariat from "Executive Secretary" to "Director-General".

(f) In proceeding under this paragraph, the CONTRACTING PARTIES shall have due regard to the factors referred to in paragraph 2 of this Article. Determinations under this paragraph shall be rendered expeditiously and, if possible, within sixty days of the initiation of the consultations.

Section C

13. If a contracting party coming within the scope of paragraph 4 (a) of this Article finds that governmental assistance is required to promote the establishment of a particular industry* with a view to raising the general standard of living of its people, but that no measure consistent with the other provisions of this Agreement is practicable to achieve that objective, it may have recourse to the provisions and procedures set out in this Section.*

14. The contracting party concerned shall notify the CONTRACTING PARTIES of the special difficulties which it meets in the achievement of the objective outlined in paragraph 13 of this Article and shall indicate the specific measure affecting imports which it proposes to introduce in order to remedy these difficulties. It shall not introduce that measure before the expiration of the time-limit laid down in paragraph 15 or 17, as the case may be, or if the measure affects imports of a product which is the subject of a concession included in the appropriate Schedule annexed to this Agreement, unless it has secured the concurrence of the CONTRACTING PARTIES in accordance with paragraph 18; *Provided* that, if the industry receiving assistance has already started production, the contracting party may, after informing the CONTRACTING PARTIES, take such measures as may be necessary to prevent, during that period, imports of the product or products concerned from increasing substantially above a normal level.*

15. If, within thirty days of the notification of the measure, the CONTRACTING PARTIES do not request the contracting party concerned to consult with them,* that contracting party shall be free to deviate from the relevant provisions of the other Articles of this Agreement to the extent necessary to apply the proposed measure.

16. If it is requested by the CONTRACTING PARTIES to do so,* the contracting party concerned shall consult with them as to the purpose of the proposed measure, as to alternative measures which may be available under this Agreement, and as to the possible effect of the measure proposed on the commercial and economic interests of other contracting parties. If, as a result of such consultation, the CONTRACTING PARTIES agree that there is no measure consistent with the other provisions of this Agreement which is practicable in order to achieve the objective outlined in paragraph 13 of this Article, and concur* in the proposed measure, the contracting party concerned shall be released from its obligations under the relevant provisions of the other Articles of this Agreement to the extent necessary to apply that measure.

17. If, within ninety days after the date of the notification of the proposed measure under paragraph 14 of this Article, the CONTRACTING PARTIES have not concurred in such measure, the contracting party concerned may introduce the measure proposed after informing the CONTRACTING PARTIES.

18. If the proposed measure affects a product which is the subject of a concession included in the appropriate Schedule annexed to this Agreement, the contracting party concerned shall enter into consultations with any other contracting party with which the concession was initially negotiated, and with any other contracting party determined by the CONTRACTING PARTIES to have a substantial interest therein. The CONTRACTING PARTIES shall concur* in the measure if they agree that there is no measure consistent with the other provisions of this Agreement which is practicable in order to achieve the objective set forth in paragraph 13 of this Article, and if they are satisfied:

(a) that agreement has been reached with such other contracting parties as a result of the consultations referred to above, or

(b) if no such agreement has been reached within sixty days after the notification provided for in paragraph 14 has been received by the CONTRACTING PARTIES, that the contracting party having recourse to this Section has made all reasonable efforts to reach an agreement and that the interests of other contracting parties are adequately safeguarded.*

The contracting party having recourse to this Section shall thereupon be released from its obligations under the relevant provisions of the other Articles of this Agreement to the extent necessary to permit it to apply the measure.

19. If a proposed measure of the type described in paragraph 13 of this Article concerns an industry the establishment of which has in the initial period been facilitated by incidental protection afforded by restrictions imposed by the contracting party concerned for balance of payments purposes under the relevant provisions of this Agreement, that contracting party may resort to the provisions and procedures of this Section; *Provided* that it shall not apply the proposed measure without the concurrence* of the CONTRACTING PARTIES.*

20. Nothing in the preceding paragraphs of this Section shall authorize any deviation from the provisions of Articles I, II and XIII of this Agreement. The provisos to paragraph 10 of this Article shall also be applicable to any restriction under this Section.

21. At any time while a measure is being applied under paragraph 17 of this Article any contracting party substantially affected by it may suspend the application to the trade of the contracting party having recourse to this Section of such substantially equivalent concessions or other obligations under this Agreement the suspension of which the CONTRACTING PARTIES do not disapprove.* *Provided* that sixty days' notice of such suspension is given to the CONTRACTING PARTIES not later than six months after the measure has been introduced or changed substantially to the detriment of the contracting party affected. Any such contracting party shall afford adequate opportunity for consultation in accordance with the provisions of Article XXII of this Agreement.

Section D

22. A contracting party coming within the scope of sub-paragraph 4 (b) of this Article desiring, in the interest of the development of its economy, to introduce a measure of the type described in paragraph 13 of this Article in respect of the establishment of a particular industry* may apply to the CONTRACTING PARTIES for approval of such measure. The CONTRACTING PARTIES shall promptly consult with such contracting party and shall, in making their decision, be guided by the considerations set out in paragraph 16. If the CONTRACTING PARTIES concur* in the proposed measure the contracting party concerned shall be released from its obligations under the relevant provisions of the other Articles of this Agreement to the extent necessary to permit it to apply the measure. If the proposed measure affects a product which is the subject of a concession included in the appropriate Schedule annexed to this Agreement, the provisions of paragraph 18 shall apply.*

23. Any measure applied under this Section shall comply with the provisions of paragraph 20 of this Article.

Article XIX: Emergency Action on Imports of Particular Products

1. (a) If, as a result of unforeseen developments and of the effect of the obligations incurred by a contracting party under this Agreement, including tariff concessions, any product is being imported into the territory of that contracting party in such increased quantities and under such conditions as to cause or threaten serious injury to domestic producers in that territory of like or directly competitive products, the contracting party shall be free, in respect of such product, and to the extent and for such time as may be necessary to prevent or remedy such injury, to suspend the

obligation in whole or in part or to withdraw or modify the concession.

(b) If any product, which is the subject of a concession with respect to a preference, is being imported into the territory of a contracting party in the circumstances set forth in subparagraph (a) of this paragraph, so as to cause or threaten serious injury to domestic producers of like or directly competitive products in the territory of a contracting party which receives or received such preference, the importing contracting party shall be free, if that other contracting party so requests, to suspend the relevant obligation in whole or in part or to withdraw or modify the concession in respect of the product, to the extent and for such time as may be necessary to prevent or remedy such injury.

2. Before any contracting party shall take action pursuant to the provisions of paragraph 1 of this Article, it shall give notice in writing to the CONTRACTING PARTIES as far in advance as may be practicable and shall afford the CONTRACTING PARTIES and those contracting parties having a substantial interest as exporters of the product concerned an opportunity to consult with it in respect of the proposed action. When such notice is given in relation to a concession with respect to a preference, the notice shall name the contracting party which has requested the action. In critical circumstances, where delay would cause damage which it would be difficult to repair, action under paragraph 1 of this Article may be taken provisionally without prior consultation, on the condition that consultation shall be effected immediately after taking such action.

3. (a) If agreement among the interested contracting parties with respect to the action is not reached, the contracting party which proposes to take or continue the action shall, nevertheless, be free to do so, and if such action is taken or continued, the affected contracting parties shall then be free, not later than ninety days after such action is taken, to suspend, upon the expiration of thirty days from the day on which written notice of such suspension is received by the CONTRACTING PARTIES, the application to the trade of the contracting party taking such action, or, in the case envisaged in paragraph 1 (b) of this Article, to the trade of the contracting party requesting such suspension, of such substantially equivalent concessions or other obligations under this Agreement the suspension of which the CONTRACTING PARTIES do not disapprove.

(b) Notwithstanding the provisions of sub-paragraph (a) of this paragraph, where action is taken under paragraph 2 of this Article without prior consultation and causes or threatens serious injury in the territory of a contracting party to the domestic producers of products affected by the action, that contracting party shall, where delay would cause damage difficult to repair, be free to suspend, upon the taking of the action and throughout the period of consultation, such concessions or other obligations as may be necessary to prevent or remedy the injury.

Article XX: General Exceptions

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:

- (a) necessary to protect public morals;
- (b) necessary to protect human, animal or plant life or health;
- (c) relating to the importations or exportations of gold or silver;
- (d) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including those relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the

protection of patents, trade marks and copyrights, and the prevention of deceptive practices;

- (e) relating to the products of prison labour;
- (f) imposed for the protection of national treasures of artistic, historic or archaeological value;
- (g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption;
- (h) undertaken in pursuance of obligations under any intergovernmental commodity agreement which conforms to criteria submitted to the CONTRACTING PARTIES and not disapproved by them or which is itself so submitted and not so disapproved;*
- (i) involving restrictions on exports of domestic materials necessary to ensure essential quantities of such materials to a domestic processing industry during periods when the domestic price of such materials is held below the world price as part of a governmental stabilization plan; *Provided* that such restrictions shall not operate to increase the exports of or the protection afforded to such domestic industry, and shall not depart from the provisions of this Agreement relating to non-discrimination;
- (j) essential to the acquisition or distribution of products in general or local short supply; *Provided* that any such measures shall be consistent with the principle that all contracting parties are entitled to an equitable share of the international supply of such products, and that any such measures, which are inconsistent with the other provisions of the Agreement shall be discontinued as soon as the conditions giving rise to them have ceased to exist. The CONTRACTING PARTIES shall review the need for this sub-paragraph not later than 30 June 1960.

Article XXI: Security Exceptions

Nothing in this Agreement shall be construed

- (a) to require any contracting party to furnish any information the disclosure of which it considers contrary to its essential security interests; or
- (b) to prevent any contracting party from taking any action which it considers necessary for the protection of its essential security interests
 - (i) relating to fissionable materials or the materials from which they are derived;
 - (ii) relating to the traffic in arms, ammunition and implements of war and to such traffic in other goods and materials as is carried on directly or indirectly for the purpose of supplying a military establishment;
 - (iii) taken in time of war or other emergency in international relations; or
- (c) to prevent any contracting party from taking any action in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security.

Article XXII: Consultation

1. Each contracting party shall accord sympathetic consideration to, and shall afford adequate opportunity for consultation regarding, such representations as may be made by another contracting party with respect to any matter affecting the operation of this Agreement.

2. The CONTRACTING PARTIES may, at the request of a contracting party, consult with any contracting party or parties in respect of any matter for which it has not been possible to find a satisfactory solution through consultation under paragraph 1.

Article XXIII: Nullification or Impairment

1. If any contracting party should consider that any benefit accruing to it directly or indirectly under this Agreement is being nullified or impaired or that the attainment of any objective of the Agreement is being impeded as the result of

- (a) the failure of another contracting party to carry out its obligations under this Agreement, or
- (b) the application by another contracting party of any measure, whether or not it conflicts with the provisions of this Agreement, or
- (c) the existence of any other situation,

the contracting party may, with a view to the satisfactory adjustment of the matter, make written representations or proposals to the other contracting party or parties which it considers to be concerned. Any contracting party thus approached shall give sympathetic consideration to the representations or proposals made to it.

2. If no satisfactory adjustment is effected between the contracting parties concerned within a reasonable time, or if the difficulty is of the type described in paragraph 1 (c) of this Article, the matter may be referred to the CONTRACTING PARTIES. The CONTRACTING PARTIES shall promptly investigate any matter so referred to them and shall make appropriate recommendations to the contracting parties which they consider to be concerned, or give a ruling on the matter, as appropriate. The CONTRACTING PARTIES may consult with contracting parties, with the Economic and Social Council of the United Nations and with any appropriate inter-governmental organization in cases where they consider such consultation necessary. If the CONTRACTING PARTIES consider that the circumstances are serious enough to justify such action, they may authorize a contracting party or parties to suspend the application to any other contracting party or parties of such concessions or other obligations under this Agreement as they determine to be appropriate in the circumstances. If the application to any contracting party of any concession or other obligation is in fact suspended, that contracting party shall then be free, not later than sixty days after such action is taken, to give written notice to the Executive Secretary¹ to the CONTRACTING PARTIES of its intention to withdraw from this Agreement and such withdrawal shall take effect upon the sixtieth day following the day on which such notice is received by him.

PART III

Article XXIV: Territorial Application - Frontier Traffic - Customs Unions and Free-trade Areas

1. The provisions of this Agreement shall apply to the metropolitan customs territories of the contracting parties and to any other customs territories in respect of which this Agreement has been accepted under Article XXVI or is being applied under Article XXXIII or pursuant to the Protocol of Provisional Application. Each such customs territory shall, exclusively for the purposes of the territorial application of this Agreement, be treated as though it were a contracting party. *Provided*

¹ By the Decision of 23 March 1965, the CONTRACTING PARTIES changed the title of the head of the GATT secretariat from "Executive Secretary" to "Director-General".

that the provisions of this paragraph shall not be construed to create any rights or obligations as between two or more customs territories in respect of which this Agreement has been accepted under Article XXVI or is being applied under Article XXXIII or pursuant to the Protocol of Provisional Application by a single contracting party.

2. For the purposes of this Agreement a customs territory shall be understood to mean any territory with respect to which separate tariffs or other regulations of commerce are maintained for a substantial part of the trade of such territory with other territories.

3. The provisions of this Agreement shall not be construed to prevent:

- (a) Advantages accorded by any contracting party to adjacent countries in order to facilitate frontier traffic;
- (b) Advantages accorded to the trade with the Free Territory of Trieste by countries contiguous to that territory, provided that such advantages are not in conflict with the Treaties of Peace arising out of the Second World War.

4. The contracting parties recognize the desirability of increasing freedom of trade by the development, through voluntary agreements, of closer integration between the economies of the countries parties to such agreements. They also recognize that the purpose of a customs union or of a free-trade area should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other contracting parties with such territories.

5. Accordingly, the provisions of this Agreement shall not prevent, as between the territories of contracting parties, the formation of a customs union or of a free-trade area or the adoption of an interim agreement necessary for the formation of a customs union or of a free-trade area; *Provided* that:

- (a) with respect to a customs union, or an interim agreement leading to a formation of a customs union, the duties and other regulations of commerce imposed at the institution of any such union or interim agreement in respect of trade with contracting parties not parties to such union or agreement shall not on the whole be higher or more restrictive than the general incidence of the duties and regulations of commerce applicable in the constituent territories prior to the formation of such union or the adoption of such interim agreement, as the case may be;
 - (b) with respect to a free-trade area, or an interim agreement leading to the formation of a free-trade area, the duties and other regulations of commerce maintained in each of the constituent territories and applicable at the formation of such free-trade area or the adoption of such interim agreement to the trade of contracting parties not included in such area or not parties to such agreement shall not be higher or more restrictive than the corresponding duties and other regulations of commerce existing in the same constituent territories prior to the formation of the free-trade area, or interim agreement as the case may be; and
 - (c) any interim agreement referred to in sub-paragraphs (a) and (b) shall include a plan and schedule for the formation of such a customs union or of such a free-trade area within a reasonable length of time.
6. If, in fulfilling the requirements of sub-paragraph 5 (a), a contracting party proposes to increase any rate of duty inconsistently with the provisions of Article II, the procedure set forth in Article XXXIII shall apply. In providing for compensatory adjustment, due account shall be taken of the compensation already afforded by the reduction brought about in the corresponding duty of the other constituents of the union.

7. (a) Any contracting party deciding to enter into a customs union or free-trade area, or an interim agreement leading to the formation of such a union or area, shall promptly notify the CONTRACTING PARTIES and shall make available to them such information regarding the proposed union or area as will enable them to make such reports and recommendations to contracting parties as they may deem appropriate.

(b) If, after having studied the plan and schedule included in an interim agreement referred to in paragraph 5 in consultation with the parties to that agreement and taking due account of the information made available in accordance with the provisions of sub-paragraph (a), the CONTRACTING PARTIES find that such agreement is not likely to result in the formation of a customs union or of a free-trade area within the period contemplated by the parties to the agreement or that such period is not a reasonable one, the CONTRACTING PARTIES shall make recommendations to the parties to the agreement. The parties shall not maintain or put into force, as the case may be, such agreement if they are not prepared to modify it in accordance with these recommendations.

(c) Any substantial change in the plan or schedule referred to in paragraph 5 (c) shall be communicated to the CONTRACTING PARTIES, which may request the contracting parties concerned to consult with them if the change seems likely to jeopardize or delay unduly the formation of the customs union or of the free-trade area.

8. For the purposes of this Agreement:

(a) A customs union shall be understood to mean the substitution of a single customs territory for two or more customs territories, so that

(i) duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated with respect to substantially all the trade between the constituent territories of the union or at least with respect to substantially all the trade in products originating in such territories, and,

(ii) subject to the provisions of paragraph 9, substantially the same duties and other regulations of commerce are applied by each of the members of the union to the trade of territories not included in the union;

(b) A free-trade area shall be understood to mean a group of two or more customs territories in which the duties and other restrictive regulations of commerce (except, where necessary, those permitted under Articles XI, XII, XIII, XIV, XV and XX) are eliminated on substantially all the trade between the constituent territories in products originating in such territories.

9. The preferences referred to in paragraph 2 of Article I shall not be affected by the formation of a customs union or of a free-trade area but may be eliminated or adjusted by means of negotiations with contracting parties affected.* This procedure of negotiations with affected contracting parties shall, in particular, apply to the elimination of preferences required to conform with the provisions of paragraph 8 (a)(i) and paragraph 8 (b).

10. The CONTRACTING PARTIES may by a two-thirds majority approve proposals which do not fully comply with the requirements of paragraphs 5 to 9 inclusive, provided that such proposals lead to the formation of a customs union or a free-trade area in the sense of this Article.

11. Taking into account the exceptional circumstances arising out of the establishment of India and Pakistan as independent States and recognizing the fact that they have long constituted an economic unit, the contracting parties agree that the provisions of this Agreement shall not prevent

the two countries from entering into special arrangements with respect to the trade between them, pending the establishment of their mutual trade relations on a definitive basis.*

12. Each contracting party shall take such reasonable measures as may be available to it to ensure observance of the provisions of this Agreement by the regional and local governments and authorities within its territories.

Article XXV: Joint Action by the Contracting Parties

1. Representatives of the contracting parties shall meet from time to time for the purpose of giving effect to those provisions of this Agreement which involve joint action and, generally, with a view to facilitating the operation and furthering the objectives of this Agreement. Wherever reference is made in this Agreement to the contracting parties acting jointly they are designated as the CONTRACTING PARTIES.

2. The Secretary-General of the United Nations is requested to convene the first meeting of the CONTRACTING PARTIES, which shall take place not later than March 1, 1948.

3. Each contracting party shall be entitled to have one vote at all meetings of the CONTRACTING PARTIES.

4. Except as otherwise provided for in this Agreement, decisions of the CONTRACTING PARTIES shall be taken by a majority of the votes cast.

5. In exceptional circumstances not elsewhere provided for in this Agreement, the CONTRACTING PARTIES may waive an obligation imposed upon a contracting party by this Agreement: *Provided* that any such decision shall be approved by a two-thirds majority of the votes cast and that such majority shall comprise more than half of the contracting parties. The CONTRACTING PARTIES may also by such a vote

- (i) define certain categories of exceptional circumstances to which other voting requirements shall apply for the waiver of obligations, and
- (ii) prescribe such criteria as may be necessary for the application of this paragraph.¹

Article XXVI: Acceptance, Entry into Force and Registration

1. The date of this Agreement shall be 30 October 1947.

2. This Agreement shall be open for acceptance by any contracting party which, on 1 March 1955, was a contracting party or was negotiating with a view to accession to this Agreement.

3. This Agreement, done in a single English original and a single French original, both texts authentic, shall be deposited with the Secretary-General of the United Nations, who shall furnish certified copies thereof to all interested governments.

4. Each government accepting this Agreement shall deposit an instrument of acceptance with the Executive Secretary¹ to the CONTRACTING PARTIES, who will inform all interested governments of the date of deposit of each instrument of acceptance and of the day on which this Agreement enters into force under paragraph 6 of this Article.

¹ The authentic text erroneously reads "sub-paragraph".

5. (a) Each government accepting this Agreement does so in respect of its metropolitan territory and of the other territories for which it has international responsibility, except such separate customs territories as it shall notify to the Executive Secretary¹ to the CONTRACTING PARTIES at the time of its own acceptance.

(b) Any government, which has so notified the Executive Secretary¹ under the exceptions in sub-paragraph (a) of this paragraph, may at any time give notice to the Executive Secretary¹ that its acceptance shall be effective in respect of any separate customs territory or territories so excepted and such notice shall take effect on the thirtieth day following the day on which it is received by the Executive Secretary.¹

(c) If any of the customs territories, in respect of which a contracting party has accepted this Agreement, possesses or acquires full autonomy in the conduct of its external commercial relations and of the other matters provided for in this Agreement, such territory shall, upon sponsorship through a declaration by the responsible contracting party establishing the above-mentioned fact, be deemed to be a contracting party.

6. This Agreement shall enter into force, as among the governments which have accepted it, on the thirtieth day following the day on which instruments of acceptance have been deposited with Executive Secretary¹ to the CONTRACTING PARTIES on behalf of governments named in Annex H, the territories of which account for 85 per centum of the total external trade of the territories of such governments, computed in accordance with the applicable column of percentages set forth therein. The instrument of acceptance of each other government shall take effect on the thirtieth day following the day on which such instrument has been deposited.

7. The United Nations is authorized to effect registration of this Agreement as soon as it enters into force.

Article XXVII: Withholding or Withdrawal of Concessions

Any contracting party shall at any time be free to withhold or to withdraw in whole or in part any concession, provided for in the appropriate Schedule annexed to this Agreement, in respect of which such contracting party determines that it was initially negotiated with a government which has not become, or has ceased to be, a contracting party. A contracting party taking such action shall notify the CONTRACTING PARTIES and, upon request, consult with contracting parties which have a substantial interest in the product concerned.

Article XXVIII: Modification of Schedules*

1. On the first day of each three-year period, the first period beginning on 1 January 1958 (or on the first day of any other period* that may be specified by the CONTRACTING PARTIES by two-thirds of the votes cast) a contracting party (hereafter in this Article referred to as the "applicant contracting party") may, by negotiation and agreement with any contracting party with which such concession was initially negotiated and with any other contracting party determined by the CONTRACTING PARTIES to have a principal supplying interest* (which two preceding categories of CONTRACTING PARTIES, together with the applicant contracting party, are in this Article hereinafter referred to as the "contracting parties primarily concerned"), and subject to consultation with any other contracting party determined by the CONTRACTING PARTIES to have a substantial interest* in such concession, modify or withdraw a concession* included in the appropriate schedule annexed to this Agreement.

¹ By the Decision of 23 March 1965, the CONTRACTING PARTIES changed the title of the head of the GATT secretariat from "Executive Secretary" to "Director-General".

2. In such negotiations and agreement, which may include provision for compensatory adjustment with respect to other products, the contracting parties concerned shall endeavour to maintain a general level of reciprocal and mutually advantageous concessions not less favourable to trade than that provided for in this Agreement prior to such negotiations.

3. (a) If agreement between the contracting parties primarily concerned cannot be reached before 1 January 1958 or before the expiration of a period envisaged in paragraph 1 of this Article, the contracting party which proposes to modify or withdraw the concession shall, nevertheless, be free to do so and if such action is taken any contracting party with which such concession was initially negotiated, any contracting party determined under paragraph 1 to have a principal supplying interest and any contracting party determined under paragraph 1 to have a substantial interest shall then be free not later than six months after such action is taken, to withdraw, upon the expiration of thirty days from the day on which written notice of such withdrawal is received by the CONTRACTING PARTIES, substantially equivalent concessions initially negotiated with the applicant contracting party.

(b) If agreement between the contracting parties primarily concerned is reached but any other contracting party determined under paragraph 1 of this Article to have a substantial interest is not satisfied, such other contracting party shall be free, not later than six months after action under such agreement is taken, to withdraw, upon the expiration of thirty days from the day on which written notice of such withdrawal is received by the CONTRACTING PARTIES, substantially equivalent concessions initially negotiated with the applicant contracting party.

4. The CONTRACTING PARTIES may, at any time, in special circumstances, authorize* a contracting party to enter into negotiations for modification or withdrawal of a concession included in the appropriate Schedule annexed to this Agreement subject to the following procedures and conditions:

(a) Such negotiations* and any related consultations shall be conducted in accordance with the provisions of paragraph 1 and 2 of this Article.

(b) If agreement between the contracting parties primarily concerned is reached in the negotiations, the provisions of paragraph 3 (b) of this Article shall apply.

(c) If agreement between the contracting parties primarily concerned is not reached within a period of sixty days* after negotiations have been authorized, or within such longer period as the CONTRACTING PARTIES may have prescribed, the applicant contracting party may refer the matter to the CONTRACTING PARTIES.

(d) Upon such reference, the CONTRACTING PARTIES shall promptly examine the matter and submit their views to the contracting parties primarily concerned with the aim of achieving a settlement. If a settlement is reached, the provisions of paragraph 3 (b) shall apply as if agreement between the contracting parties primarily concerned had been reached. If no settlement is reached between the contracting parties primarily concerned, the applicant contracting party shall be free to modify or withdraw the concession, unless the CONTRACTING PARTIES determine that the applicant contracting party has unreasonably failed to offer adequate compensation.* If such action is taken, any contracting party with which the concession was initially negotiated, any contracting party determined under paragraph 4 (a) to have a principal supplying interest and any contracting party determined under paragraph 4 (a) to have a substantial interest, shall be free, not later than six months after such action is taken, to modify or withdraw, upon the expiration of thirty days from the day on which written notice of such withdrawal is received by the CONTRACTING PARTIES, substantially equivalent concessions initially negotiated with applicant

contracting party.

5. Before 1 January 1958 and before the end of any period envisaged in paragraph 1 a contracting party may elect by notifying the CONTRACTING PARTIES to reserve the right, for the duration of the next period, to modify the appropriate Schedule in accordance with the procedures of paragraph 1 to 3. If a contracting party so elects, other contracting parties shall have the right, during the same period, to modify or withdraw, in accordance with the same procedures, concessions initially negotiated with that contracting party.

Article XXVIII bis: Tariff Negotiations

1. The contracting parties recognize that customs duties often constitute serious obstacles to trade; thus negotiations on a reciprocal and mutually advantageous basis, directed to the substantial reduction of the general level of tariffs and other charges on imports and exports and in particular to the reduction of such high tariffs as discourage the importation even of minimum quantities, and conducted with due regard to the objectives of this Agreement and the varying needs of individual contracting parties, are of great importance to the expansion of international trade. The CONTRACTING PARTIES may therefore sponsor such negotiations from time to time.

2. (a) Negotiations under this Article may be carried out on a selective product-by-product basis or by the application of such multilateral procedures as may be accepted by the contracting parties concerned. Such negotiations may be directed towards the reduction of duties, the binding of duties at then existing levels or undertakings that individual duties or the average duties on specified categories of products shall not exceed specified levels. The binding against increase of low duties or of duty-free treatment shall, in principle, be recognized as a concession equivalent in value to the reduction of high duties.

(b) The contracting parties recognize that in general the success of multilateral negotiations would depend on the participation of all contracting parties which conduct a substantial proportion of their external trade with one another.

3. Negotiations shall be conducted on a basis which affords adequate opportunity to take into account:

- (a) the needs of individual contracting parties and individual industries;
- (b) the needs of less-developed countries for a more flexible use of tariff protection to assist their economic development and the special needs of these countries to maintain tariffs for revenue purposes; and
- (c) all other relevant circumstances, including the fiscal,* developmental, strategic and other needs of the contracting parties concerned.

Article XXIX: The Relation of this Agreement to the Havana Charter

1. The contracting parties undertake to observe to the fullest extent of their executive authority the general principles of Chapters I to VI inclusive and of Chapter IX of the Havana Charter pending their acceptance of it in accordance with their constitutional procedures.*

2. Part II of this Agreement shall be suspended on the day on which the Havana Charter enters into force.

3. If by September 30, 1949, the Havana Charter has not entered into force, the contracting parties shall meet before December 31, 1949, to agree whether this Agreement shall be amended,

supplemented or maintained.

4. If at any time the Havana Charter should cease to be in force, the CONTRACTING PARTIES shall meet as soon as practicable thereafter to agree whether this Agreement shall be supplemented, amended or maintained. Pending such agreement, Part II of this Agreement shall again enter into force; *Provided* that the provisions of Part II other than Article XXIII shall be replaced, *mutatis mutandis*, in the form in which they then appeared in the Havana Charter; and *Provided* further that no contracting party shall be bound by any provisions which did not bind it at the time when the Havana Charter ceased to be in force.

5. If any contracting party has not accepted the Havana Charter by the date upon which it enters into force, the CONTRACTING PARTIES shall confer to agree whether, and if so in what way, this Agreement in so far as it affects relations between such contracting party and other contracting parties, shall be supplemented or amended. Pending such agreement the provisions of Part II of this Agreement shall, notwithstanding the provisions of paragraph 2 of this Article, continue to apply as between such contracting party and other contracting parties.

6. Contracting parties which are Members of the International Trade Organization shall not invoke the provisions of this Agreement so as to prevent the operation of any provision of the Havana Charter. The application of the principle underlying this paragraph to any contracting party which is not a Member of the International Trade Organization shall be the subject of an agreement pursuant to paragraph 5 of this Article.

Article XXX: Amendments

1. Except where provision for modification is made elsewhere in this Agreement, amendments to the provisions of Part I of this Agreement or the provisions of Article XXIX or of this Article shall become effective upon acceptance by all the contracting parties, and other amendments to this Agreement shall become effective, in respect of those contracting parties which accept them, upon acceptance by two-thirds of the contracting parties and thereafter for each other contracting party upon acceptance by it.

2. Any contracting party accepting an amendment to this Agreement shall deposit an instrument of acceptance with the Secretary-General of the United Nations within such period as the CONTRACTING PARTIES may specify. The CONTRACTING PARTIES may decide that any amendment made effective under this Article is of such a nature that any contracting party which has not accepted it within a period specified by the CONTRACTING PARTIES shall be free to withdraw from this Agreement, or to remain a contracting party with the consent of the CONTRACTING PARTIES.

Article XXXI: Withdrawal

Without prejudice to the provisions of paragraph 12 of Article XVIII, of Article XXIII or of paragraph 2 of Article XXX, any contracting party may withdraw from this Agreement, or may separately withdraw on behalf of any of the separate customs territories for which it has international responsibility and which at the time possesses full autonomy in the conduct of its external commercial relations and of the other matters provided for in this Agreement. The withdrawal shall take effect upon the expiration of six months from the day on which written notice of withdrawal is received by the Secretary-General of the United Nations.

Article XXXII: Contracting Parties

1. The contracting parties to this Agreement shall be understood to mean those governments which are applying the provisions of this Agreement under Articles XXVI or XXXIII or pursuant to the Protocol of Provisional Application.

2. At any time after the entry into force of this Agreement pursuant to paragraph 6 of Article XXVI, those contracting parties which have accepted this Agreement pursuant to paragraph 4 of Article XXVI may decide that any contracting party which has not so accepted it shall cease to be a contracting party.

Article XXXIII: Accession

A government not party to this Agreement, or a government acting on behalf of a separate customs territory possessing full autonomy in the conduct of its external commercial relations and of the other matters provided for in this Agreement, may accede to this Agreement, on its own behalf or on behalf of that territory, on terms to be agreed between such government and the CONTRACTING PARTIES. Decisions of the CONTRACTING PARTIES under this paragraph shall be taken by a two-thirds majority.

Article XXXIV: Annexes

The annexes to this Agreement are hereby made an integral part of this Agreement.

Article XXXV: Non-application of the Agreement between Particular Contracting Parties

1. This Agreement, or alternatively Article II of this Agreement, shall not apply as between any contracting party and any other contracting party if:
 - (a) the two contracting parties have not entered into tariff negotiations with each other, and
 - (b) either of the contracting parties, at the time either becomes a contracting party, does not consent to such application.
2. The CONTRACTING PARTIES may review the operation of this Article in particular cases at the request of any contracting party and make appropriate recommendations.

PART IV*: TRADE AND DEVELOPMENT

Article XXXVI: Principles and Objectives

- 1.* The contracting parties,
 - (a) recalling that the basic objectives of this Agreement include the raising of standards of living and the progressive development of the economies of all contracting parties, and considering that the attainment of these objectives is particularly urgent for less-developed contracting parties;
 - (b) considering that export earnings of the less-developed contracting parties can play a vital part in their economic development and that the extent of this contribution depends on the prices paid by the less-developed contracting parties for essential imports, the volume of their exports, and the prices received for these exports;
 - (c) noting, that there is a wide gap between standards of living in less-developed countries and in other countries;
 - (d) recognizing that individual and joint action is essential to further the development of the

economies of less-developed contracting parties and to bring about a rapid advance in the standards of living in these countries;

- (e) recognizing that international trade as a means of achieving economic and social advancement should be governed by such rules and procedures and measures in conformity with such rules and procedures as are consistent with the objectives set forth in this Article;
- (f) noting that the CONTRACTING PARTIES may enable less-developed contracting parties to use special measures to promote their trade and development;

agree as follows.

 2. There is need for a rapid and sustained expansion of the export earnings of the less-developed contracting parties.
 3. There is need for positive efforts designed to ensure that less-developed contracting parties secure a share in the growth in international trade commensurate with the needs of their economic development.
 4. Given the continued dependence of many less-developed contracting parties on the exportation of a limited range of primary products,* there is need to provide in the largest possible measure more favourable and acceptable conditions of access to world markets for these products, and wherever appropriate to devise measures designed to stabilize and improve conditions of world and markets in these products, including in particular measures designed to attain stable, equitable and remunerative prices, thus permitting an expansion of world trade and demand and a dynamic and steady growth of the real export earnings of these countries so as to provide them with expanding resources for their economic development.
 5. The rapid expansion of the economies of the less-developed contracting parties will be facilitated by a diversification* of the structure of their economies and the avoidance of an excessive dependence on the export of primary products. There is, therefore, need for increased access in the largest possible measure to markets under favourable conditions for processed and manufactured products currently or potentially of particular export interest to less-developed contracting parties.
 6. Because of the chronic deficiency in the export proceeds and other foreign exchange earnings of less-developed contracting parties, there are important inter-relationships between trade and financial assistance to development. There is, therefore, need for close and continuing collaboration between the CONTRACTING PARTIES and the international lending agencies so that they can contribute most effectively to alleviating the burdens these less-developed contracting parties assume in the interest of their economic development.
 7. There is need for appropriate collaboration between the CONTRACTING PARTIES, other intergovernmental bodies and the organs and agencies of the United Nations system, whose activities relate to the trade and economic development of less-developed countries.
 8. The developed contracting parties do not expect reciprocity for commitments made by them in trade negotiations to reduce or remove tariffs and other barriers to the trade of less-developed contracting parties.*
 9. The adoption of measures to give effect to these principles and objectives shall be a matter of conscious and purposeful effort on the part of the contracting parties both individually and jointly.

Article XXXVII: Commitments

1. The developed contracting parties shall to the fullest extent possible _ that is, except when compelling reasons, which may include legal reasons, make it impossible _ give effect to the following provisions:
 - (a) accord high priority to the reduction and elimination of barriers to products currently or potentially of particular export interest to less-developed contracting parties, including customs duties and other restrictions which differentiate unreasonably between such products in their primary and in their processed forms;*
 - (b) refrain from introducing, or increasing the incidence of, customs duties or non-tariff import barriers on products currently or potentially of particular export interest to less-developed contracting parties; and
 - (c) (i) refrain from imposing new fiscal measures, and
 - (ii) in any adjustments of fiscal policy accord high priority to the reduction and elimination of fiscal measures,
 - which would hamper, or which hamper, significantly the growth of consumption of primary products, in raw or processed form, wholly or mainly produced in the territories of less-developed contracting parties, and which are applied specifically to those products.
2. (a) Whenever it is considered that effect is not being given to any of the provisions of sub-paragraph (a), (b) or (c) of paragraph 1, the matter shall be reported to the CONTRACTING PARTIES either by the contracting party not so giving effect to the relevant provisions or by any other interested contracting party.
 - (b) (i) The CONTRACTING PARTIES shall, if requested so to do by any interested contracting party, and without prejudice to any bilateral consultations that may be undertaken, consult with the contracting party concerned and all interested contracting parties with respect to the matter with a view to reaching solutions satisfactory to all contracting parties concerned in order to further the objectives set forth in Article XXXVI. In the course of these consultations, the reasons given in cases where effect was not being given to the provisions of sub-paragraph (a), (b) or (c) of paragraph 1 shall be examined.
 - (ii) As the implementation of the provisions of sub-paragraph (a), (b) or (c) of paragraph 1 by individual contracting parties may in some cases be more readily achieved where action is taken jointly with other developed contracting parties, such consultation might, where appropriate, be directed towards this end.
 - (iii) The consultations by the CONTRACTING PARTIES might also, in appropriate cases, be directed towards agreement on joint action designed to further the objectives of this Agreement as envisaged in paragraph 1 of Article XXV.
3. The developed contracting parties shall:
 - (a) make every effort, in cases where a government directly or indirectly determines the resale price of products wholly or mainly produced in the territories of less-developed contracting parties, to maintain trade margins at equitable levels;
 - (b) give active consideration to the adoption of other measures* designed to provide greater

scope for the development of imports from less-developed contracting parties and collaborate in appropriate international action to this end;

- (c) have special regard to the trade interests of less-developed contracting parties when considering the application of other measures permitted under this Agreement to meet particular problems and explore all possibilities of constructive remedies before applying such measures where they would affect essential interests of those contracting parties.
4. Less-developed contracting parties agree to take appropriate action in implementation of the provisions of Part IV for the benefit of the trade of other less-developed contracting parties, in so far as such action is consistent with their individual present and future development, financial and trade needs taking into account past trade developments as well as the trade interests of less-developed contracting parties as a whole.
5. In the implementation of the commitments set forth in paragraph 1 to 4 each contracting party shall afford to any other interested contracting party or contracting parties full and prompt opportunity for consultations under the normal procedures of this Agreement with respect to any matter or difficulty which may arise.

Article XXXVIII: Joint Action

1. The contracting parties shall collaborate jointly, with the framework of this Agreement and elsewhere, as appropriate, to further the objectives set forth in Article XXXVI.
2. In particular, the CONTRACTING PARTIES shall:
 - (a) where appropriate, take action, including action through international arrangements, to provide improved and acceptable conditions of access to world markets for primary products of particular interest to less-developed contracting parties and to devise measures designed to stabilize and improve conditions of world markets in these products including measures designed to attain stable, equitable and remunerative prices for exports of such products;
 - (b) seek appropriate collaboration in matters of trade and development policy with the United Nations and its organs and agencies, including any institutions that may be created on the basis of recommendations by the United Nations Conference on Trade and Development;
 - (c) collaborate in analysing the development plans and policies of individual less-developed contracting parties and in examining trade and aid relationships with a view to devising concrete measures to promote the development of export potential and to facilitate access to export markets for the products of the industries thus developed and, in this connection, seek appropriate collaboration with governments and international organizations, and in particular with organizations having competence in relation to financial assistance for economic development, in systematic studies of trade and aid relationships in individual less-developed contracting parties aimed at obtaining a clear analysis of export potential, market prospects and any further action that may be required;
 - (d) keep under continuous review the development of world trade with special reference to the rate of growth of the trade of less-developed contracting parties and make such recommendations to contracting parties as may, in the circumstances, be deemed appropriate;
 - (e) collaborate in seeking feasible methods to expand trade for the purpose of economic development, through international harmonization and adjustment of national policies and

regulations, through technical and commercial standards affecting production, transportation and marketing, and through export promotion by the establishment of facilities for the increased flow of trade information and the development of market research; and

- (f) establish such institutional arrangements as may be necessary to further the objectives set forth in Article XXXVI and to give effect to the provision of this Part.

ANNEX A: List of Territories referred to in Paragraph 2 (a) of Article I

United Kingdom of Great Britain and Northern Ireland
 Dependent territories of the United Kingdom of Great Britain and Northern Ireland
 Canada
 Commonwealth of Australia
 Dependent territories of the Commonwealth of Australia
 New Zealand
 Dependent territories of New Zealand
 Union of South Africa including South West Africa
 Ireland
 India (as on April 10, 1947)
 Newfoundland
 Southern Rhodesia
 Burma
 Ceylon

Certain of the territories listed above have two or more preferential rates in force for certain products. Any such territory may, by agreement with the other contracting parties which are principal suppliers of such products at the most-favoured-nation rate, substitute for such preferential rates a single preferential rate which shall not on the whole be less favourable to suppliers at the most-favoured-nation rate than the preferences in force prior to such substitution.

The imposition of an equivalent margin of tariff preference to replace a margin of preference in an internal tax existing on April 10, 1947 exclusively between two or more of the territories listed in this Annex or to replace the preferential quantitative arrangements described in the following paragraph, shall not be deemed to constitute an increase in a margin of tariff preference.

The preferential arrangements referred to in paragraph 5 (b) of Article XIV are those existing in the United Kingdom on 10 April 1947, under contractual agreements with the Governments of Canada, Australia and New Zealand, in respect of chilled and frozen beef and veal, frozen mutton and lamb, chilled and frozen pork and bacon. It is the intention, without prejudice to any action taken under sub-paragraph (b) of Article XX, that these arrangements shall be eliminated or replaced by tariff preferences, and that negotiations to this end shall take place as soon as practicable among the countries substantially concerned or involved.

The film hire tax in force in New Zealand on 10 April 1947, shall, for the purposes of this Agreement, be treated as a customs duty under Article I. The renters' film quota in force in New Zealand on April 10, 1947, shall, for the purposes of this Agreement, be treated as a screen quota under Article IV.

The Dominions of India and Pakistan have not been mentioned separately in the above list since they had not come into existence as such on the base date of April 10, 1947.

ANNEX B: List of Territories of the French Union referred to in Paragraph 2 (b) of Article I

France
 French Equatorial Africa (Treaty Basin of the Congo² and other territories)

¹ The authentic text erroneously reads "part I (b)".

² For imports into Metropolitan France and Territories of the French Union.

French West Africa
 Cameroons under French Trusteeship¹
 French Somali Coast and Dependencies
 French Establishments in Oceania
 French Establishments in the Condominium of the New Hebrides¹
 Indo-China
 Madagascar and Dependencies
 Morocco (French zone)¹
 New Caledonia and Dependencies
 Saint-Pierre and Miquelon
 Togo under French Trusteeship¹
 Tunisia

ANNEX C: List of Territories referred to in Paragraph 2 (b) of Article I as respects the Customs Union of Belgium, Luxembourg and the Netherlands

The Economic Union of Belgium and Luxembourg
 Belgian Congo
 Ruanda Urundi
 Netherlands
 New Guinea
 Surinam
 Netherlands Antilles
 Republic of Indonesia

For imports into the territories constituting the Customs Union only.

ANNEX D: List of Territories referred to in Paragraph 2 (b) of Article I as respects the United States of America

United States of America (customs territory)
 Dependent territories of the United States of America
 Republic of the Philippines

The imposition of an equivalent margin of tariff preference to replace a margin of preference in an internal tax existing on 10 April, 1947, exclusively between two or more of the territories listed in this Annex shall not be deemed to constitute an increase in a margin of tariff preference.

ANNEX E: List of Territories covered by Preferential Arrangements between Chile and Neighbouring Countries referred to in Paragraph 2 (d) of Article I

Preferences in force exclusively between Chile on the one hand, and

1. Argentina
 2. Bolivia
 3. Peru
- on the other hand.

ANNEX F: List of Territories covered by Preferential Arrangements

¹ For imports into Metropolitan France and Territories of the French Union.

between Lebanon and Syria and Neighbouring Countries referred to in Paragraph 2 (d) of Article I

Preferences in force exclusively between the Lebano-Syrian Customs Union, on the one hand, and

1. Palestine
 2. Transjordan
- on the other hand.

ANNEX G: Dates establishing Maximum Margins of Preference referred to in Paragraph 4¹ of Article I

Australia	October 15, 1946
Canada	July 1, 1939
France	January 1, 1939
Lebano-Syrian Customs Union	November 30, 1938
Union of South Africa	July 1, 1938
Southern Rhodesia	May 1, 1941

ANNEX H: Percentage Shares of Total External Trade to be used for the Purpose of Making the Determination referred to in Article XXVI

(based on the average of 1949-1953)

If, prior to the accession of the Government of Japan to the General Agreement, the present Agreement has been accepted by contracting parties the external trade of which under Column I accounts for the percentage of such trade specified in paragraph 6 of Article XXVI, column I shall be applicable for the purposes of that paragraph. If the present Agreement has not been so accepted prior to the accession of the Government of Japan, column II shall be applicable for the purposes of that paragraph.

	<i>Column I</i>	<i>Column II</i>
	(Contracting parties on 1 March 1955)	(Contracting parties on 1 March 1955 and Japan)
Australia	3.1	3.0
Austria	0.9	0.8
Belgium-Luxembourg	4.3	4.2
Brazil	2.5	2.4
Burma	0.3	0.3
Canada	6.7	6.5
Ceylon	0.5	0.5
Chile	0.6	0.6
Cuba	1.1	1.1
Czechoslovakia	1.4	1.4
Denmark	1.4	1.4
Dominican Republic	0.1	0.1

¹ The authentic text erroneously reads "Paragraph 3".

Finland	1.0
France	8.5
Germany, Federal Republic of	5.3
Greece	0.4
Haiti	0.1
India	2.4
Indonesia	1.3
Italy	2.9
Netherlands, Kingdom of the	4.7
New Zealand	1.0
Nicaragua	0.1
Norway	1.1
Pakistan	0.9
Peru	0.4
Rhodesia and Nyasaland	0.6
Sweden	2.5
Turkey	0.6
Union of South Africa	1.8
United Kingdom	20.3
United States of America	20.6
Uruguay	0.4
Japan	—
	100.0
	100.0

Note: These percentages have been computed taking into account the trade of all territories in respect of which the General Agreement on Tariffs and Trade is applied.

ANNEX I: Notes and Supplementary Provisions

Ad Article I

Paragraph 1

The obligations incorporated in paragraph 1 of Article I by reference to paragraphs 2 and 4 of Article III and those incorporated in paragraph 2 (b) of Article II by reference to Article VI shall be considered as falling within Part II for the purposes of the Protocol of Provisional Application.

The cross-references, in the paragraph immediately above and in paragraph 1 of Article I, to paragraphs 2 and 4 of Article III shall only apply after Article III has been modified by the entry into force of the amendment provided for in the Protocol Modifying Part II and Article XXVI of the General Agreement on Tariffs and Trade, dated September 14, 1948.¹

Paragraph 4

The term "margin of preference" means the absolute difference between the most-favoured-nation rate of duty and the preferential rate of duty for the like product, and not the proportionate relation between those rates. As examples:

- (1) If the most-favoured-nation rate were 36 per cent *ad valorem* and the preferential rate were 24 per cent *ad valorem*, the margin of preference would be 12 per cent *ad valorem*, and not one-third of the most-favoured-nation rate;
- (2) If the most-favoured-nation rate were 36 per cent *ad valorem* and the preferential rate were expressed as two-thirds of the most-favoured-nation rate, the margin of preference would be 12 per cent *ad valorem*;
- (3) If the most-favoured-nation rate were 2 francs per kilogramme and the preferential rate were 1.50 francs per kilogramme, the margin of preference would be 0.50 franc per kilogramme.

The following kinds of customs action, taken in accordance with established uniform procedures, would not be contrary to a general binding of margins of preference:

- (i) The re-application to an imported product of a tariff classification or rate of duty, properly applicable to such product, in cases in which the application of such classification or rate to such product was temporarily suspended or inoperative on April 10, 1947; and
- (ii) The classification of a particular product under a tariff item other than that under which importations of that product were classified on April 10, 1947, in cases in which the tariff law clearly contemplates that such product may be classified under more than one tariff item.

Ad Article II

Paragraph 2 (a)

The cross-reference, in paragraph 2 (a) of Article II, to paragraph 2 of Article III shall only apply after Article III has been modified by the entry into force of the amendment provided for in the Protocol Modifying Part II and Article XXVI of the General Agreement on Tariffs and Trade, dated September 14, 1948.¹

Paragraph 2 (b)

See the note relating to paragraph 1 of Article I.

Paragraph 4

Except where otherwise specifically agreed between the contracting parties which initially negotiated the concession, the provisions of this paragraph will be applied in the light of the provisions of Article 31 of the Havana Charter.

Ad Article III

Any internal tax or other internal charge, or any law, regulation or requirement of the kind referred to in paragraph 1 which applies to an imported product and to the like domestic product and is collected or enforced in the case of the imported product at the time or point of importation, is nevertheless to be regarded as an internal tax or other internal charge, or a law, regulation or requirement of the kind referred to in paragraph 1, and is accordingly subject to the provisions of Article III.

¹ This Protocol entered into force on 14 December 1948.

¹ This Protocol entered into force on 14 December 1948.

Paragraph 1

The application of paragraph 1 to internal taxes imposed by local governments and authorities with the territory of a contracting party is subject to the provisions of the final paragraph of Article XXIV. The term "reasonable measures" in the last-mentioned paragraph would not require, for example, the repeal of existing national legislation authorizing local governments to impose internal taxes which, although technically inconsistent with the letter of Article III, are not in fact inconsistent with its spirit, if such repeal would result in a serious financial hardship for the local governments or authorities concerned. With regard to taxation by local governments or authorities which is inconsistent with both the letter and spirit of Article III, the term "reasonable measures" would permit a contracting party to eliminate the inconsistent taxation gradually over a transition period, if abrupt action would create serious administrative and financial difficulties.

Paragraph 2

A tax conforming to the requirements of the first sentence of paragraph 2 would be considered to be inconsistent with the provisions of the second sentence only in cases where competition was involved between, on the one hand, the taxed product and, on the other hand, a directly competitive or substitutable product which was not similarly taxed.

Paragraph 5

Regulations consistent with the provisions of the first sentence of paragraph 5 shall not be considered to be contrary to the provisions of the second sentence in any case in which all of the products subject to the regulations are produced domestically in substantial quantities. A regulation cannot be justified as being consistent with the provisions of the second sentence on the ground that the proportion or amount allocated to each of the products which are the subject of the regulation constitutes an equitable relationship between imported and domestic products.

*Ad Article V**Paragraph 5*

With regard to transportation charges, the principle laid down in paragraph 5 refers to like products being transported on the same route under like conditions.

*Ad Article VI**Paragraph 1*

1. Hidden dumping by associated houses (that is, the sale by an importer at a price below that corresponding to the price invoiced by an exporter with whom the importer is associated, and also below the price in the exporting country) constitutes a form of price dumping with respect to which the margin of dumping may be calculated on the basis of the price at which the goods are resold by the importer.

2. It is recognized that, in the case of imports from a country which has a complete or substantially complete monopoly of its trade and where all domestic prices are fixed by the State, special difficulties may exist in determining price comparability for the purposes of paragraph 1, and in such cases importing contracting parties may find it necessary to take into account the possibility that a strict comparison with domestic prices in such a country may not always be appropriate.

Paragraphs 2 and 3

1. As in many other cases in customs administration, a contracting party may require reasonable security (bond or cash deposit) for the payment of anti-dumping or countervailing duty pending final determination of the facts in any case of suspected dumping or subsidization.

2. Multiple currency practices can in certain circumstances constitute a subsidy to exports which may be met by countervailing duties under paragraph 3 or can constitute a form of dumping by means of a partial depreciation of a country's currency which may be met by action under paragraph 2. By "multiple currency practices" is meant practices by governments or sanctioned by governments.

Paragraph 6 (b)

Waivers under the provisions of this sub-paragraph shall be granted only on application by the contracting party proposing to levy an anti-dumping or countervailing duty, as the case may be.

*Ad Article VII**Paragraph 1*

The expression "or other charges" is not to be regarded as including internal taxes or equivalent charges imposed on or in connection with imported products.

Paragraph 2

1. It would be in conformity with Article VII to presume that "actual value" may be represented by the invoice price, plus any non-included charges for legitimate costs which are proper elements of "actual value" and plus any abnormal discount or other reduction from the ordinary competitive price.

2. It would be in conformity with Article VII, paragraph 2 (b), for a contracting party to construe the phrase "in the ordinary course of trade ... under fully competitive conditions", as excluding any transaction wherein the buyer and seller are not independent of each other and price is not the sole consideration.

3. The standard of "fully competitive conditions" permits a contracting party to exclude from consideration prices involving special discounts limited to exclusive agents.

4. The wording of sub-paragraphs (a) and (b) permits a contracting party to determine the value for customs purposes uniformly either (1) on the basis of a particular exporter's prices of the imported merchandise, or (2) on the basis of the general price level of like merchandise.

Ad Article VIII

1. While Article VIII does not cover the use of multiple rates of exchange as such, paragraphs 1 and 4 condemn the use of exchange taxes or fees as a device for implementing multiple currency practices; if, however, a contracting party is using multiple currency exchange fees for balance of payments reasons with the approval of the International Monetary Fund, the provisions of paragraph 9 (a) of Article XV fully safeguard its position.

2. It would be consistent with paragraph 1 if, on the importation of products from the territory of a contracting party into the territory of another contracting party, the production of certificates of origin should only be required to the extent that is strictly indispensable.

Ad Articles XI, XII, XIII, XIV and XVIII

Throughout Articles XI, XII, XIII, XIV and XVIII, the terms "import restrictions" or "export restrictions" include restrictions made effective through state-trading operations.

Ad Article XI

Paragraph 2 (c)

The term "in any form" in this paragraph covers the same products when in an early stage of processing and still perishable, which compete directly with the fresh product and if freely imported would tend to make the restriction on the fresh product ineffective.

Paragraph 2, last sub-paragraph

The term "special factors" includes changes in relative productive efficiency as between domestic and foreign producers, or as between different foreign producers, but not changes artificially brought about by means not permitted under the Agreement.

Ad Article XVII

The CONTRACTING PARTIES shall make provision for the utmost secrecy in the conduct of any consultation under the provisions of this Article.

Paragraph 3 (c)(i)

Contracting parties applying restrictions shall endeavour to avoid causing serious prejudice to exports of a commodity on which the economy of a contracting party is largely dependent.

Paragraph 4 (b)

It is agreed that the date shall be within ninety days after the entry into force of the amendments of this Article effected by the Protocol Amending the Preamble and Parts II and III of this Agreement. However, should the CONTRACTING PARTIES find that conditions were not suitable for the application of the provisions of this sub-paragraph at the time envisaged, they may determine a later date; *Provided* that such date is not more than thirty days after such time as the obligations of Article VIII, Sections 2, 3 and 4, of the Articles of Agreement of the International Monetary Fund become applicable to contracting parties, members of the Fund, the combined foreign trade of which constitutes at least fifty per centum of the aggregate foreign trade of all contracting parties.

Paragraph 4 (e)

It is agreed that paragraph 4 (e) does not add any new criteria for the imposition or maintenance of quantitative restrictions for balance of payments reasons. It is solely intended to ensure that all external factors such as changes in the terms of trade, quantitative restrictions, excessive tariffs and subsidies, which may be contributing to the balance of payments difficulties of the contracting party applying restrictions, will be fully taken into account.

Ad Article XIII

Paragraph 2 (d)

No mention was made of "commercial considerations" as a rule for the allocation of quotas because it was considered that its application by governmental authorities might not always be practicable. Moreover, in cases where it is practicable, a contracting party could apply these

considerations in the process of seeking agreement, consistently with the general rule laid down in the opening sentence of paragraph 2.

Paragraph 4

See note relating to "special factors" in connection with the last sub-paragraph of paragraph 2 of Article XI.

Ad Article XIV

Paragraph 1

The provisions of this paragraph shall not be so construed as to preclude full consideration by the CONTRACTING PARTIES, in the consultations provided for in paragraph 4 of Article XII and in paragraph 12 of Article XVIII, of the nature, effects and reasons for discrimination in the field of import restrictions.

Paragraph 2

One of the situations contemplated in paragraph 2 is that of a contracting party holding balances acquired as a result of current transactions which it finds itself unable to use without a measure of discrimination.

Ad Article XV

Paragraph 4

The word "frustrate" is intended to indicate, for example, that infringements of the letter of any Article of this Agreement by exchange action shall not be regarded as a violation of that Article if, in practice, there is no appreciable departure from the intent of the Article. Thus, a contracting party which, as part of its exchange control operated in accordance with the Articles of Agreement of the International Monetary Fund, requires payment to be received for its exports in its own currency or in the currency of one or more members of the International Monetary Fund will not thereby be deemed to contravene Article XI or Article XIII. Another example would be that of a contracting party which specifies on an import licence the country from which the goods may be imported, for the purpose not of introducing any additional element of discrimination in its import licensing system but of enforcing permissible exchange controls.

Ad Article XVI

The exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption, or the remission of such duties or taxes in amounts not in excess of those which have accrued, shall not be deemed to be a subsidy.

Section B

1. Nothing in Section B shall preclude the use by a contracting party of multiple rates of exchange in accordance with the Articles of Agreement of the International Monetary Fund.

2. For the purposes of Section B, a "primary product" is understood to be any product of farm, forest or fishery, or any mineral, in its natural form or which has undergone such processing as is customarily required to prepare it for marketing in substantial volume in international trade.

Paragraph 3

1. The fact that a contracting party has not exported the product in question during the previous representative period would not in itself preclude that contracting party from establishing its right to obtain a share of the trade in the product concerned.
2. A system for the stabilization of the domestic price or of the return to domestic producers of a primary product independently of the movements of export prices, which results at times in the sale of the product for export at a price lower than the comparable price charged for the like product to buyers in the domestic market, shall be considered not to involve a subsidy on exports within the meaning of paragraph 3 if the CONTRACTING PARTIES determine that:
 - (a) the system has also resulted, or is so designed as to result, in the sale of the product for export at a price higher than the comparable price charged for the like product to buyers in the domestic market; and
 - (b) the system is so operated, or is designed so to operate, either because of the effective regulation of production or otherwise, as not to stimulate exports unduly or otherwise seriously to prejudice the interests of other contracting parties.

Notwithstanding such determination by the CONTRACTING PARTIES, operations under such a system shall be subject to the provisions of paragraph 3 where they are wholly or partly financed out of government funds in addition to the funds collected from producers in respect of the product concerned.

Paragraph 4

The intention of paragraph 4 is that the contracting parties should seek before the end of 1957 to reach agreement to abolish all remaining subsidies as from 1 January 1958; or, failing this, to reach agreement to extend the application of the standstill until the earliest date thereafter by which they can expect to reach such agreement.

Ad Article XVII

Paragraph 1

The operations of Marketing Boards, which are established by contracting parties and are engaged in purchasing or selling, are subject to the provisions of sub-paragraphs (a) and (b).

The activities of Marketing Boards which are established by contracting parties and which do not purchase or sell but lay down regulations covering private trade are governed by the relevant Articles of this Agreement.

The charging by a state enterprise of different prices for its sales of a product in different markets is not precluded by the provisions of this Article, provided that such different prices are charged for commercial reasons, to meet conditions of supply and demand in export markets.

Paragraph 1 (a)

Governmental measures imposed to insure standards of quality and efficiency in the operation of external trade, or privileges granted for the exploitation of national natural resources but which do not empower the government to exercise control over the trading activities of the enterprise in question, do not constitute "exclusive or special privileges".

Paragraph 1 (b)

A country receiving a "tied loan" is free to take this loan into account as a "commercial consideration" when purchasing requirements abroad.

Paragraph 2

The term "goods" is limited to products as understood in commercial practice, and is not intended to include the purchase or sale of services.

Paragraph 3

Negotiations which contracting parties agree to conduct under this paragraph may be directed towards the reduction of duties and other charges on imports and exports or towards the conclusion of any other mutually satisfactory arrangement consistent with the provisions of this Agreement. (See paragraph 4 of Article II and the note to that paragraph.)

Paragraph 4 (b)

The term "import mark-up" in this paragraph shall represent the margin by which the price charged by the import monopoly for the imported product (exclusive of internal taxes within the purview of Article III, transportation, distribution, and other expenses incident to the purchase, sale or further processing, and a reasonable margin of profit) exceeds the landed cost.

Ad Article XVIII

The CONTRACTING PARTIES and the contracting parties concerned shall preserve the utmost secrecy in respect of matters arising under this Article.

Paragraphs 1 and 4

1. When they consider whether the economy of a contracting party "can only support low standards of living", the CONTRACTING PARTIES shall take into consideration the normal position of that economy and shall not base their determination on exceptional circumstances such as those which may result from the temporary existence of exceptionally favourable conditions for the staple export product or products of such contracting party.

2. The phrase "in the early stages of development" is not meant to apply only to contracting parties which have just started their economic development, but also to contracting parties the economies of which are undergoing a process of industrialization to correct an excessive dependence on primary production.

Paragraphs 2, 3, 7, 13 and 22

The reference to the establishment of particular industries shall apply not only to the establishment of a new industry, but also to the establishment of a new branch of production in an existing industry and to the substantial transformation of an existing industry, and to the substantial expansion of an existing industry supplying a relatively small proportion of the domestic demand. It shall also cover the reconstruction of an industry destroyed or substantially damaged as a result of hostilities or natural disasters.

Paragraph 7 (b)

A modification or withdrawal, pursuant to paragraph 7 (b), by a contracting party, other than the applicant contracting party, referred to in paragraph 7 (a), shall be made within six months of the

day on which the action is taken by the applicant contracting party, and shall become effective on the thirtieth day following the day on which such modification or withdrawal has been notified to the CONTRACTING PARTIES.

Paragraph 11

The second sentence in paragraph 11 shall not be interpreted to mean that a contracting party is required to relax or remove restrictions if such relaxation or removal would thereupon produce conditions justifying the intensification or institution, respectively, of restrictions under paragraph 9 of Article XVIII.

Paragraph 12 (b)

The date referred to in paragraph 12 (b) shall be the date determined by the CONTRACTING PARTIES in accordance with the provisions of paragraph 4 (b) of Article XII of this Agreement.

Paragraphs 13 and 14

It is recognized that, before deciding on the introduction of a measure and notifying the CONTRACTING PARTIES in accordance with paragraph 14, a contracting party may need a reasonable period of time to assess the competitive position of the industry concerned.

Paragraphs 15 and 16

It is understood that the CONTRACTING PARTIES shall invite a contracting party proposing to apply a measure under Section C to consult with them pursuant to paragraph 16 if they are requested to do so by a contracting party the trade of which would be appreciably affected by the measure in question.

Paragraphs 16, 18, 19 and 22

1. It is understood that the CONTRACTING PARTIES may concur in a proposed measure subject to specific conditions or limitations. If the measure as applied does not conform to the terms of the concurrence it will to that extent be deemed a measure in which the CONTRACTING PARTIES have not concurred. In cases in which the CONTRACTING PARTIES have concurred in a measure for a specified period, the contracting party concerned, if it finds that the maintenance of the measure for a further period of time is required to achieve the objective for which the measure was originally taken, may apply to the CONTRACTING PARTIES for an extension of that period in accordance with the provisions and procedures of Section C or D, as the case may be.

2. It is expected that the CONTRACTING PARTIES will, as a rule, refrain from concurring in a measure which is likely to cause serious prejudice to exports of a commodity on which the economy of a contracting party is largely dependent.

Paragraph 18 and 22

The phrase "that the interests of other contracting parties are adequately safeguarded" is meant to provide latitude sufficient to permit consideration in each case of the most appropriate method of safeguarding those interests. The appropriate method may, for instance, take the form of an additional concession to be applied by the contracting party having recourse to Section C or D during such time as the deviation from the other Articles of the Agreement would remain in force or of the temporary suspension by any other contracting party referred to in paragraph 18 of a concession substantially equivalent to the impairment due to the introduction of the measure in question. Such contracting party would have the right to safeguard its interests through such a

temporary suspension of a concession; *Provided* that this right will not be exercised when, in the case of a measure imposed by a contracting party coming within the scope of paragraph 4 (a), the CONTRACTING PARTIES have determined that the extent of the compensatory concession proposed was adequate.

Paragraph 19

The provisions of paragraph 19 are intended to cover the cases where an industry has been in existence beyond the "reasonable period of time" referred to in the note to paragraphs 13 and 14, and should not be so construed as to deprive a contracting party coming within the scope of paragraph 4 (a) of Article XVIII, of its right to resort to the other provisions of Section C, including paragraph 17, with regard to a newly established industry even though it has benefited from incidental protection afforded by balance of payments import restrictions.

Paragraph 21

Any measure taken pursuant to the provisions of paragraph 21 shall be withdrawn forthwith if the action taken in accordance with paragraph 17 is withdrawn or if the CONTRACTING PARTIES concur in the measure proposed after the expiration of the ninety-day time limit specified in paragraph 17.

Ad Article XX

Sub-paragraph (h)

The exception provided for in this sub-paragraph extends to any commodity agreement which conforms to the principles approved by the Economic and Social Council in its resolution 30 (IV) of 28 March 1947.

Ad Article XXIV

Paragraph 9

It is understood that the provisions of Article I would require that, when a product which has been imported into the territory of a member of a customs union or free-trade area at a preferential rate of duty is re-exported to the territory of another member of such union or area, the latter member should collect a duty equal to the difference between the duty already paid and any higher duty that would be payable if the product were being imported directly into its territory.

Paragraph 11

Measures adopted by India and Pakistan in order to carry out definitive trade arrangements between them, once they have been agreed upon, might depart from particular provisions of this Agreement, but these measures would in general be consistent with the objectives of the Agreement.
Ad Article XXVII

The CONTRACTING PARTIES and each contracting party concerned should arrange to conduct the negotiations and consultations with the greatest possible secrecy in order to avoid premature disclosure of details of prospective tariff changes. The CONTRACTING PARTIES shall be informed immediately of all changes in national tariffs resulting from recourse to this Article.

Paragraph 1

1. If the CONTRACTING PARTIES specify a period other than a three-year period, a contracting

party may act pursuant to paragraph 1 or paragraph 3 of Article XXVIII on the first day following the expiration of such other period and, unless the CONTRACTING PARTIES have again specified another period, subsequent periods will be three-year periods following the expiration of such specified period.

2. The provision that on 1 January 1958, and on other days determined pursuant to paragraph 1, a contracting party "may ... modify or withdraw a concession" means that on such day, and on the first day after the end of each period, the legal obligation of such contracting party under Article II is altered; it does not mean that the changes in its customs tariff should necessarily be made effective on that day. If a tariff change resulting from negotiations undertaken pursuant to this Article is delayed, the entry into force of any compensatory concessions may be similarly delayed.

3. Not earlier than six months, nor later than three months, prior to 1 January 1958, or to the termination date of any subsequent period, a contracting party wishing to modify or withdraw any concession embodied in the appropriate Schedule, should notify the CONTRACTING PARTIES to this effect. The CONTRACTING PARTIES shall then determine the contracting party or contracting parties with which the negotiations or consultations referred to in paragraph 1 shall take place. Any contracting party so determined shall participate in such negotiations or consultations with the applicant contracting party with the aim of reaching agreement before the end of the period. Any extension of the assured life of the Schedules shall relate to the Schedules as modified after such negotiations, in accordance with paragraphs 1, 2, and 3 of Article XXVIII. If the CONTRACTING PARTIES are arranging for multilateral tariff negotiations to take place within the period of six months before 1 January 1958, or before any other day determined pursuant to paragraph 1, they shall include in the arrangements for such negotiations suitable procedures for carrying out the negotiations referred to in this paragraph.

4. The object of providing for the participation in the negotiation of any contracting party with a principle supplying interest, in addition to any contracting party with which the concession was originally negotiated, is to ensure that a contracting party with a larger share in the trade affected by the concession than a contracting party with which the concession was originally negotiated shall have an effective opportunity to protect the contractual right which it enjoys under this Agreement. On the other hand, it is not intended that the scope of the negotiations should be such as to make negotiations and agreement under Article XXVIII unduly difficult nor to create complications in the application of this Article in the future to concessions which result from negotiations thereunder. Accordingly, the CONTRACTING PARTIES should only determine that a contracting party has a principal supplying interest if that contracting party has had, over a reasonable period of time prior to the negotiations, a larger share in the market of the applicant contracting party than a contracting party with which the concession was initially negotiated or would, in the judgement of the CONTRACTING PARTIES, have had such a share in the absence of discriminatory quantitative restrictions maintained by the applicant contracting party. It would therefore not be appropriate for the CONTRACTING PARTIES to determine that more than one contracting party, or in those exceptional cases where there is near equality more than two contracting parties, had a principal supplying interest.

5. Notwithstanding the definition of a principal supplying interest in note 4 to paragraph 1, the CONTRACTING PARTIES may exceptionally determine that a contracting party has a principal supplying interest if the concession in question affects trade which constitutes a major part of the total exports of such contracting party.

6. It is not intended that provision for participation in the negotiations of any contracting party with a principal supplying interest, and for consultation with any contracting party having a substantial interest in the concession which the applicant contracting party is seeking to modify or withdraw, should have the effect that it should have to pay compensation or suffer retaliation greater than the withdrawal or modification sought, judged in the light of the conditions of trade at the time

of the proposed withdrawal or modification, making allowance for any discriminatory quantitative restrictions maintained by the applicant contracting party.

7. The expression "substantial interest" is not capable of a precise definition and accordingly may present difficulties for the CONTRACTING PARTIES. It is, however, intended to be construed to cover only those contracting parties which have, or in the absence of discriminatory quantitative restrictions affecting their exports could reasonably be expected to have, a significant share in the market of the contracting party seeking to modify or withdraw the concession.

Paragraph 4

1. Any request for authorization to enter into negotiations shall be accompanied by all relevant statistical and other data. A decision on such request shall be made within thirty days of its submission.

2. It is recognized that to permit certain contracting parties, depending in large measure on a relatively small number of primary commodities and relying on the tariff as an important aid for furthering diversification of their economies or as an important source of revenue, normally to negotiate for the modification or withdrawal of concessions only under paragraph 1 of Article XXVIII, might cause them at such time to make modifications or withdrawals which in the long run would prove unnecessary. To avoid such a situation the CONTRACTING PARTIES shall authorize any such contracting party, under paragraph 4, to enter into negotiations unless they consider this would result in, or contribute substantially towards, such an increase in tariff levels as to threaten the stability of the Schedules to this Agreement or lead to undue disturbance of international trade.

3. It is expected that negotiations authorized under paragraph 4 for modification or withdrawal of a single item, or a very small group of items, could normally be brought to a conclusion in sixty days. It is recognized, however, that such a period will be inadequate for cases involving negotiations for the modification or withdrawal of a larger number of items and in such cases, therefore, it would be appropriate for the CONTRACTING PARTIES to prescribe a longer period.

4. The determination referred to in paragraph 4 (d) shall be made by the CONTRACTING PARTIES within thirty days of the submission of the matter to them unless the applicant contracting party agrees to a longer period.

5. In determining under paragraph 4 (d) whether an applicant contracting party has unreasonably failed to offer adequate compensation, it is understood that the CONTRACTING PARTIES will take due account of the special position of a contracting party which has bound a high proportion of its tariffs at very low rates of duty and to this extent has less scope than other contracting parties to make compensatory adjustment.

Ad Article XXVIII bis

Paragraph 3

It is understood that the reference to fiscal needs would include the revenues aspect of duties and particularly duties imposed primarily for revenue purpose, or duties imposed on products which can be substituted for products subject to revenue duties to prevent the avoidance of such duties.

Ad Article XXIX

Paragraph 1

Chapters VII and VIII of the Havana Charter have been excluded from paragraph 1 because

they generally deal with the organization, functions and procedures of the International Trade Organization.

Ad Part IV

The words "developed contracting parties" and the words "less-developed contracting parties" as used in Part IV are to be understood to refer to developed and less-developed countries which are parties to the General Agreement on Tariffs and Trade.

Ad Article XXXVII

Paragraph 1

This Article is based upon the objectives set forth in Article I as it will be amended by Section A of paragraph 1 of the Protocol Amending Part I and Articles XXIX and XXX when that Protocol enters into force.¹

Paragraph 4

The term "primary products" includes agricultural products, *vide* paragraph 2 of the note *ad* Article XVI, Section B.

Paragraph 5

A diversification programme would generally include the intensification of activities for the processing of primary products and the development of manufacturing industries, taking into account the situation of the particular contracting party and the world outlook for production and consumption of different commodities.

Paragraph 8

It is understood that the phrase "do not expect reciprocity" means, in accordance with the objectives set forth in this Article, that the less-developed contracting parties should not be expected, in the course of trade negotiations, to make contributions which are inconsistent with their individual development, financial and trade needs, taking into consideration past trade developments.

This paragraph would apply in the event of action under Section A of Article XVIII, Article XXVIII, Article XXVIII *bis* (Article XXIX after the amendment set forth in Section A of paragraph 1 of the Protocol Amending Part I and Articles XXIX and XXX shall have become effective), Article XXXIII, or any other procedure under this Agreement.

Ad Article XXXVII

Paragraph 1 (a)

This paragraph would apply in the event of negotiations for reduction or elimination of tariffs or other restrictive regulations of commerce under Articles XXVIII, XXVIII *bis* (XXIX after the amendment set forth in Section A of paragraph 1 of the Protocol Amending Part I and Articles XXIX and XXX shall have become effective), and Article XXXIII, as well as in connection with other action to effect such reduction or elimination which contracting parties may be able to undertake.

¹ This Protocol was abandoned on 1 January 1968.

Paragraph 3 (b)

The other measures referred to in this paragraph might include steps to promote domestic structural changes, to encourage the consumption of particular products, or to introduce measures of trade promotion.

PROTOCOL OF PROVISIONAL APPLICATION OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE

1. The Governments of the COMMONWEALTH OF AUSTRALIA, the KINGDOM OF BELGIUM (in respect of its metropolitan territory), CANADA, the FRENCH REPUBLIC (in respect of its metropolitan territory), the GRAND-DUCHY OF LUXEMBURG, the KINGDOM OF THE NETHERLANDS (in respect of its metropolitan territory), the UNITED KINGDOM OF GREAT BRITAIN AND NORTHERN IRELAND (in respect of its metropolitan territory), and the UNITED STATES OF AMERICA undertake, provided that this Protocol shall have been signed on behalf of all the foregoing Governments not later than 15 November 1947, to apply provisionally on and after 1 January 1948:

- (a) Parts I and III of the General Agreement on Tariffs and Trade, and
 - (b) Part II of that Agreement to the fullest extent not inconsistent with existing legislation.
2. The foregoing Governments shall make effective such provisional application of the General Agreement, in respect of any of their territories other than their metropolitan territories, on or after 1 January 1948, upon the expiration of thirty days from the day on which notice of such application is received by the Secretary-General of the United Nations.
3. Any other government signatory to this Protocol shall make effective such provisional application of the General Agreement, on or after 1 January 1948, upon the expiration of thirty days from the day of signature of this Protocol on behalf of such Government.
4. This Protocol shall remain open for signature at the Headquarters of the United Nations (a) until 15 November 1947, on behalf of any government named in paragraph 1 of this Protocol which has not signed it on this day, and (b) until 30 June 1948, on behalf of any other Government signatory to the Final Act adopted at the conclusion of the Second Session of the Preparatory Committee of the United Nations Conference on Trade and Employment which has not signed it on this day.
5. Any government applying this Protocol shall be free to withdraw such application, and such withdrawal shall take effect upon the expiration of sixty days from the day on which written notice of such withdrawal is received by the Secretary-General of the United Nations.
6. The original of this Protocol shall be deposited with the Secretary-General of the United Nations, who will furnish certified copies thereof to all interested Governments.

In WITNESS WHEREOF the respective Representatives, after having communicated their full powers, found to be in good and due form, have signed the Protocol.

DONE at Geneva, in a single copy, in the English and the French languages, both texts authentic, this thirtieth day of October one thousand nine hundred and forty-seven.

General Agreement on Tariffs and Trade. 1994

GENERAL AGREEMENT ON TARIFFS AND TRADE 1994

1. The General Agreement on Tariffs and Trade 1994 ("GATT 1994") shall consist of:
 - (a) the provisions in the General Agreement on Tariffs and Trade, dated 30 October 1947, annexed to the Final Act Adopted at the Conclusion of the Second Session of the Preparatory Committee of the United Nations Conference on Trade and Employment (excluding the Protocol of Provisional Application), as rectified, amended or modified by the terms of legal instruments which have entered into force before the date of entry into force of the WTO Agreement;
 - (b) the provisions of the legal instruments set forth below that have entered into force under the GATT 1947 before the date of entry into force of the WTO Agreement:
 - (i) protocols and certifications relating to tariff concessions;
 - (ii) protocols of accession (excluding the provisions (a) concerning provisional application and withdrawal of provisional application and (b) providing that Part II of GATT 1947 shall be applied provisionally to the fullest extent not inconsistent with legislation existing on the date of the Protocol);
 - (iii) decisions on waivers granted under Article XXV of GATT 1947 and still in force on the date of entry into force of the WTO Agreement¹;
 - (iv) other decisions of the CONTRACTING PARTIES to GATT 1947;
 - (c) the Understandings set forth below:
 - (i) Understanding on the Interpretation of Article II:1(b) of the General Agreement on Tariffs and Trade 1994;
 - (ii) Understanding on the Interpretation of Article XVII of the General Agreement on Tariffs and Trade 1994;
 - (iii) Understanding on Balance-of-Payments Provisions of the General Agreement on Tariffs and Trade 1994;
 - (iv) Understanding on the Interpretation of Article XXIV of the General Agreement on Tariffs and Trade 1994;
 - (v) Understanding in Respect of Waivers of Obligations under the General Agreement on Tariffs and Trade 1994;
 - (vi) Understanding on the Interpretation of Article XXVIII of the General Agreement on Tariffs and Trade 1994; and
 - (d) the Marrakesh Protocol to GATT 1994.

¹The waivers covered by this provision are listed in footnote 7 on pages 11 and 12 in Part II of document MTN/FA of 15 December 1993 and in MTN/FA/Corr.6 of 21 March 1994. The Ministerial Conference shall establish at its first session a revised list of waivers covered by this provision that adds any waivers granted under GATT 1947 after 15 December 1993 and before the date of entry into force of the WTO Agreement, and deletes the waivers which will have expired by that time.

2. Explanatory Notes

- (a) The references to "contracting party" in the provisions of GATT 1994 shall be deemed to read "Member". The references to "less-developed contracting party" and "developed contracting party" shall be deemed to read "developing country Member" and "developed country Member". The references to "Executive Secretary" shall be deemed to read "Director-General of the WTO".
- (b) The references to the CONTRACTING PARTIES acting jointly in Articles XV:1, XV:2, XV:8, XXXVIII and the Notes *Ad Article XII* and XXVIII; and in the provisions on special exchange agreements in Articles XV:2, XV:3, XV:6, XV:7 and XV:9 of GATT 1994 shall be deemed to be references to the WTO. The other functions that the provisions of GATT 1994 assign to the CONTRACTING PARTIES acting jointly shall be allocated by the Ministerial Conference.
 - (c) (i) The text of GATT 1994 shall be authentic in English, French and Spanish.
 - (ii) The text of GATT 1994 in the French language shall be subject to the rectifications of terms indicated in Annex A to document MTN.TNC/41.
 - (iii) The authentic text of GATT 1994 in the Spanish language shall be the text in Volume IV of the Basic Instruments and Selected Documents series, subject to the rectifications of terms indicated in Annex B to document MTN.TNC/41.
3. (a) The provisions of Part II of GATT 1994 shall not apply to measures taken by a Member under specific mandatory legislation, enacted by that Member before it became a contracting party to GATT 1947, that prohibits the use, sale or lease of foreign-built or foreign-reconstructed vessels in commercial applications between points in national waters or the waters of an exclusive economic zone. This exemption applies to: (a) the continuation or prompt renewal of a non-conforming provision of such legislation; and (b) the amendment to a non-conforming provision of such legislation to the extent that the amendment does not decrease the conformity of the provision with Part II of GATT 1947. This exemption is limited to measures taken under legislation described above that is notified and specified prior to the date of entry into force of the WTO Agreement. If such legislation is subsequently modified to decrease its conformity with Part II of GATT 1994, it will no longer qualify for coverage under this paragraph.
 - (b) The Ministerial Conference shall review this exemption not later than five years after the date of entry into force of the WTO Agreement and thereafter every two years for as long as the exemption is in force for the purpose of examining whether the conditions which created the need for the exemption still prevail.
 - (c) A Member whose measures are covered by this exemption shall annually submit a detailed statistical notification consisting of a five-year moving average of actual and expected deliveries of relevant vessels as well as additional information on the use, sale, lease or repair of relevant vessels covered by this exemption.
 - (d) A Member that considers that this exemption operates in such a manner as to justify a reciprocal and proportionate limitation on the use, sale, lease or repair of vessels constructed in the territory of the Member invoking the exemption shall be free to introduce such a limitation subject to prior notification to the Ministerial Conference.
 - (e) This exemption is without prejudice to solutions concerning specific aspects of the legislation covered by this exemption negotiated in sectoral agreements or in other fora.

**UNDERSTANDING ON THE INTERPRETATION OF ARTICLE II:1(b)
OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE 1994**

Members hereby agree as follows:

1. In order to ensure transparency of the legal rights and obligations deriving from paragraph 1(b) of Article II, the nature and level of any "other duties or charges" levied on bound tariff items, as referred to in that provision, shall be recorded in the Schedules of concessions annexed to GATT 1994 against the tariff item to which they apply. It is understood that such recording does not change the legal character of "other duties or charges".
2. The date as of which "other duties or charges" are bound, for the purposes of Article II, shall be 15 April 1994. "Other duties or charges" shall therefore be recorded in the Schedules at the levels applying on this date. At each subsequent renegotiation of a concession or negotiation of a new concession the applicable date for the tariff item in question shall become the date of the incorporation of the new concession in the appropriate Schedule. However, the date of the instrument by which a concession on any particular tariff item was first incorporated into GATT 1947 or GATT 1994 shall also continue to be recorded in column 6 of the Loose-Leaf Schedules.
3. "Other duties or charges" shall be recorded in respect of all tariff bindings.
4. Where a tariff item has previously been the subject of a concession, the level of "other duties or charges" recorded in the appropriate Schedule shall not be higher than the level obtaining at the time of the first incorporation of the concession in that Schedule. It will be open to any Member to challenge the existence of an "other duty or charge", on the ground that no such "other duty or charge" existed at the time of the original binding of the item in question, as well as the consistency of the recorded level of any "other duty or charge" with the previously bound level, for a period of three years after the date of entry into force of the WTO Agreement or three years after the date of deposit with the Director-General of the WTO of the instrument incorporating the Schedule in question into GATT 1994, if that is a later date.
5. The recording of "other duties or charges" in the Schedules is without prejudice to their consistency with rights and obligations under GATT 1994 other than those affected by paragraph 4. All Members retain the right to challenge, at any time, the consistency of any "other duty or charge" with such obligations.
6. For the purposes of this Understanding, the provisions of Articles XXII and XXIII of GATT 1994 as elaborated and applied by the Dispute Settlement Understanding shall apply.
7. "Other duties or charges" omitted from a Schedule at the time of deposit of the instrument incorporating the Schedule in question into GATT 1994 with, until the date of entry into force of the WTO Agreement, the Director-General to the CONTRACTING PARTIES to GATT 1947 or, thereafter, with the Director-General of the WTO, shall not subsequently be added to it and any "other duty or charge" recorded at a level lower than that prevailing on the applicable date shall not be restored to that level unless such additions or changes are made within six months of the date of deposit of the instrument.
8. The decision in paragraph 2 regarding the date applicable to each concession for the purposes of paragraph 1(b) of Article II of GATT 1994 supersedes the decision regarding the applicable date taken on 26 March 1980 (BISD 27S/24).

**UNDERSTANDING ON THE INTERPRETATION OF ARTICLE XVII
OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE 1994**

Members,

Noting that Article XVII provides for obligations on Members in respect of the activities of the state trading enterprises referred to in paragraph 1 of Article XVII, which are required to be consistent with the general principles of non-discriminatory treatment prescribed in GATT 1994 for governmental measures affecting imports or exports by private traders;

Noting further that Members are subject to their GATT 1994 obligations in respect of those governmental measures affecting state trading enterprises;

Recognizing that this Understanding is without prejudice to the substantive disciplines prescribed in Article XVII;

Hereby agree as follows:

1. In order to ensure the transparency of the activities of state trading enterprises, Members shall notify such enterprises to the Council for Trade in Goods, for review by the working party to be set up under paragraph 5, in accordance with the following working definition:

"Governmental and non-governmental enterprises, including marketing boards, which have been granted exclusive or special rights or privileges, including statutory or constitutional powers, in the exercise of which they influence through their purchases or sales the level or direction of imports or exports."

This notification requirement does not apply to imports of products for immediate or ultimate consumption in governmental use or in use by an enterprise as specified above and not otherwise for resale or use in the production of goods for sale.

2. Each Member shall conduct a review of its policy with regard to the submission of notifications on state trading enterprises to the Council for Trade in Goods, taking account of the provisions of this Understanding. In carrying out such a review, each Member should have regard to the need to ensure the maximum transparency possible in its notifications so as to permit a clear appreciation of the manner of operation of the enterprises notified and the effect of their operations on international trade.
3. Notifications shall be made in accordance with the questionnaire on state trading adopted on 24 May 1960 (BISD 9S/184-185), it being understood that Members shall notify the enterprises referred to in paragraph 1 whether or not imports or exports have in fact taken place.
4. Any Member which has reason to believe that another Member has not adequately met its notification obligation may raise the matter with the Member concerned. If the matter is not satisfactorily resolved it may make a counter-notification to the Council for Trade in Goods, for consideration by the working party set up under paragraph 5, simultaneously informing the Member concerned.
5. A working party shall be set up, on behalf of the Council for Trade in Goods, to review notifications and counter-notifications. In the light of this review and without prejudice to paragraph 4(c) of Article XVII, the Council for Trade in Goods may make recommendations

with regard to the adequacy of notifications and the need for further information. The working party shall also review, in the light of the notifications received, the adequacy of the above-mentioned questionnaire on state trading and the coverage of state trading enterprises notified under paragraph 1. It shall also develop an illustrative list showing the kinds of relationships between governments and enterprises, and the kinds of activities, engaged in by these enterprises, which may be relevant for the purposes of Article XVII. It is understood that the Secretariat will provide a general background paper for the working party on the operations of state trading enterprises as they relate to international trade. Membership of the working party shall be open to all Members indicating their wish to serve on it. It shall meet within a year of the date of entry into force of the WTO Agreement and thereafter at least once a year. It shall report annually to the Council for Trade in Goods.¹

UNDERSTANDING ON THE BALANCE-OF-PAYMENTS PROVISIONS OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE 1994

Members,

Recognizing the provisions of Articles XII and XVIII:B of GATT 1994 and of the Declaration on Trade Measures Taken for Balance-of-Payments Purposes adopted on 28 November 1979 (BISD 26S/205-209, referred to in this Understanding as the "1979 Declaration") and in order to clarify such provisions¹;

Hereby *agree* as follows:

Application of Measures

1. Members confirm their commitment to announce publicly, as soon as possible, time-schedules for the removal of restrictive import measures taken for balance-of-payments purposes. It is understood that such time-schedules may be modified as appropriate to take into account changes in the balance-of-payments situation. Whenever a time-schedule is not publicly announced by a Member, that Member shall provide justification as to the reasons therefor.
2. Members confirm their commitment to give preference to those measures which have the least disruptive effect on trade. Such measures (referred to in this Understanding as "price-based measures") shall be understood to include import surcharges, import deposit requirements or other equivalent trade measures with an impact on the price of imported goods. It is understood that, notwithstanding the provisions of Article II, price-based measures taken for balance-of-payments purposes may be applied by a Member in excess of the duties inscribed in the Schedule of that Member. Furthermore, that Member shall indicate the amount by which the price-based measure exceeds the bound duty clearly and separately under the notification procedures of this Understanding.
3. Members shall seek to avoid the imposition of new quantitative restrictions for balance-of-payments purposes unless, because of a critical balance-of-payments situation, price-based measures cannot arrest a sharp deterioration in the external payments position. In those cases in which a Member applies quantitative restrictions, it shall provide justification as to the reasons why price-based measures are not an adequate instrument to deal with the balance-of-payments situation. A Member maintaining quantitative restrictions shall indicate in successive consultations the progress made in significantly reducing the incidence and restrictive effect of such measures. It is understood that not more than one type of restrictive import measure taken for balance-of-payments purposes may be applied on the same product.
4. Members confirm that restrictive import measures taken for balance-of-payments purposes may only be applied to control the general level of imports and may not exceed what is necessary to address the balance-of-payments situation. In order to minimize any incidental protective effects, a Member shall administer restrictions in a transparent manner. The authorities of the importing Member shall provide adequate justification as to the criteria used to determine which products are subject to restriction. As provided in paragraph 3 of Article XII

¹Nothing in this Understanding is intended to modify the rights and obligations of Members under Articles XII or XVIII:B of GATT 1994. The provisions of Articles XXII and XXIII of GATT 1994 as elaborated and applied by the Dispute Settlement Understanding may be invoked with respect to any matters arising from the application of restrictive import measures taken for balance-of-payments purposes.

¹The activities of this working party shall be coordinated with those of the working group provided for in Section III of the Ministerial Decision on Notification Procedures adopted on 15 April 1994.

and paragraph 10 of Article XVIII, Members may, in the case of certain essential products, exclude or limit the application of surcharges applied across the board or other measures applied for balance-of-payments purposes. The term "essential products" shall be understood to mean products which meet basic consumption needs or which contribute to the Member's effort to improve its balance-of-payments situation, such as capital goods or inputs needed for production. In the administration of quantitative restrictions, a Member shall use discretionary licensing only when unavoidable and shall phase it out progressively. Appropriate justification shall be provided as to the criteria used to determine allowable import quantities or values.

Procedures for Balance-of-Payments Consultations

5. The Committee on Balance-of-Payments Restrictions (referred to in this Understanding as the "Committee") shall carry out consultations in order to review all restrictive import measures taken for balance-of-payments purposes. The membership of the Committee is open to all Members indicating their wish to serve on it. The Committee shall follow the procedures for consultations on balance-of-payments restrictions approved on 28 April 1970 (BISD 18S/48-53, referred to in this Understanding as "full consultation procedures"), subject to the provisions set out below.

6. A Member applying new restrictions or raising the general level of its existing restrictions by a substantial intensification of the measures shall enter into consultations with the Committee within four months of the adoption of such measures. The Member adopting such measures may request that a consultation be held under paragraph 4(a) of Article XII or paragraph 12(a) of Article XVIII as appropriate. If no such request has been made, the Chairman of the Committee shall invite the Member to hold such a consultation. Factors that may be examined in the consultation would include, *inter alia*, the introduction of new types of restrictive measures for balance-of-payments purposes, or an increase in the level or product coverage of restrictions.

7. All restrictions applied for balance-of-payments purposes shall be subject to periodic review in the Committee under paragraph 4(b) of Article XII or under paragraph 12(b) of Article XVIII, subject to the possibility of altering the periodicity of consultations in agreement with the consulting Member or pursuant to any specific review procedure that may be recommended by the General Council.

8. Consultations may be held under the simplified procedures approved on 19 December 1972 (BISD 20S/47-49, referred to in this Understanding as "simplified consultation procedures") in the case of least-developed country Members or in the case of developing country Members which are pursuing liberalization efforts in conformity with the schedule presented to the Committee in previous consultations. Simplified consultation procedures may also be used when the Trade Policy Review of a developing country Member is scheduled for the same calendar year as the date fixed for the consultations. In such cases the decision as to whether full consultation procedures should be used will be made on the basis of the factors enumerated in paragraph 8 of the 1979 Declaration. Except in the case of least-developed country Members, no more than two successive consultations may be held under simplified consultation procedures.

Notification and Documentation

9. A Member shall notify to the General Council the introduction of or any changes in the application of restrictive import measures taken for balance-of-payments purposes, as well as any modifications in time-schedules for the removal of such measures as announced under paragraph 1. Significant changes shall be notified to the General Council prior to or not later than 30 days after their announcement. On a yearly basis, each Member shall make available to the Secretariat a consolidated notification, including all changes in laws, regulations, policy

statements or public notices, for examination by Members. Notifications shall include full information, as far as possible, at the tariff-line level, on the type of measures applied, the criteria used for their administration, product coverage and trade flows affected.

10. At the request of any Member, notifications may be reviewed by the Committee. Such reviews would be limited to the clarification of specific issues raised by a notification or examination of whether a consultation under paragraph 4(a) of Article XII or paragraph 12(a) of Article XVIII is required. Members which have reasons to believe that a restrictive import measure applied by another Member was taken for balance-of-payments purposes may bring the matter to the attention of the Committee. The Chairman of the Committee shall request information on the measure and make it available to all Members. Without prejudice to the right of any member of the Committee to seek appropriate clarifications in the course of consultations, questions may be submitted in advance for consideration by the consulting Member.

11. The consulting Member shall prepare a Basic Document for the consultations which, in addition to any other information considered to be relevant, should include: (a) an overview of the balance-of-payments situation and prospects, including a consideration of the internal and external factors having a bearing on the balance-of-payments situation and the domestic policy measures taken in order to restore equilibrium on a sound and lasting basis; (b) a full description of the restrictions applied for balance-of-payments purposes, their legal basis and steps taken to reduce incidental protective effects; (c) measures taken since the last consultation to liberalize import restrictions, in the light of the conclusions of the Committee; (d) a plan for the elimination and progressive relaxation of remaining restrictions. References may be made, when relevant, to the information provided in other notifications or reports made to the WTO. Under simplified consultation procedures, the consulting Member shall submit a written statement containing essential information on the elements covered by the Basic Document.

12. The Secretariat shall, with a view to facilitating the consultations in the Committee, prepare a factual background paper dealing with the different aspects of the plan for consultations. In the case of developing country Members, the Secretariat document shall include relevant background and analytical material on the incidence of the external trading environment on the balance-of-payments situation and prospects of the consulting Member. The technical assistance services of the Secretariat shall, at the request of a developing country Member, assist in preparing the documentation for the consultations.

Conclusions of Balance-of-Payments Consultations

13. The Committee shall report on its consultations to the General Council. When full consultation procedures have been used, the report should indicate the Committee's conclusions on the different elements of the plan for consultations, as well as the facts and reasons on which they are based. The Committee shall endeavour to include in its conclusions proposals for recommendations aimed at promoting the implementation of Articles XII and XVIII:B, the 1979 Declaration and this Understanding. In those cases in which a time-schedule has been presented for the removal of restrictive measures taken for balance-of-payments purposes, the General Council may recommend that, in adhering to such a time-schedule, a Member shall be deemed to be in compliance with its GATT 1994 obligations. Whenever the General Council has made specific recommendations, the rights and obligations of Members shall be assessed in the light of such recommendations. In the absence of specific proposals for recommendations by the General Council, the Committee's conclusions should record the different views expressed in the Committee. When simplified consultation procedures have

been used, the report shall include a summary of the main elements discussed in the Committee and a decision on whether full consultation procedures are required.

UNDERSTANDING ON THE INTERPRETATION OF ARTICLE XXIV OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE 1994

Members,

Having regard to the provisions of Article XXIV of GATT 1994;

Recognizing that customs unions and free trade areas have greatly increased in number and importance since the establishment of GATT 1947 and today cover a significant proportion of world trade;

Recognizing the contribution to the expansion of world trade that may be made by closer integration between the economies of the parties to such agreements;

Recognizing also that such contribution is increased if the elimination between the constituent territories of duties and other restrictive regulations of commerce extends to all trade, and diminished if any major sector of trade is excluded;

Reaffirming that the purpose of such agreements should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other Members with such territories; and that in their formation or enlargement the parties to them should to the greatest possible extent avoid creating adverse effects on the trade of other Members;

Convinced also of the need to reinforce the effectiveness of the role of the Council for Trade in Goods in reviewing agreements notified under Article XXIV, by clarifying the criteria and procedures for the assessment of new or enlarged agreements, and improving the transparency of all Article XXIV agreements;

Recognizing the need for a common understanding of the obligations of Members under paragraph 12 of Article XXIV;

Hereby agree as follows:

1. Customs unions, free-trade areas, and interim agreements leading to the formation of a customs union or free-trade area, to be consistent with Article XXIV, must satisfy, *inter alia*, the provisions of paragraphs 5, 6, 7 and 8 of that Article.

Article XXIV:5

2. The evaluation under paragraph 5(a) of Article XXIV of the general incidence of the duties and other regulations of commerce applicable before and after the formation of a customs union shall in respect of duties and charges be based upon an overall assessment of weighted average tariff rates and of customs duties collected. This assessment shall be based on import statistics for a previous representative period to be supplied by the customs union, on a tariff-line basis and in values and quantities, broken down by WTO country of origin. The Secretariat shall compute the weighted average tariff rates and customs duties collected in accordance with the methodology used in the assessment of tariff offers in the Uruguay Round of Multilateral Trade Negotiations. For this purpose, the duties and charges to be taken into consideration shall be the applied rates of duty. It is recognized that for the purpose of the overall assessment of the incidence of other regulations of commerce for which quantification and aggregation are difficult, the examination of individual measures, regulations, products covered and trade flows affected may be required.

3. The "reasonable length of time" referred to in paragraph 5(c) of Article XXIV should exceed 10 years only in exceptional cases. In cases where Members parties to an interim agreement believe that 10 years would be insufficient they shall provide a full explanation to the Council for Trade in Goods of the need for a longer period.

Article XXIV:6

4. Paragraph 6 of Article XXIV establishes the procedure to be followed when a Member forming a customs union proposes to increase a bound rate of duty. In this regard Members reaffirm that the procedure set forth in Article XXVIII, as elaborated in the guidelines adopted on 10 November 1980 (BISD 27S/26-28) and in the Understanding on the Interpretation of Article XXVIII of GATT 1994, must be commenced before tariff concessions are modified or withdrawn upon the formation of a customs union or an interim agreement leading to the formation of a customs union.

5. These negotiations will be entered into in good faith with a view to achieving mutually satisfactory compensatory adjustment. In such negotiations, as required by paragraph 6 of Article XXIV, due account shall be taken of reductions of duties on the same tariff line made by other constituents of the customs union upon its formation. Should such reductions not be sufficient to provide the necessary compensatory adjustment, the customs union would offer compensation, which may take the form of reductions of duties on other tariff lines. Such an offer shall be taken into consideration by the Members having negotiating rights in the binding being modified or withdrawn. Should the compensatory adjustment remain unacceptable, negotiations should be continued. Where, despite such efforts, agreement in negotiations on compensatory adjustment under Article XXVIII as elaborated by the Understanding on the Interpretation of Article XXVIII of GATT 1994 cannot be reached within a reasonable period from the initiation of negotiations, the customs union shall, nevertheless, be free to modify or withdraw the concessions; affected Members shall then be free to withdraw substantially equivalent concessions in accordance with Article XXVIII.

6. GATT 1994 imposes no obligation on Members benefiting from a reduction of duties consequent upon the formation of a customs union, or an interim agreement leading to the formation of a customs union, to provide compensatory adjustment to its constituents.

Review of Customs Unions and Free-Trade Areas

7. All notifications made under paragraph 7(a) of Article XXIV shall be examined by a working party in the light of the relevant provisions of GATT 1994 and of paragraph 1 of this Understanding. The working party shall submit a report to the Council for Trade in Goods on its findings in this regard. The Council for Trade in Goods may make such recommendations to Members as it deems appropriate.

8. In regard to interim agreements, the working party may in its report make appropriate recommendations on the proposed time-frame and on measures required to complete the formation of the customs union or free-trade area. It may if necessary provide for further review of the agreement.

9. Members parties to an interim agreement shall notify substantial changes in the plan and schedule included in that agreement to the Council for Trade in Goods and, if so requested, the Council shall examine the changes.

10. Should an interim agreement notified under paragraph 7(a) of Article XXIV not include a plan and schedule, contrary to paragraph 5(c) of Article XXIV, the working party shall in

its report recommend such a plan and schedule. The parties shall not maintain or put into force, as the case may be, such agreement if they are not prepared to modify it in accordance with these recommendations. Provision shall be made for subsequent review of the implementation of the recommendations.

11. Customs unions and constituents of free-trade areas shall report periodically to the Council for Trade in Goods, as envisaged by the CONTRACTING PARTIES to GATT 1947 in their instruction to the GATT 1947 Council concerning reports on regional agreements (BISD 18S/38), on the operation of the relevant agreement. Any significant changes and/or developments in the agreements should be reported as they occur.

Dispute Settlement

12. The provisions of Articles XXII and XXIII of GATT 1994 as elaborated and applied by the Dispute Settlement Understanding may be invoked with respect to any matters arising from the application of those provisions of Article XXIV relating to customs unions, free-trade areas or interim agreements leading to the formation of a customs union or free-trade area.

Article XXIV:12

13. Each Member is fully responsible under GATT 1994 for the observance of all provisions of GATT 1994, and shall take such reasonable measures as may be available to it to ensure such observance by regional and local governments and authorities within its territory.

14. The provisions of Articles XXII and XXIII of GATT 1994 as elaborated and applied by the Dispute Settlement Understanding may be invoked in respect of measures affecting its observance taken by regional or local governments or authorities within the territory of a Member. When the Dispute Settlement Body has ruled that a provision of GATT 1994 has not been observed, the responsible Member shall take such reasonable measures as may be available to it to ensure its observance. The provisions relating to compensation and suspension of concessions or other obligations apply in cases where it has not been possible to secure such observance.

15. Each Member undertakes to accord sympathetic consideration to and afford adequate opportunity for consultation regarding any representations made by another Member concerning measures affecting the operation of GATT 1994 taken within the territory of the former.

**UNDERSTANDING IN RESPECT OF WAIVERS OF OBLIGATIONS
UNDER THE GENERAL AGREEMENT ON TARIFFS AND TRADE 1994**

Members hereby agree as follows:

1. A request for a waiver or for an extension of an existing waiver shall describe the measures which the Member proposes to take, the specific policy objectives which the Member seeks to pursue and the reasons which prevent the Member from achieving its policy objectives by measures consistent with its obligations under GATT 1994.
2. Any waiver in effect on the date of entry into force of the WTO Agreement shall terminate, unless extended in accordance with the procedures above and those of Article IX of the WTO Agreement, on the date of its expiry or two years from the date of entry into force of the WTO Agreement, whichever is earlier.
3. Any Member considering that a benefit accruing to it under GATT 1994 is being nullified or impaired as a result of:
 - (a) the failure of the Member to whom a waiver was granted to observe the terms or conditions of the waiver, or
 - (b) the application of a measure consistent with the terms and conditions of the waiver
 may invoke the provisions of Article XXIII of GATT 1994 as elaborated and applied by the Dispute Settlement Understanding.

**UNDERSTANDING ON THE INTERPRETATION OF ARTICLE XXVIII
OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE 1994**

Members hereby agree as follows:

1. For the purposes of modification or withdrawal of a concession, the Member which has the highest ratio of exports affected by the concession (i.e. exports of the product to the market of the Member modifying or withdrawing the concession) to its total exports shall be deemed to have a principal supplying interest if it does not already have an initial negotiating right or a principal supplying interest as provided for in paragraph 1 of Article XXVIII. It is however agreed that this paragraph will be reviewed by the Council for Trade in Goods five years from the date of entry into force of the WTO Agreement with a view to deciding whether this criterion has worked satisfactorily in securing a redistribution of negotiating rights in favour of small and medium-sized exporting Members. If this is not the case, consideration will be given to possible improvements, including, in the light of the availability of adequate data, the adoption of a criterion based on the ratio of exports affected by the concession to exports to all markets of the product in question.
2. Where a Member considers that it has a principal supplying interest in terms of paragraph 1, it should communicate its claim in writing, with supporting evidence, to the Member proposing to modify or withdraw a concession, and at the same time inform the Secretariat. Paragraph 4 of the "Procedures for Negotiations under Article XXVIII" adopted on 10 November 1980 (BISD 27S/26-28) shall apply in these cases.
3. In the determination of which Members have a principal supplying interest (whether as provided for in paragraph 1 above or in paragraph 1 of Article XXVIII) or substantial interest, only trade in the affected product which has taken place on an MFN basis shall be taken into consideration. However, trade in the affected product which has taken place under non-contractual preferences shall also be taken into account if the trade in question has ceased to benefit from such preferential treatment, thus becoming MFN trade, at the time of the negotiation for the modification or withdrawal of the concession, or will do so by the conclusion of that negotiation.
4. When a tariff concession is modified or withdrawn on a new product (i.e. a product for which three years' trade statistics are not available) the Member possessing initial negotiating rights on the tariff line where the product is or was formerly classified shall be deemed to have an initial negotiating right in the concession in question. The determination of principal supplying and substantial interests and the calculation of compensation shall take into account, *inter alia*, production capacity and investment in the affected product in the exporting Member and estimates of export growth, as well as forecasts of demand for the product in the importing Member. For the purposes of this paragraph, "new product" is understood to include a tariff item created by means of a breakout from an existing tariff line.
5. Where a Member considers that it has a principal supplying or a substantial interest in terms of paragraph 4, it should communicate its claim in writing, with supporting evidence, to the Member proposing to modify or withdraw a concession, and at the same time inform the Secretariat. Paragraph 4 of the above-mentioned "Procedures for Negotiations under Article XXVIII" shall apply in these cases.
6. When an unlimited tariff concession is replaced by a tariff rate quota, the amount of compensation provided should exceed the amount of the trade actually affected by the modification of the concession. The basis for the calculation of compensation should be the

amount by which future trade prospects exceed the level of the quota. It is understood that the calculation of future trade prospects should be based on the greater of:

- (a) the average annual trade in the most recent representative three-year period, increased by the average annual growth rate of imports in that same period, or by 10 per cent, whichever is the greater; or
- (b) trade in the most recent year increased by 10 per cent.

In no case shall a Member's liability for compensation exceed that which would be entailed by complete withdrawal of the concession.

7. Any Member having a principal supplying interest, whether as provided for in paragraph 1 above or in paragraph 1 of Article XXVIII, in a concession which is modified or withdrawn shall be accorded an initial negotiating right in the compensatory concessions, unless another form of compensation is agreed by the Members concerned.

**MARRAKESH PROTOCOL TO THE
GENERAL AGREEMENT ON TARIFFS AND TRADE 1994**

Members,

Having carried out negotiations within the framework of GATT 1947, pursuant to the Ministerial Declaration on the Uruguay Round,

Hereby *agree* as follows:

1. The schedule annexed to this Protocol relating to a Member shall become a Schedule to GATT 1994 relating to that Member on the day on which the WTO Agreement enters into force for that Member. Any schedule submitted in accordance with the Ministerial Decision on measures in favour of least-developed countries shall be deemed to be annexed to this Protocol.
2. The tariff reductions agreed upon by each Member shall be implemented in five equal rate reductions, except as may be otherwise specified in a Member's Schedule. The first such reduction shall be made effective on the date of entry into force of the WTO Agreement, each successive reduction shall be made effective on 1 January of each of the following years, and the final rate shall become effective no later than the date four years after the date of entry into force of the WTO Agreement, except as may be otherwise specified in that Member's Schedule. Unless otherwise specified in its Schedule, a Member that accepts the WTO Agreement after its entry into force shall, on the date that Agreement enters into force for it, make effective all rate reductions that have already taken place together with the reductions which it would under the preceding sentence have been obligated to make effective on 1 January of the year following, and shall make effective all remaining rate reductions on the schedule specified in the previous sentence. The reduced rate should in each stage be rounded off to the first decimal. For agricultural products, as defined in Article 2 of the Agreement on Agriculture, the staging of reductions shall be implemented as specified in the relevant parts of the schedules.
3. The implementation of the concessions and commitments contained in the schedules annexed to this Protocol shall, upon request, be subject to multilateral examination by the Members. This would be without prejudice to the rights and obligations of Members under Agreements in Annex 1A of the WTO Agreement.
4. After the schedule annexed to this Protocol relating to a Member has become a Schedule to GATT 1994 pursuant to the provisions of paragraph 1, such Member shall be free at any time to withhold or to withdraw in whole or in part the concession in such Schedule with respect to any product for which the principal supplier is any other Uruguay Round participant the schedule of which has not yet become a Schedule to GATT 1994. Such action can, however, only be taken after written notice of any such withholding or withdrawal of a concession has been given to the Council for Trade in Goods and after consultations have been held, upon request, with any Member, the relevant schedule relating to which has become a Schedule to GATT 1994 and which has a substantial interest in the product involved. Any concessions so withheld or withdrawn shall be applied on and after the day on which the schedule of the Member which has the principal supplying interest becomes a Schedule to GATT 1994.
5. (a) Without prejudice to the provisions of paragraph 2 of Article 4 of the Agreement on Agriculture, for the purpose of the reference in paragraphs 1:(b) and 1(c) of Article II of GATT 1994 to the date of that Agreement, the applicable date in respect of each product which is the subject of a concession provided for in a schedule of concessions annexed to this Protocol shall be the date of this Protocol.

- (b) For the purpose of the reference in paragraph 6(a) of Article II of GATT 1994 to the date of that Agreement, the applicable date in respect of a schedule of concessions annexed to this Protocol shall be the date of this Protocol.
6. In cases of modification or withdrawal of concessions relating to non-tariff measures as contained in Part III of the schedules, the provisions of Article XXVIII of GATT 1994 and the "Procedures for Negotiations under Article XXVIII" adopted on 10 November 1980 (BISD 27S/26-28) shall apply. This would be without prejudice to the rights and obligations of Members under GATT 1994.
7. In each case in which a schedule annexed to this Protocol results for any product in treatment less favourable than was provided for such product in the Schedules of GATT 1947 prior to the entry into force of the WTO Agreement, the Member to whom the schedule relates shall be deemed to have taken appropriate action as would have been otherwise necessary under the relevant provisions of Article XXVIII of GATT 1947 or 1994. The provisions of this paragraph shall apply only to Egypt, Peru, South Africa and Uruguay.
8. The Schedules annexed hereto are authentic in the English, French or Spanish language as specified in each Schedule.
9. The date of this Protocol is 15 April 1994.

[The agreed schedules of participants will be annexed to the Marrakesh Protocol in the treaty copy of the WTO Agreement.]

**Agreement on the Application of Sanitary and
Phytosanitary Measures, 1994**

AGREEMENT ON THE APPLICATION OF SANITARY AND PHYTOSANITARY MEASURES

Members,

Recognizing that no Member should be prevented from adopting or enforcing measures necessary to protect human, animal or plant life or health, subject to the requirement that these measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between Members where the same conditions prevail¹ or a disguised restriction on international trade;

Desiring to improve the human health, animal health and phytosanitary situation in all Members;

Noting that sanitary and phytosanitary measures are often applied on the basis of bilateral agreements or protocols;

Desiring the establishment of a multilateral framework of rules and disciplines to guide the development, adoption and enforcement of sanitary and phytosanitary measures in order to minimize their negative effects on trade;

Recognizing the important contribution that international standards, guidelines and recommendations can make in this regard;

Desiring to further the use of harmonized sanitary and phytosanitary measures between Members, on the basis of international standards, guidelines and recommendations developed by the relevant international organizations, including the Codex Alimentarius Commission, the International Office of Epizootics, and the relevant international and regional organizations operating within the framework of the International Plant Protection Convention, without requiring Members to change their appropriate level of protection of human, animal or plant life or health;

Recognizing that developing country Members may encounter special difficulties in complying with the sanitary or phytosanitary measures of importing Members, and as a consequence in access to markets, and also in the formulation and application of sanitary or phytosanitary measures in their own territories, and desiring to assist them in their endeavours in this regard;

Desiring therefore to elaborate rules for the application of the provisions of GATT 1994 which relate to the use of sanitary or phytosanitary measures, in particular the provisions of Article XX(b);

Hereby agree as follows:

Article 1

General Provisions

1. This Agreement applies to all sanitary and phytosanitary measures which may, directly or indirectly, affect international trade. Such measures shall be developed and applied in accordance with the provisions of this Agreement.

¹In this Agreement, reference to Article XX(b) includes also the chapeau of that Article.

2. For the purposes of this Agreement, the definitions provided in Annex A shall apply.
3. The annexes are an integral part of this Agreement.
4. Nothing in this Agreement shall affect the rights of Members under the Agreement on Technical Barriers to Trade with respect to measures not within the scope of this Agreement.

Article 2

Basic Rights and Obligations

1. Members have the right to take sanitary and phytosanitary measures necessary for the protection of human, animal or plant life or health, provided that such measures are not inconsistent with the provisions of this Agreement.
2. Members shall ensure that any sanitary or phytosanitary measure is applied only to the extent necessary to protect human, animal or plant life or health, is based on scientific principles and is not maintained without sufficient scientific evidence, except as provided for in paragraph 7 of Article 5.
3. Members shall ensure that their sanitary and phytosanitary measures do not arbitrarily or unjustifiably discriminate between Members where identical or similar conditions prevail, including between their own territory and that of other Members. Sanitary and phytosanitary measures shall not be applied in a manner which would constitute a disguised restriction on international trade.
4. Sanitary or phytosanitary measures which conform to the relevant provisions of this Agreement shall be presumed to be in accordance with the obligations of the Members under the provisions of GATT 1994 which relate to the use of sanitary or phytosanitary measures, in particular the provisions of Article XX(b).

Article 3

Harmonization

1. To harmonize sanitary and phytosanitary measures on as wide a basis as possible, Members shall base their sanitary or phytosanitary measures on international standards, guidelines or recommendations, where they exist, except as otherwise provided for in this Agreement, and in particular in paragraph 3.
2. Sanitary or phytosanitary measures which conform to international standards, guidelines or recommendations shall be deemed to be necessary to protect human, animal or plant life or health, and presumed to be consistent with the relevant provisions of this Agreement and of GATT 1994.
3. Members may introduce or maintain sanitary or phytosanitary measures which result in a higher level of sanitary or phytosanitary protection than would be achieved by measures based on the relevant international standards, guidelines or recommendations, if there is a scientific justification, or as a consequence of the level of sanitary or phytosanitary protection a Member determines to be appropriate

in accordance with the relevant provisions of paragraphs 1 through 8 of Article 5.² Notwithstanding the above, all measures which result in a level of sanitary or phytosanitary protection different from that which would be achieved by measures based on international standards, guidelines or recommendations shall not be inconsistent with any other provision of this Agreement.

4. Members shall play a full part, within the limits of their resources, in the relevant international organizations and their subsidiary bodies, in particular the Codex Alimentarius Commission, the International Office of Epizootics, and the international and regional organizations operating within the framework of the International Plant Protection Convention, to promote within these organizations the development and periodic review of standards, guidelines and recommendations with respect to all aspects of sanitary and phytosanitary measures.

5. The Committee on Sanitary and Phytosanitary Measures provided for in paragraphs 1 and 4 of Article 12 (referred to in this Agreement as the "Committee") shall develop a procedure to monitor the process of international harmonization and coordinate efforts in this regard with the relevant international organizations.

Article 4

Equivalence

1. Members shall accept the sanitary or phytosanitary measures of other Members as equivalent, even if these measures differ from their own or from those used by other Members trading in the same product, if the exporting Member objectively demonstrates to the importing Member that its measures achieve the importing Member's appropriate level of sanitary or phytosanitary protection. For this purpose, reasonable access shall be given, upon request, to the importing Member for inspection, testing and other relevant procedures.

2. Members shall, upon request, enter into consultations with the aim of achieving bilateral and multilateral agreements on recognition of the equivalence of specified sanitary or phytosanitary measures.

Article 5

Assessment of Risk and Determination of the Appropriate Level of Sanitary or Phytosanitary Protection

1. Members shall ensure that their sanitary or phytosanitary measures are based on an assessment, as appropriate to the circumstances, of the risks to human, animal or plant life or health, taking into account risk assessment techniques developed by the relevant international organizations.

2. In the assessment of risks, Members shall take into account available scientific evidence; relevant processes and production methods; relevant inspection, sampling and testing methods; prevalence

²For the purposes of paragraph 3 of Article 3, there is a scientific justification if, on the basis of an examination and evaluation of available scientific information in conformity with the relevant provisions of this Agreement, a Member determines that the relevant international standards, guidelines or recommendations are not sufficient to achieve its appropriate level of sanitary or phytosanitary protection.

of specific diseases or pests; existence of pest- or disease-free areas; relevant ecological and environmental conditions; and quarantine or other treatment.

3. In assessing the risk to animal or plant life or health and determining the measure to be applied for achieving the appropriate level of sanitary or phytosanitary protection from such risk, Members shall take into account as relevant economic factors: the potential damage in terms of loss of production or sales in the event of the entry, establishment or spread of a pest or disease; the costs of control or eradication in the territory of the importing Member; and the relative cost-effectiveness of alternative approaches to limiting risks.

4. Members should, when determining the appropriate level of sanitary or phytosanitary protection, take into account the objective of minimizing negative trade effects.

5. With the objective of achieving consistency in the application of the concept of appropriate level of sanitary or phytosanitary protection against risks to human life or health, or to animal and plant life or health, each Member shall avoid arbitrary or unjustifiable distinctions in the levels it considers to be appropriate in different situations, if such distinctions result in discrimination or a disguised restriction on international trade. Members shall cooperate in the Committee, in accordance with paragraphs 1, 2 and 3 of Article 12, to develop guidelines to further the practical implementation of this provision. In developing the guidelines, the Committee shall take into account all relevant factors, including the exceptional character of human health risks to which people voluntarily expose themselves.

6. Without prejudice to paragraph 2 of Article 3, when establishing or maintaining sanitary or phytosanitary measures to achieve the appropriate level of sanitary or phytosanitary protection, Members shall ensure that such measures are not more trade-restrictive than required to achieve their appropriate level of sanitary or phytosanitary protection, taking into account technical and economic feasibility.³

7. In cases where relevant scientific evidence is insufficient, a Member may provisionally adopt sanitary or phytosanitary measures on the basis of available pertinent information, including that from the relevant international organizations as well as from sanitary or phytosanitary measures applied by other Members. In such circumstances, Members shall seek to obtain the additional information necessary for a more objective assessment of risk and review the sanitary or phytosanitary measure accordingly within a reasonable period of time.

8. When a Member has reason to believe that a specific sanitary or phytosanitary measure introduced or maintained by another Member is constraining, or has the potential to constrain, its exports and the measure is not based on the relevant international standards, guidelines or recommendations, or such standards, guidelines or recommendations do not exist, an explanation of the reasons for such sanitary or phytosanitary measure may be requested and shall be provided by the Member maintaining the measure.

³For purposes of paragraph 6 of Article 5, a measure is not more trade-restrictive than required unless there is another measure, reasonably available taking into account technical and economic feasibility, that achieves the appropriate level of sanitary or phytosanitary protection and is significantly less restrictive to trade.

Article 6

Adaptation to Regional Conditions, Including Pest- or Disease-Free Areas and Areas of Low Pest or Disease Prevalence

1. Members shall ensure that their sanitary or phytosanitary measures are adapted to the sanitary or phytosanitary characteristics of the area - whether all of a country, part of a country, or all or parts of several countries - from which the product originated and to which the product is destined. In assessing the sanitary or phytosanitary characteristics of a region, Members shall take into account, *inter alia*, the level of prevalence of specific diseases or pests, the existence of eradication or control programmes, and appropriate criteria or guidelines which may be developed by the relevant international organizations.
2. Members shall, in particular, recognize the concepts of pest- or disease-free areas and areas of low pest or disease prevalence. Determination of such areas shall be based on factors such as geography, ecosystems, epidemiological surveillance, and the effectiveness of sanitary or phytosanitary controls.
3. Exporting Members claiming that areas within their territories are pest- or disease-free areas or areas of low pest or disease prevalence shall provide the necessary evidence thereof in order to objectively demonstrate to the importing Member that such areas are, and are likely to remain, pest- or disease-free areas or areas of low pest or disease prevalence, respectively. For this purpose, reasonable access shall be given, upon request, to the importing Member for inspection, testing and other relevant procedures.

Article 7

Transparency

Members shall notify changes in their sanitary or phytosanitary measures and shall provide information on their sanitary or phytosanitary measures in accordance with the provisions of Annex B.

Article 8

Control, Inspection and Approval Procedures

Members shall observe the provisions of Annex C in the operation of control, inspection and approval procedures, including national systems for approving the use of additives or for establishing tolerances for contaminants in foods, beverages or feedstuffs, and otherwise ensure that their procedures are not inconsistent with the provisions of this Agreement.

Article 9

Technical Assistance

1. Members agree to facilitate the provision of technical assistance to other Members, especially developing country Members, either bilaterally or through the appropriate international organizations. Such assistance may be, *inter alia*, in the areas of processing technologies, research and infrastructure, including in the establishment of national regulatory bodies, and may take the form of advice, credits, donations and grants, including for the purpose of seeking technical expertise, training and equipment to allow such countries to adjust to, and comply with, sanitary or phytosanitary measures necessary to achieve the appropriate level of sanitary or phytosanitary protection in their export markets.
2. Where substantial investments are required in order for an exporting developing country Member to fulfil the sanitary or phytosanitary requirements of an importing Member, the latter shall consider providing such technical assistance as will permit the developing country Member to maintain and expand its market access opportunities for the product involved.

Article 10

Special and Differential Treatment

1. In the preparation and application of sanitary or phytosanitary measures, Members shall take account of the special needs of developing country Members, and in particular of the least-developed country Members.
2. Where the appropriate level of sanitary or phytosanitary protection allows scope for the phased introduction of new sanitary or phytosanitary measures, longer time-frames for compliance should be accorded on products of interest to developing country Members so as to maintain opportunities for their exports.
3. With a view to ensuring that developing country Members are able to comply with the provisions of this Agreement, the Committee is enabled to grant to such countries, upon request, specified, time-limited exceptions in whole or in part from obligations under this Agreement, taking into account their financial, trade and development needs.
4. Members should encourage and facilitate the active participation of developing country Members in the relevant international organizations.

Article 11

Consultations and Dispute Settlement

1. The provisions of Articles XXII and XXIII of GATT 1994 as elaborated and applied by the Dispute Settlement Understanding shall apply to consultations and the settlement of disputes under this Agreement, except as otherwise specifically provided herein.
2. In a dispute under this Agreement involving scientific or technical issues, a panel should seek advice from experts chosen by the panel in consultation with the parties to the dispute. To this end,

the panel may, when it deems it appropriate, establish an advisory technical experts group, or consult the relevant international organizations, at the request of either party to the dispute or on its own initiative.

3. Nothing in this Agreement shall impair the rights of Members under other international agreements, including the right to resort to the good offices or dispute settlement mechanisms of other international organizations or established under any international agreement.

Article 12

Administration

1. A Committee on Sanitary and Phytosanitary Measures is hereby established to provide a regular forum for consultations. It shall carry out the functions necessary to implement the provisions of this Agreement and the furtherance of its objectives, in particular with respect to harmonization. The Committee shall reach its decisions by consensus.

2. The Committee shall encourage and facilitate ad hoc consultations or negotiations among Members on specific sanitary or phytosanitary issues. The Committee shall encourage the use of international standards, guidelines or recommendations by all Members and, in this regard, shall sponsor technical consultation and study with the objective of increasing coordination and integration between international and national systems and approaches for approving the use of food additives or for establishing tolerances for contaminants in foods, beverages or feedstuffs.

3. The Committee shall maintain close contact with the relevant international organizations in the field of sanitary and phytosanitary protection, especially with the Codex Alimentarius Commission, the International Office of Epizootics, and the Secretariat of the International Plant Protection Convention, with the objective of securing the best available scientific and technical advice for the administration of this Agreement and in order to ensure that unnecessary duplication of effort is avoided.

4. The Committee shall develop a procedure to monitor the process of international harmonization and the use of international standards, guidelines or recommendations. For this purpose, the Committee should, in conjunction with the relevant international organizations, establish a list of international standards, guidelines or recommendations relating to sanitary or phytosanitary measures which the Committee determines to have a major trade impact. The list should include an indication by Members of those international standards, guidelines or recommendations which they apply as conditions for import or on the basis of which imported products conforming to these standards can enjoy access to their markets. For those cases in which a Member does not apply an international standard, guideline or recommendation as a condition for import, the Member should provide an indication of the reason therefor, and, in particular, whether it considers that the standard is not stringent enough to provide the appropriate level of sanitary or phytosanitary protection. If a Member revises its position, following its indication of the use of a standard, guideline or recommendation as a condition for import, it should provide an explanation for its change and so inform the Secretariat as well as the relevant international organizations, unless such notification and explanation is given according to the procedures of Annex B.

5. In order to avoid unnecessary duplication, the Committee may decide, as appropriate, to use the information generated by the procedures, particularly for notification, which are in operation in the relevant international organizations.

6. The Committee may, on the basis of an initiative from one of the Members, through appropriate channels invite the relevant international organizations or their subsidiary bodies to examine specific matters with respect to a particular standard, guideline or recommendation, including the basis of explanations for non-use given according to paragraph 4.

7. The Committee shall review the operation and implementation of this Agreement three years after the date of entry into force of the WTO Agreement, and thereafter as the need arises. Where appropriate, the Committee may submit to the Council for Trade in Goods proposals to amend the text of this Agreement having regard, *inter alia*, to the experience gained in its implementation.

Article 13

Implementation

Members are fully responsible under this Agreement for the observance of all obligations set forth herein. Members shall formulate and implement positive measures and mechanisms in support of the observance of the provisions of this Agreement by other than central government bodies. Members shall take such reasonable measures as may be available to them to ensure that non-governmental entities within their territories, as well as regional bodies in which relevant entities within their territories are members, comply with the relevant provisions of this Agreement. In addition, Members shall not take measures which have the effect of, directly or indirectly, requiring or encouraging such regional or non-governmental entities, or local governmental bodies, to act in a manner inconsistent with the provisions of this Agreement. Members shall ensure that they rely on the services of non-governmental entities for implementing sanitary or phytosanitary measures only if these entities comply with the provisions of this Agreement.

Article 14

Final Provisions

The least-developed country Members may delay application of the provisions of this Agreement for a period of five years following the date of entry into force of the WTO Agreement with respect to their sanitary or phytosanitary measures affecting importation or imported products. Other developing country Members may delay application of the provisions of this Agreement, other than paragraph 8 of Article 5 and Article 7, for two years following the date of entry into force of the WTO Agreement with respect to their existing sanitary or phytosanitary measures affecting importation or imported products, where such application is prevented by a lack of technical expertise, technical infrastructure or resources.

ANNEX A

DEFINITIONS⁴1. *Sanitary or phytosanitary measure* - Any measure applied:

- (a) to protect animal or plant life or health within the territory of the Member from risks arising from the entry, establishment or spread of pests, diseases, disease-carrying organisms or disease-causing organisms;
- (b) to protect human or animal life or health within the territory of the Member from risks arising from additives, contaminants, toxins or disease-causing organisms in foods, beverages or feedstuffs;
- (c) to protect human life or health within the territory of the Member from risks arising from diseases carried by animals, plants or products thereof, or from the entry, establishment or spread of pests; or
- (d) to prevent or limit other damage within the territory of the Member from the entry, establishment or spread of pests.

Sanitary or phytosanitary measures include all relevant laws, decrees, regulations, requirements and procedures including, *inter alia*, end product criteria; processes and production methods; testing, inspection, certification and approval procedures; quarantine treatments including relevant requirements associated with the transport of animals or plants, or with the materials necessary for their survival during transport; provisions on relevant statistical methods, sampling procedures and methods of risk assessment; and packaging and labelling requirements directly related to food safety.

2. *Harmonization* - The establishment, recognition and application of common sanitary and phytosanitary measures by different Members.3. *International standards, guidelines and recommendations*

- (a) for food safety, the standards, guidelines and recommendations established by the Codex Alimentarius Commission relating to food additives, veterinary drug and pesticide residues, contaminants, methods of analysis and sampling, and codes and guidelines of hygienic practice;
- (b) for animal health and zoonoses, the standards, guidelines and recommendations developed under the auspices of the International Office of Epizootics;
- (c) for plant health, the international standards, guidelines and recommendations developed under the auspices of the Secretariat of the International Plant Protection Convention in cooperation with regional organizations operating within the framework of the International Plant Protection Convention; and

⁴For the purpose of these definitions, "animal" includes fish and wild fauna; "plant" includes forests and wild flora; "pests" include weeds; and "contaminants" include pesticide and veterinary drug residues and extraneous matter.

- (d) for matters not covered by the above organizations, appropriate standards, guidelines and recommendations promulgated by other relevant international organizations open for membership to all Members, as identified by the Committee.

4. *Risk assessment* - The evaluation of the likelihood of entry, establishment or spread of a pest or disease within the territory of an importing Member according to the sanitary or phytosanitary measures which might be applied, and of the associated potential biological and economic consequences; or the evaluation of the potential for adverse effects on human or animal health arising from the presence of additives, contaminants, toxins or disease-causing organisms in food, beverages or feedstuffs.

5. *Appropriate level of sanitary or phytosanitary protection* - The level of protection deemed appropriate by the Member establishing a sanitary or phytosanitary measure to protect human, animal or plant life or health within its territory.

NOTE: Many Members otherwise refer to this concept as the "acceptable level of risk".

6. *Pest- or disease-free area* - An area, whether all of a country, part of a country, or all or parts of several countries, as identified by the competent authorities, in which a specific pest or disease does not occur.

NOTE: A pest- or disease-free area may surround, be surrounded by, or be adjacent to an area - whether within part of a country or in a geographic region which includes parts of or all of several countries - in which a specific pest or disease is known to occur but is subject to regional control measures such as the establishment of protection, surveillance and buffer zones which will confine or eradicate the pest or disease in question.

7. *Area of low pest or disease prevalence* - An area, whether all of a country, part of a country, or all or parts of several countries, as identified by the competent authorities, in which a specific pest or disease occurs at low levels and which is subject to effective surveillance, control or eradication measures.

ANNEX B

TRANSPARENCY OF SANITARY AND PHYTOSANITARY REGULATIONS

Publication of regulations

1. Members shall ensure that all sanitary and phytosanitary regulations⁵ which have been adopted are published promptly in such a manner as to enable interested Members to become acquainted with them.
2. Except in urgent circumstances, Members shall allow a reasonable interval between the publication of a sanitary or phytosanitary regulation and its entry into force in order to allow time for producers in exporting Members, and particularly in developing country Members, to adapt their products and methods of production to the requirements of the importing Member.

Enquiry points

3. Each Member shall ensure that one enquiry point exists which is responsible for the provision of answers to all reasonable questions from interested Members as well as for the provision of relevant documents regarding:
 - (a) any sanitary or phytosanitary regulations adopted or proposed within its territory;
 - (b) any control and inspection procedures, production and quarantine treatment, pesticide tolerance and food additive approval procedures, which are operated within its territory;
 - (c) risk assessment procedures, factors taken into consideration, as well as the determination of the appropriate level of sanitary or phytosanitary protection;
 - (d) the membership and participation of the Member, or of relevant bodies within its territory, in international and regional sanitary and phytosanitary organizations and systems, as well as in bilateral and multilateral agreements and arrangements within the scope of this Agreement, and the texts of such agreements and arrangements.

4. Members shall ensure that where copies of documents are requested by interested Members, they are supplied at the same price (if any), apart from the cost of delivery, as to the nationals⁶ of the Member concerned.

⁵Sanitary and phytosanitary measures such as laws, decrees or ordinances which are applicable generally.

⁶When "nationals" are referred to in this Agreement, the term shall be deemed, in the case of a separate customs territory Member of the WTO, to mean persons, natural or legal, who are domiciled or who have a real and effective industrial or commercial establishment in that customs territory.

Notification procedures

5. Whenever an international standard, guideline or recommendation does not exist or the content of a proposed sanitary or phytosanitary regulation is not substantially the same as the content of an international standard, guideline or recommendation, and if the regulation may have a significant effect on trade of other Members, Members shall:
 - (a) publish a notice at an early stage in such a manner as to enable interested Members to become acquainted with the proposal to introduce a particular regulation;
 - (b) notify other Members, through the Secretariat, of the products to be covered by the regulation together with a brief indication of the objective and rationale of the proposed regulation. Such notifications shall take place at an early stage, when amendments can still be introduced and comments taken into account;
 - (c) provide upon request to other Members copies of the proposed regulation and, whenever possible, identify the parts which in substance deviate from international standards, guidelines or recommendations;
 - (d) without discrimination, allow reasonable time for other Members to make comments in writing, discuss these comments upon request, and take the comments and the results of the discussions into account.
6. However, where urgent problems of health protection arise or threaten to arise for a Member, that Member may omit such of the steps enumerated in paragraph 5 of this Annex as it finds necessary, provided that the Member:
 - (a) immediately notifies other Members, through the Secretariat, of the particular regulation and the products covered, with a brief indication of the objective and the rationale of the regulation, including the nature of the urgent problem(s);
 - (b) provides, upon request, copies of the regulation to other Members;
 - (c) allows other Members to make comments in writing, discusses these comments upon request, and takes the comments and the results of the discussions into account.
7. Notifications to the Secretariat shall be in English, French or Spanish.
8. Developed country Members shall, if requested by other Members, provide copies of the documents or, in case of voluminous documents, summaries of the documents covered by a specific notification in English, French or Spanish.
9. The Secretariat shall promptly circulate copies of the notification to all Members and interested international organizations and draw the attention of developing country Members to any notifications relating to products of particular interest to them.
10. Members shall designate a single central government authority as responsible for the implementation, on the national level, of the provisions concerning notification procedures according to paragraphs 5, 6, 7 and 8 of this Annex.

General reservations

ANNEX C

CONTROL, INSPECTION AND APPROVAL PROCEDURES⁷

11. Nothing in this Agreement shall be construed as requiring:

- (a) the provision of particulars or copies of drafts or the publication of texts other than in the language of the Member except as stated in paragraph 8 of this Annex; or
- (b) Members to disclose confidential information which would impede enforcement of sanitary or phytosanitary legislation or which would prejudice the legitimate commercial interests of particular enterprises.

1. Members shall ensure, with respect to any procedure to check and ensure the fulfilment of sanitary or phytosanitary measures, that:

- (a) such procedures are undertaken and completed without undue delay and in no less favourable manner for imported products than for like domestic products;
- (b) the standard processing period of each procedure is published or that the anticipated processing period is communicated to the applicant upon request; when receiving an application, the competent body promptly examines the completeness of the documentation and informs the applicant in a precise and complete manner of all deficiencies; the competent body transmits as soon as possible the results of the procedure in a precise and complete manner to the applicant so that corrective action may be taken if necessary; even when the application has deficiencies, the competent body proceeds as far as practicable with the procedure if the applicant so requests; and that upon request, the applicant is informed of the stage of the procedure, with any delay being explained;
- (c) information requirements are limited to what is necessary for appropriate control, inspection and approval procedures, including for approval of the use of additives or for the establishment of tolerances for contaminants in food, beverages or feedstuffs;
- (d) the confidentiality of information about imported products arising from or supplied in connection with control, inspection and approval is respected in a way no less favourable than for domestic products and in such a manner that legitimate commercial interests are protected;
- (e) any requirements for control, inspection and approval of individual specimens of a product are limited to what is reasonable and necessary;
- (f) any fees imposed for the procedures on imported products are equitable in relation to any fees charged on like domestic products or products originating in any other Member and should be no higher than the actual cost of the service;
- (g) the same criteria should be used in the siting of facilities used in the procedures and the selection of samples of imported products as for domestic products so as to minimize the inconvenience to applicants, importers, exporters or their agents;
- (h) whenever specifications of a product are changed subsequent to its control and inspection in light of the applicable regulations, the procedure for the modified product is limited to what is necessary to determine whether adequate confidence exists that the product still meets the regulations concerned; and

⁷Control, inspection and approval procedures include, *inter alia*, procedures for sampling, testing and certification.

- (i) a procedure exists to review complaints concerning the operation of such procedures and to take corrective action when a complaint is justified.

Where an importing Member operates a system for the approval of the use of food additives or for the establishment of tolerances for contaminants in food, beverages or feedstuffs which prohibits or restricts access to its domestic markets for products based on the absence of an approval, the importing Member shall consider the use of a relevant international standard as the basis for access until a final determination is made.

2. Where a sanitary or phytosanitary measure specifies control at the level of production, the Member in whose territory the production takes place shall provide the necessary assistance to facilitate such control and the work of the controlling authorities.
3. Nothing in this Agreement shall prevent Members from carrying out reasonable inspection within their own territories.

Agreement on Technical Barriers to Trade, 1994

AGREEMENT ON TECHNICAL BARRIERS TO TRADE

Members,

Having regard to the Uruguay Round of Multilateral Trade Negotiations;

Desiring to further the objectives of GATT 1994;

Recognizing the important contribution that international standards and conformity assessment systems can make in this regard by improving efficiency of production and facilitating the conduct of international trade;

Desiring therefore to encourage the development of such international standards and conformity assessment systems;

Desiring however to ensure that technical regulations and standards, including packaging, marking and labelling requirements, and procedures for assessment of conformity with technical regulations and standards do not create unnecessary obstacles to international trade;

Recognizing that no country should be prevented from taking measures necessary to ensure the quality of its exports, or for the protection of human, animal or plant life or health, of the environment, or for the prevention of deceptive practices, at the levels it considers appropriate, subject to the requirement that they are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail or a disguised restriction on international trade, and are otherwise in accordance with the provisions of this Agreement;

Recognizing that no country should be prevented from taking measures necessary for the protection of its essential security interest;

Recognizing the contribution which international standardization can make to the transfer of technology from developed to developing countries;

Recognizing that developing countries may encounter special difficulties in the formulation and application of technical regulations and standards and procedures for assessment of conformity with technical regulations and standards, and desiring to assist them in their endeavours in this regard;

Hereby agree as follows:

Article I

General Provisions

1.1 General terms for standardization and procedures for assessment of conformity shall normally have the meaning given to them by definitions adopted within the United Nations system and by international standardizing bodies taking into account their context and in the light of the object and purpose of this Agreement.

1.2 However, for the purposes of this Agreement the meaning of the terms given in Annex 1 applies.

1.3 All products, including industrial and agricultural products, shall be subject to the provisions of this Agreement.

1.4 Purchasing specifications prepared by governmental bodies for production or consumption requirements of governmental bodies are not subject to the provisions of this Agreement but are addressed in the Agreement on Government Procurement, according to its coverage.

1.5 The provisions of this Agreement do not apply to sanitary and phytosanitary measures as defined in Annex A of the Agreement on the Application of Sanitary and Phytosanitary Measures.

1.6 All references in this Agreement to technical regulations, standards and conformity assessment procedures shall be construed to include any amendments thereto and any additions to the rules or the product coverage thereof, except amendments and additions of an insignificant nature.

TECHNICAL REGULATIONS AND STANDARDS

Article 2

Preparation, Adoption and Application of Technical Regulations by Central Government Bodies

With respect to their central government bodies:

2.1 Members shall ensure that in respect of technical regulations, products imported from the territory of any Member shall be accorded treatment no less favourable than that accorded to like products of national origin and to like products originating in any other country.

2.2 Members shall ensure that technical regulations are not prepared, adopted or applied with a view to or with the effect of creating unnecessary obstacles to international trade. For this purpose, technical regulations shall not be more trade-restrictive than necessary to fulfil a legitimate objective, taking account of the risks non-fulfilment would create. Such legitimate objectives are, *inter alia*: national security requirements; the prevention of deceptive practices; protection of human health or safety, animal or plant life or health, or the environment. In assessing such risks, relevant elements of consideration are, *inter alia*: available scientific and technical information, related processing technology or intended end-uses of products.

2.3 Technical regulations shall not be maintained if the circumstances or objectives giving rise to their adoption no longer exist or if the changed circumstances or objectives can be addressed in a less trade-restrictive manner.

2.4 Where technical regulations are required and relevant international standards exist or their completion is imminent, Members shall use them, or the relevant parts of them, as a basis for their technical regulations except when such international standards or relevant parts would be an ineffective or inappropriate means for the fulfilment of the legitimate objectives pursued, for instance because of fundamental climatic or geographical factors or fundamental technological problems.

2.5 A Member preparing, adopting or applying a technical regulation which may have a significant effect on trade of other Members shall, upon the request of another Member, explain the justification for that technical regulation in terms of the provisions of paragraphs 2 to 4. Whenever a technical regulation is prepared, adopted or applied for one of the legitimate objectives explicitly mentioned in paragraph 2, and is in accordance with relevant international standards, it shall be rebuttably presumed not to create an unnecessary obstacle to international trade.

- 2.6 With a view to harmonizing technical regulations on as wide a basis as possible, Members shall play a full part, within the limits of their resources, in the preparation by appropriate international standardizing bodies of international standards for products for which they either have adopted, or expect to adopt, technical regulations.
- 2.7 Members shall give positive consideration to accepting as equivalent technical regulations of other Members, even if these regulations differ from their own, provided they are satisfied that these regulations adequately fulfil the objectives of their own regulations.
- 2.8 Wherever appropriate, Members shall specify technical regulations based on product requirements in terms of performance rather than design or descriptive characteristics.
- 2.9 Whenever a relevant international standard does not exist or the technical content of a proposed technical regulation is not in accordance with the technical content of relevant international standards, and if the technical regulation may have a significant effect on trade of other Members, Members shall:
- 2.9.1 publish a notice in a publication at an early appropriate stage, in such a manner as to enable interested parties in other Members to become acquainted with it, that they propose to introduce a particular technical regulation;
 - 2.9.2 notify other Members through the Secretariat of the products to be covered by the proposed technical regulation, together with a brief indication of its objective and rationale. Such notifications shall take place at an early appropriate stage, when amendments can still be introduced and comments taken into account;
 - 2.9.3 upon request, provide to other Members particulars or copies of the proposed technical regulation and, whenever possible, identify the parts which in substance deviate from relevant international standards;
 - 2.9.4 without discrimination, allow reasonable time for other Members to make comments in writing, discuss these comments upon request, and take these written comments and the results of these discussions into account.
- 2.10 Subject to the provisions in the lead-in to paragraph 9, where urgent problems of safety, health, environmental protection or national security arise or threaten to arise for a Member, that Member may omit such of the steps enumerated in paragraph 9 as it finds necessary, provided that the Member, upon adoption of a technical regulation, shall:
- 2.10.1 notify immediately other Members through the Secretariat of the particular technical regulation and the products covered, with a brief indication of the objective and the rationale of the technical regulation, including the nature of the urgent problems;
 - 2.10.2 upon request, provide other Members with copies of the technical regulation;
 - 2.10.3 without discrimination, allow other Members to present their comments in writing, discuss these comments upon request, and take these written comments and the results of these discussions into account.
- 2.11 Members shall ensure that all technical regulations which have been adopted are published promptly or otherwise made available in such a manner as to enable interested parties in other Members to become acquainted with them.

2.12 Except in those urgent circumstances referred to in paragraph 10, Members shall allow a reasonable interval between the publication of technical regulations and their entry into force in order to allow time for producers in exporting Members, and particularly in developing country Members, to adapt their products or methods of production to the requirements of the importing Member.

Article 3

Preparation, Adoption and Application of Technical Regulations by Local Government Bodies and Non-Governmental Bodies

With respect to their local government and non-governmental bodies within their territories:

- 3.1 Members shall take such reasonable measures as may be available to them to ensure compliance by such bodies with the provisions of Article 2, with the exception of the obligation to notify as referred to in paragraphs 9.2 and 10.1 of Article 2.
- 3.2 Members shall ensure that the technical regulations of local governments on the level directly below that of the central government in Members are notified in accordance with the provisions of paragraphs 9.2 and 10.1 of Article 2, noting that notification shall not be required for technical regulations the technical content of which is substantially the same as that of previously notified technical regulations of central government bodies of the Member concerned.
- 3.3 Members may require contact with other Members, including the notifications, provision of information, comments and discussions referred to in paragraphs 9 and 10 of Article 2, to take place through the central government.
- 3.4 Members shall not take measures which require or encourage local government bodies or non-governmental bodies within their territories to act in a manner inconsistent with the provisions of Article 2.
- 3.5 Members are fully responsible under this Agreement for the observance of all provisions of Article 2. Members shall formulate and implement positive measures and mechanisms in support of the observance of the provisions of Article 2 by other than central government bodies.

Article 4

Preparation, Adoption and Application of Standards

- 4.1 Members shall ensure that their central government standardizing bodies accept and comply with the Code of Good Practice for the Preparation, Adoption and Application of Standards in Annex 3 to this Agreement (referred to in this Agreement as the "Code of Good Practice"). They shall take such reasonable measures as may be available to them to ensure that local government and non-governmental standardizing bodies within their territories, as well as regional standardizing bodies of which they or one or more bodies within their territories are members, accept and comply with this Code of Good Practice. In addition, Members shall not take measures which have the effect of, directly or indirectly, requiring or encouraging such standardizing bodies to act in a manner inconsistent with the Code of Good Practice. The obligations of Members with respect to compliance of standardizing bodies with the provisions of the Code of Good Practice shall apply irrespective of whether or not a standardizing body has accepted the Code of Good Practice.

4.2 Standardizing bodies that have accepted and are complying with the Code of Good Practice shall be acknowledged by the Members as complying with the principles of this Agreement.

CONFORMITY WITH TECHNICAL REGULATIONS AND STANDARDS

Article 5

Procedures for Assessment of Conformity by Central Government Bodies

5.1 Members shall ensure that, in cases where a positive assurance of conformity with technical regulations or standards is required, their central government bodies apply the following provisions to products originating in the territories of other Members:

- 5.1.1 conformity assessment procedures are prepared, adopted and applied so as to grant access for suppliers of like products originating in the territories of other Members under conditions no less favourable than those accorded to suppliers of like products of national origin or originating in any other country, in a comparable situation; access entails suppliers' right to an assessment of conformity under the rules of the procedure, including, when foreseen by this procedure, the possibility to have conformity assessment activities undertaken at the site of facilities and to receive the mark of the system;
- 5.1.2 conformity assessment procedures are not prepared, adopted or applied with a view to or with the effect of creating unnecessary obstacles to international trade. This means, *inter alia*, that conformity assessment procedures shall not be more strict or be applied more strictly than is necessary to give the importing Member adequate confidence that products conform with the applicable technical regulations or standards, taking account of the risks non-conformity would create.

5.2 When implementing the provisions of paragraph 1, Members shall ensure that:

- 5.2.1 conformity assessment procedures are undertaken and completed as expeditiously as possible and in a no less favourable order for products originating in the territories of other Members than for like domestic products;
- 5.2.2 the standard processing period of each conformity assessment procedure is published or that the anticipated processing period is communicated to the applicant upon request; when receiving an application, the competent body promptly examines the completeness of the documentation and informs the applicant in a precise and complete manner of all deficiencies; the competent body transmits as soon as possible the results of the assessment in a precise and complete manner to the applicant so that corrective action may be taken if necessary; even when the application has deficiencies, the competent body proceeds as far as practicable with the conformity assessment if the applicant so requests; and that, upon request, the applicant is informed of the stage of the procedure, with any delay being explained;
- 5.2.3 information requirements are limited to what is necessary to assess conformity and determine fees;
- 5.2.4 the confidentiality of information about products originating in the territories of other Members arising from or supplied in connection with such conformity assessment

procedures is respected in the same way as for domestic products and in such a manner that legitimate commercial interests are protected;

- 5.2.5 any fees imposed for assessing the conformity of products originating in the territories of other Members are equitable in relation to any fees chargeable for assessing the conformity of like products of national origin or originating in any other country, taking into account communication, transportation and other costs arising from differences between location of facilities of the applicant and the conformity assessment body;
- 5.2.6 the siting of facilities used in conformity assessment procedures and the selection of samples are not such as to cause unnecessary inconvenience to applicants or their agents;
- 5.2.7 whenever specifications of a product are changed subsequent to the determination of its conformity to the applicable technical regulations or standards, the conformity assessment procedure for the modified product is limited to what is necessary to determine whether adequate confidence exists that the product still meets the technical regulations or standards concerned;
- 5.2.8 a procedure exists to review complaints concerning the operation of a conformity assessment procedure and to take corrective action when a complaint is justified.
- 5.3 Nothing in paragraphs 1 and 2 shall prevent Members from carrying out reasonable spot checks within their territories.
- 5.4 In cases where a positive assurance is required that products conform with technical regulations or standards, and relevant guides or recommendations issued by international standardizing bodies exist or their completion is imminent, Members shall ensure that central government bodies use them, or the relevant parts of them, as a basis for their conformity assessment procedures, except where, as duly explained upon request, such guides or recommendations or relevant parts are inappropriate for the Members concerned, for, *inter alia*, such reasons as: national security requirements; the prevention of deceptive practices; protection of human health or safety, animal or plant life or health, or the environment; fundamental climatic or other geographical factors; fundamental technological or infrastructural problems.
- 5.5 With a view to harmonizing conformity assessment procedures on as wide a basis as possible, Members shall play a full part, within the limits of their resources, in the preparation by appropriate international standardizing bodies of guides and recommendations for conformity assessment procedures.
- 5.6 Whenever a relevant guide or recommendation issued by an international standardizing body does not exist or the technical content of a proposed conformity assessment procedure is not in accordance with relevant guides and recommendations issued by international standardizing bodies, and if the conformity assessment procedure may have a significant effect on trade of other Members, Members shall:
- 5.6.1 publish a notice in a publication at an early appropriate stage, in such a manner as to enable interested parties in other Members to become acquainted with it, that they propose to introduce a particular conformity assessment procedure;
- 5.6.2 notify other Members through the Secretariat of the products to be covered by the proposed conformity assessment procedure, together with a brief indication of its objective and rationale. Such notifications shall take place at an early appropriate stage, when amendments can still be introduced and comments taken into account;

- 5.6.3 upon request, provide to other Members particulars or copies of the proposed procedure and, whenever possible, identify the parts which in substance deviate from relevant guides or recommendations issued by international standardizing bodies;
- 5.6.4 without discrimination, allow reasonable time for other Members to make comments in writing, discuss these comments upon request, and take these written comments and the results of these discussions into account.
- 5.7 Subject to the provisions in the lead-in to paragraph 6, where urgent problems of safety, health, environmental protection or national security arise or threaten to arise for a Member, that Member may omit such of the steps enumerated in paragraph 6 as it finds necessary, provided that the Member, upon adoption of the procedure, shall:
- 5.7.1 notify immediately other Members through the Secretariat of the particular procedure and the products covered, with a brief indication of the objective and the rationale of the procedure, including the nature of the urgent problems;
- 5.7.2 upon request, provide other Members with copies of the rules of the procedure;
- 5.7.3 without discrimination, allow other Members to present their comments in writing, discuss these comments upon request, and take these written comments and the results of these discussions into account.
- 5.8 Members shall ensure that all conformity assessment procedures which have been adopted are published promptly or otherwise made available in such a manner as to enable interested parties in other Members to become acquainted with them.
- 5.9 Except in those urgent circumstances referred to in paragraph 7, Members shall allow a reasonable interval between the publication of requirements concerning conformity assessment procedures and their entry into force in order to allow time for producers in exporting Members, and particularly in developing country Members, to adapt their products or methods of production to the requirements of the importing Member.

Article 6

Recognition of Conformity Assessment by Central Government Bodies

With respect to their central government bodies:

- 6.1 Without prejudice to the provisions of paragraphs 3 and 4, Members shall ensure, whenever possible, that results of conformity assessment procedures in other Members are accepted, even when those procedures differ from their own, provided they are satisfied that those procedures offer an assurance of conformity with applicable technical regulations or standards equivalent to their own procedures. It is recognized that prior consultations may be necessary in order to arrive at a mutually satisfactory understanding regarding, in particular:

- 6.1.1 adequate and enduring technical competence of the relevant conformity assessment bodies in the exporting Member, so that confidence in the continued reliability of their conformity assessment results can exist; in this regard, verified compliance, for instance through accreditation, with relevant guides or recommendations issued by international standardizing bodies shall be taken into account as an indication of adequate technical competence;

- 6.1.2 limitation of the acceptance of conformity assessment results to those produced by designated bodies in the exporting Member.
- 6.2 Members shall ensure that their conformity assessment procedures permit, as far as practicable, the implementation of the provisions in paragraph 1.
- 6.3 Members are encouraged, at the request of other Members, to be willing to enter into negotiations for the conclusion of agreements for the mutual recognition of results of each other's conformity assessment procedures. Members may require that such agreements fulfil the criteria of paragraph 1 and give mutual satisfaction regarding their potential for facilitating trade in the products concerned.
- 6.4 Members are encouraged to permit participation of conformity assessment bodies located in the territories of other Members in their conformity assessment procedures under conditions no less favourable than those accorded to bodies located within their territory or the territory of any other country.

Article 7

Procedures for Assessment of Conformity by Local Government Bodies

With respect to their local government bodies within their territories:

- 7.1 Members shall take such reasonable measures as may be available to them to ensure compliance by such bodies with the provisions of Articles 5 and 6, with the exception of the obligation to notify as referred to in paragraphs 6.2 and 7.1 of Article 5.
- 7.2 Members shall ensure that the conformity assessment procedures of local governments on the level directly below that of the central government in Members are notified in accordance with the provisions of paragraphs 6.2 and 7.1 of Article 5, noting that notifications shall not be required for conformity assessment procedures the technical content of which is substantially the same as that of previously notified conformity assessment procedures of central government bodies of the Members concerned.

- 7.3 Members may require contact with other Members, including the notifications, provision of information, comments and discussions referred to in paragraphs 6 and 7 of Article 5, to take place through the central government.

- 7.4 Members shall not take measures which require or encourage local government bodies within their territories to act in a manner inconsistent with the provisions of Articles 5 and 6.

- 7.5 Members are fully responsible under this Agreement for the observance of all provisions of Articles 5 and 6. Members shall formulate and implement positive measures and mechanisms in support of the observance of the provisions of Articles 5 and 6 by other than central government bodies.

Article 8

Procedures for Assessment of Conformity by Non-Governmental Bodies

- 8.1 Members shall take such reasonable measures as may be available to them to ensure that non-governmental bodies within their territories which operate conformity assessment procedures comply with the provisions of Articles 5 and 6, with the exception of the obligation to notify proposed conformity assessment procedures. In addition, Members shall not take measures which have the effect of, directly

or indirectly, requiring or encouraging such bodies to act in a manner inconsistent with the provisions of Articles 5 and 6.

8.2 Members shall ensure that their central government bodies rely on conformity assessment procedures operated by non-governmental bodies only if these latter bodies comply with the provisions of Articles 5 and 6, with the exception of the obligation to notify proposed conformity assessment procedures.

Article 9

International and Regional Systems

9.1 Where a positive assurance of conformity with a technical regulation or standard is required, Members shall, wherever practicable, formulate and adopt international systems for conformity assessment and become members thereof or participate therein.

9.2 Members shall take such reasonable measures as may be available to them to ensure that international and regional systems for conformity assessment in which relevant bodies within their territories are members or participants comply with the provisions of Articles 5 and 6. In addition, Members shall not take any measures which have the effect of, directly or indirectly, requiring or encouraging such systems to act in a manner inconsistent with any of the provisions of Articles 5 and 6.

9.3 Members shall ensure that their central government bodies rely on international or regional conformity assessment systems only to the extent that these systems comply with the provisions of Articles 5 and 6, as applicable.

INFORMATION AND ASSISTANCE

Article 10

Information About Technical Regulations, Standards and Conformity Assessment Procedures

10.1 Each Member shall ensure that an enquiry point exists which is able to answer all reasonable enquiries from other Members and interested parties in other Members as well as to provide the relevant documents regarding:

10.1.1 any technical regulations adopted or proposed within its territory by central or local government bodies, by non-governmental bodies which have legal power to enforce a technical regulation, or by regional standardizing bodies of which such bodies are members or participants;

10.1.2 any standards adopted or proposed within its territory by central or local government bodies, or by regional standardizing bodies of which such bodies are members or participants;

10.1.3 any conformity assessment procedures, or proposed conformity assessment procedures, which are operated within its territory by central or local government bodies, or by non-governmental bodies which have legal power to enforce a technical regulation, or by regional bodies of which such bodies are members or participants;

10.1.4 the membership and participation of the Member, or of relevant central or local government bodies within its territory, in international and regional standardizing bodies and conformity assessment systems, as well as in bilateral and multilateral arrangements within the scope of this Agreement; it shall also be able to provide reasonable information on the provisions of such systems and arrangements;

10.1.5 the location of notices published pursuant to this Agreement, or the provision of information as to where such information can be obtained; and

10.1.6 the location of the enquiry points mentioned in paragraph 3.

10.2 If, however, for legal or administrative reasons more than one enquiry point is established by a Member, that Member shall provide to the other Members complete and unambiguous information on the scope of responsibility of each of these enquiry points. In addition, that Member shall ensure that any enquiries addressed to an incorrect enquiry point shall promptly be conveyed to the correct enquiry point.

10.3 Each Member shall take such reasonable measures as may be available to it to ensure that one or more enquiry points exist which are able to answer all reasonable enquiries from other Members and interested parties in other Members as well as to provide the relevant documents or information as to where they can be obtained regarding:

10.3.1 any standards adopted or proposed within its territory by non-governmental standardizing bodies, or by regional standardizing bodies of which such bodies are members or participants; and

10.3.2 any conformity assessment procedures, or proposed conformity assessment procedures, which are operated within its territory by non-governmental bodies, or by regional bodies of which such bodies are members or participants;

10.3.3 the membership and participation of relevant non-governmental bodies within its territory in international and regional standardizing bodies and conformity assessment systems, as well as in bilateral and multilateral arrangements within the scope of this Agreement; they shall also be able to provide reasonable information on the provisions of such systems and arrangements.

10.4 Members shall take such reasonable measures as may be available to them to ensure that where copies of documents are requested by other Members or by interested parties in other Members, in accordance with the provisions of this Agreement, they are supplied at an equitable price (if any) which shall, apart from the real cost of delivery, be the same for the nationals¹ of the Member concerned or of any other Member.

10.5 Developed country Members shall, if requested by other Members, provide, in English, French or Spanish, translations of the documents covered by a specific notification or, in case of voluminous documents, of summaries of such documents.

10.6 The Secretariat shall, when it receives notifications in accordance with the provisions of this Agreement, circulate copies of the notifications to all Members and interested international standardizing

¹"Nationals" here shall be deemed, in the case of a separate customs territory Member of the WTO, to mean persons, natural or legal, who are domiciled or who have a real and effective industrial or commercial establishment in that customs territory.

and conformity assessment bodies, and draw the attention of developing country Members to any notifications relating to products of particular interest to them.

10.7 Whenever a Member has reached an agreement with any other country or countries on issues related to technical regulations, standards or conformity assessment procedures which may have a significant effect on trade, at least one Member party to the agreement shall notify other Members through the Secretariat of the products to be covered by the agreement and include a brief description of the agreement. Members concerned are encouraged to enter, upon request, into consultations with other Members for the purposes of concluding similar agreements or of arranging for their participation in such agreements.

10.8 Nothing in this Agreement shall be construed as requiring:

10.8.1 the publication of texts other than in the language of the Member;

10.8.2 the provision of particulars or copies of drafts other than in the language of the Member except as stated in paragraph 5; or

10.8.3 Members to furnish any information, the disclosure of which they consider contrary to their essential security interests.

10.9 Notifications to the Secretariat shall be in English, French or Spanish.

10.10 Members shall designate a single central government authority that is responsible for the implementation on the national level of the provisions concerning notification procedures under this Agreement except those included in Annex 3.

10.11 If, however, for legal or administrative reasons the responsibility for notification procedures is divided among two or more central government authorities, the Member concerned shall provide to the other Members complete and unambiguous information on the scope of responsibility of each of these authorities.

Article 11

Technical Assistance to Other Members

11.1 Members shall, if requested, advise other Members, especially the developing country Members, on the preparation of technical regulations.

11.2 Members shall, if requested, advise other Members, especially the developing country Members, and shall grant them technical assistance on mutually agreed terms and conditions regarding the establishment of national standardizing bodies, and participation in the international standardizing bodies, and shall encourage their national standardizing bodies to do likewise.

11.3 Members shall, if requested, take such reasonable measures as may be available to them to arrange for the regulatory bodies within their territories to advise other Members, especially the developing country Members, and shall grant them technical assistance on mutually agreed terms and conditions regarding:

11.3.1 the establishment of regulatory bodies, or bodies for the assessment of conformity with technical regulations; and

11.3.2 the methods by which their technical regulations can best be met.

11.4 Members shall, if requested, take such reasonable measures as may be available to them to arrange for advice to be given to other Members, especially the developing country Members, and shall grant them technical assistance on mutually agreed terms and conditions regarding the establishment of bodies for the assessment of conformity with standards adopted within the territory of the requesting Member.

11.5 Members shall, if requested, advise other Members, especially the developing country Members, and shall grant them technical assistance on mutually agreed terms and conditions regarding the steps that should be taken by their producers if they wish to have access to systems for conformity assessment operated by governmental or non-governmental bodies within the territory of the Member receiving the request.

11.6 Members which are members or participants of international or regional systems for conformity assessment shall, if requested, advise other Members, especially the developing country Members, and shall grant them technical assistance on mutually agreed terms and conditions regarding the establishment of the institutions and legal framework which would enable them to fulfil the obligations of membership or participation in such systems.

11.7 Members shall, if so requested, encourage bodies within their territories which are members or participants of international or regional systems for conformity assessment to advise other Members, especially the developing country Members, and should consider requests for technical assistance from them regarding the establishment of the institutions which would enable the relevant bodies within their territories to fulfil the obligations of membership or participation.

11.8 In providing advice and technical assistance to other Members in terms of paragraphs 1 to 7, Members shall give priority to the needs of the least-developed country Members.

Article 12

Special and Differential Treatment of Developing Country Members

12.1 Members shall provide differential and more favourable treatment to developing country Members to this Agreement, through the following provisions as well as through the relevant provisions of other Articles of this Agreement.

12.2 Members shall give particular attention to the provisions of this Agreement concerning developing country Members' rights and obligations and shall take into account the special development, financial and trade needs of developing country Members in the implementation of this Agreement, both nationally and in the operation of this Agreement's institutional arrangements.

12.3 Members shall, in the preparation and application of technical regulations, standards and conformity assessment procedures, take account of the special development, financial and trade needs of developing country Members, with a view to ensuring that such technical regulations, standards and conformity assessment procedures do not create unnecessary obstacles to exports from developing country Members.

12.4 Members recognize that, although international standards, guides or recommendations may exist, in their particular technological and socio-economic conditions, developing country Members adopt certain technical regulations, standards or conformity assessment procedures aimed at preserving indigenous technology and production methods and processes compatible with their development needs.

Members therefore recognize that developing country Members should not be expected to use international standards as a basis for their technical regulations or standards, including test methods, which are not appropriate to their development, financial and trade needs.

12.5 Members shall take such reasonable measures as may be available to them to ensure that international standardizing bodies and international systems for conformity assessment are organized and operated in a way which facilitates active and representative participation of relevant bodies in all Members, taking into account the special problems of developing country Members.

12.6 Members shall take such reasonable measures as may be available to them to ensure that international standardizing bodies, upon request of developing country Members, examine the possibility of, and, if practicable, prepare international standards concerning products of special interest to developing country Members.

12.7 Members shall, in accordance with the provisions of Article 11, provide technical assistance to developing country Members to ensure that the preparation and application of technical regulations, standards and conformity assessment procedures do not create unnecessary obstacles to the expansion and diversification of exports from developing country Members. In determining the terms and conditions of the technical assistance, account shall be taken of the stage of development of the requesting Members and in particular of the least-developed country Members.

12.8 It is recognized that developing country Members may face special problems, including institutional and infrastructural problems, in the field of preparation and application of technical regulations, standards and conformity assessment procedures. It is further recognized that the special development and trade needs of developing country Members, as well as their stage of technological development, may hinder their ability to discharge fully their obligations under this Agreement. Members, therefore, shall take this fact fully into account. Accordingly, with a view to ensuring that developing country Members are able to comply with this Agreement, the Committee on Technical Barriers to Trade provided for in Article 13 (referred to in this Agreement as the "Committee") is enabled to grant, upon request, specified, time-limited exceptions in whole or in part from obligations under this Agreement. When considering such requests the Committee shall take into account the special problems, in the field of preparation and application of technical regulations, standards and conformity assessment procedures, and the special development and trade needs of the developing country Member, as well as its stage of technological development, which may hinder its ability to discharge fully its obligations under this Agreement. The Committee shall, in particular, take into account the special problems of the least-developed country Members.

12.9 During consultations, developed country Members shall bear in mind the special difficulties experienced by developing country Members in formulating and implementing standards and technical regulations and conformity assessment procedures, and in their desire to assist developing country Members with their efforts in this direction, developed country Members shall take account of the special needs of the former in regard to financing, trade and development.

12.10 The Committee shall examine periodically the special and differential treatment, as laid down in this Agreement, granted to developing country Members on national and international levels.

INSTITUTIONS, CONSULTATION AND DISPUTE SETTLEMENT

Article 13

The Committee on Technical Barriers to Trade

13.1 A Committee on Technical Barriers to Trade is hereby established, and shall be composed of representatives from each of the Members. The Committee shall elect its own Chairman and shall meet as necessary, but no less than once a year, for the purpose of affording Members the opportunity of consulting on any matters relating to the operation of this Agreement or the furtherance of its objectives, and shall carry out such responsibilities as assigned to it under this Agreement or by the Members.

13.2 The Committee shall establish working parties or other bodies as may be appropriate, which shall carry out such responsibilities as may be assigned to them by the Committee in accordance with the relevant provisions of this Agreement.

13.3 It is understood that unnecessary duplication should be avoided between the work under this Agreement and that of governments in other technical bodies. The Committee shall examine this problem with a view to minimizing such duplication.

Article 14

Consultation and Dispute Settlement

14.1 Consultations and the settlement of disputes with respect to any matter affecting the operation of this Agreement shall take place under the auspices of the Dispute Settlement Body and shall follow, *mutatis mutandis*, the provisions of Articles XXII and XXIII of GATT 1994, as elaborated and applied by the Dispute Settlement Understanding.

14.2 At the request of a party to a dispute, or at its own initiative, a panel may establish a technical expert group to assist in questions of a technical nature, requiring detailed consideration by experts.

14.3 Technical expert groups shall be governed by the procedures of Annex 2.

14.4 The dispute settlement provisions set out above can be invoked in cases where a Member considers that another Member has not achieved satisfactory results under Articles 3, 4, 7, 8 and 9 and its trade interests are significantly affected. In this respect, such results shall be equivalent to those as if the body in question were a Member.

FINAL PROVISIONS

Article 15

Final Provisions

Reservations

15.1 Reservations may not be entered in respect of any of the provisions of this Agreement without the consent of the other Members.

ANNEX 1

TERMS AND THEIR DEFINITIONS FOR THE
PURPOSE OF THIS AGREEMENT

The terms presented in the sixth edition of the ISO/IEC Guide 2: 1991, General Terms and Their Definitions Concerning Standardization and Related Activities, shall, when used in this Agreement, have the same meaning as given in the definitions in the said Guide taking into account that services are excluded from the coverage of this Agreement.

For the purpose of this Agreement, however, the following definitions shall apply:

1. *Technical regulation*

Document which lays down product characteristics or their related processes and production methods, including the applicable administrative provisions, with which compliance is mandatory. It may also include or deal exclusively with terminology, symbols, packaging, marking or labelling requirements as they apply to a product, process or production method.

Explanatory note

The definition in ISO/IEC Guide 2 is not self-contained, but based on the so-called "building block" system.

2. *Standard*

Document approved by a recognized body, that provides, for common and repeated use, rules, guidelines or characteristics for products or related processes and production methods, with which compliance is not mandatory. It may also include or deal exclusively with terminology, symbols, packaging, marking or labelling requirements as they apply to a product, process or production method.

Explanatory note

The terms as defined in ISO/IEC Guide 2 cover products, processes and services. This Agreement deals only with technical regulations, standards and conformity assessment procedures related to products or processes and production methods. Standards as defined by ISO/IEC Guide 2 may be mandatory or voluntary. For the purpose of this Agreement standards are defined as voluntary and technical regulations as mandatory documents. Standards prepared by the international standardization community are based on consensus. This Agreement covers also documents that are not based on consensus.

3. *Conformity assessment procedures*

Any procedure used, directly or indirectly, to determine that relevant requirements in technical regulations or standards are fulfilled.

Explanatory note

Conformity assessment procedures include, *inter alia*, procedures for sampling, testing and inspection; evaluation, verification and assurance of conformity; registration, accreditation and approval as well as their combinations.

Review

15.2 Each Member shall, promptly after the date on which the WTO Agreement enters into force for it, inform the Committee of measures in existence or taken to ensure the implementation and administration of this Agreement. Any changes of such measures thereafter shall also be notified to the Committee.

15.3 The Committee shall review annually the implementation and operation of this Agreement taking into account the objectives thereof.

15.4 Not later than the end of the third year from the date of entry into force of the WTO Agreement and at the end of each three-year period thereafter, the Committee shall review the operation and implementation of this Agreement, including the provisions relating to transparency, with a view to recommending an adjustment of the rights and obligations of this Agreement where necessary to ensure mutual economic advantage and balance of rights and obligations, without prejudice to the provisions of Article 12. Having regard, *inter alia*, to the experience gained in the implementation of the Agreement, the Committee shall, where appropriate, submit proposals for amendments to the text of this Agreement to the Council for Trade in Goods.

Annexes

15.5 The annexes to this Agreement constitute an integral part thereof.

4. *International body or system*

Body or system whose membership is open to the relevant bodies of at least all Members.

5. *Regional body or system*

Body or system whose membership is open to the relevant bodies of only some of the Members.

6. *Central government body*

Central government, its ministries and departments or any body subject to the control of the central government in respect of the activity in question.

Explanatory note:

In the case of the European Communities the provisions governing central government bodies apply. However, regional bodies or conformity assessment systems may be established within the European Communities, and in such cases would be subject to the provisions of this Agreement on regional bodies or conformity assessment systems.

7. *Local government body*

Government other than a central government (e.g. states, provinces, Länder, cantons, municipalities, etc.), its ministries or departments or any body subject to the control of such a government in respect of the activity in question.

8. *Non-governmental body*

Body other than a central government body or a local government body, including a non-governmental body which has legal power to enforce a technical regulation.

ANNEX 2

TECHNICAL EXPERT GROUPS

The following procedures shall apply to technical expert groups established in accordance with the provisions of Article 14.

1. Technical expert groups are under the panel's authority. Their terms of reference and detailed working procedures shall be decided by the panel, and they shall report to the panel.
2. Participation in technical expert groups shall be restricted to persons of professional standing and experience in the field in question.
3. Citizens of parties to the dispute shall not serve on a technical expert group without the joint agreement of the parties to the dispute, except in exceptional circumstances when the panel considers that the need for specialized scientific expertise cannot be fulfilled otherwise. Government officials of parties to the dispute shall not serve on a technical expert group. Members of technical expert groups shall serve in their individual capacities and not as government representatives, nor as representatives of any organization. Governments or organizations shall therefore not give them instructions with regard to matters before a technical expert group.
4. Technical expert groups may consult and seek information and technical advice from any source they deem appropriate. Before a technical expert group seeks such information or advice from a source within the jurisdiction of a Member, it shall inform the government of that Member. Any Member shall respond promptly and fully to any request by a technical expert group for such information as the technical expert group considers necessary and appropriate.
5. The parties to a dispute shall have access to all relevant information provided to a technical expert group, unless it is of a confidential nature. Confidential information provided to the technical expert group shall not be released without formal authorization from the government, organization or person providing the information. Where such information is requested from the technical expert group but release of such information by the technical expert group is not authorized, a non-confidential summary of the information will be provided by the government, organization or person supplying the information.
6. The technical expert group shall submit a draft report to the Members concerned with a view to obtaining their comments, and taking them into account, as appropriate, in the final report, which shall also be circulated to the Members concerned when it is submitted to the panel.

ANNEX 3

CODE OF GOOD PRACTICE FOR THE PREPARATION, ADOPTION AND APPLICATION OF STANDARDS

General Provisions

- A. For the purposes of this Code the definitions in Annex 1 of this Agreement shall apply.
- B. This Code is open to acceptance by any standardizing body within the territory of a Member of the WTO, whether a central government body, a local government body, or a non-governmental body; to any governmental regional standardizing body one or more members of which are Members of the WTO; and to any non-governmental regional standardizing body one or more members of which are situated within the territory of a Member of the WTO (referred to in this Code collectively as "standardizing bodies" and individually as "the standardizing body").
- C. Standardizing bodies that have accepted or withdrawn from this Code shall notify this fact to the ISO/IEC Information Centre in Geneva. The notification shall include the name and address of the body concerned and the scope of its current and expected standardization activities. The notification may be sent either directly to the ISO/IEC Information Centre, or through the national member body of ISO/IEC or, preferably, through the relevant national member or international affiliate of ISONET, as appropriate.

SUBSTANTIVE PROVISIONS

- D. In respect of standards, the standardizing body shall accord treatment to products originating in the territory of any other Member of the WTO no less favourable than that accorded to like products of national origin and to like products originating in any other country.
- E. The standardizing body shall ensure that standards are not prepared, adopted or applied with a view to, or with the effect of, creating unnecessary obstacles to international trade.
- F. Where international standards exist or their completion is imminent, the standardizing body shall use them, or the relevant parts of them, as a basis for the standards it develops, except where such international standards or relevant parts would be ineffective or inappropriate, for instance, because of an insufficient level of protection or fundamental climatic or geographical factors or fundamental technological problems.
- G. With a view to harmonizing standards on as wide a basis as possible, the standardizing body shall, in an appropriate way, play a full part, within the limits of its resources, in the preparation by relevant international standardizing bodies of international standards regarding subject matter for which it either has adopted, or expects to adopt, standards. For standardizing bodies within the territory of a Member, participation in a particular international standardization activity shall, whenever possible, take place through one delegation representing all standardizing bodies in the territory that have adopted, or expect to adopt, standards for the subject matter to which the international standardization activity relates.
- H. The standardizing body within the territory of a Member shall make every effort to avoid duplication of, or overlap with, the work of other standardizing bodies in the national territory or with the work of relevant international or regional standardizing bodies. They shall also make every effort to achieve a national consensus on the standards they develop. Likewise the regional standardizing

body shall make every effort to avoid duplication of, or overlap with, the work of relevant international standardizing bodies.

- I. Wherever appropriate, the standardizing body shall specify standards based on product requirements in terms of performance rather than design or descriptive characteristics.
- J. At least once every six months, the standardizing body shall publish a work programme containing its name and address, the standards it is currently preparing and the standards which it has adopted in the preceding period. A standard is under preparation from the moment a decision has been taken to develop a standard until that standard has been adopted. The titles of specific draft standards shall, upon request, be provided in English, French or Spanish. A notice of the existence of the work programme shall be published in a national or, as the case may be, regional publication of standardization activities.
- The work programme shall for each standard indicate, in accordance with any ISONET rules, the classification relevant to the subject matter, the stage attained in the standard's development, and the references of any international standards taken as a basis. No later than at the time of publication of its work programme, the standardizing body shall notify the existence thereof to the ISO/IEC Information Centre in Geneva.
- The notification shall contain the name and address of the standardizing body, the name and issue of the publication in which the work programme is published, the period to which the work programme applies, its price (if any), and how and where it can be obtained. The notification may be sent directly to the ISO/IEC Information Centre, or, preferably, through the relevant national member or international affiliate of ISONET, as appropriate.
- K. The national member of ISO/IEC shall make every effort to become a member of ISONET or to appoint another body to become a member as well as to acquire the most advanced membership type possible for the ISONET member. Other standardizing bodies shall make every effort to associate themselves with the ISONET member.
- L. Before adopting a standard, the standardizing body shall allow a period of at least 60 days for the submission of comments on the draft standard by interested parties within the territory of a Member of the WTO. This period may, however, be shortened in cases where urgent problems of safety, health or environment arise or threaten to arise. No later than at the start of the comment period, the standardizing body shall publish a notice announcing the period for commenting in the publication referred to in paragraph J. Such notification shall include, as far as practicable, whether the draft standard deviates from relevant international standards.
- M. On the request of any interested party within the territory of a Member of the WTO, the standardizing body shall promptly provide, or arrange to provide, a copy of a draft standard which it has submitted for comments. Any fees charged for this service shall, apart from the real cost of delivery, be the same for foreign and domestic parties.
- N. The standardizing body shall take into account, in the further processing of the standard, the comments received during the period for commenting. Comments received through standardizing bodies that have accepted this Code of Good Practice shall, if so requested, be replied to as promptly as possible. The reply shall include an explanation why a deviation from relevant international standards is necessary.
- O. Once the standard has been adopted, it shall be promptly published.
- P. On the request of any interested party within the territory of a Member of the WTO, the standardizing body shall promptly provide, or arrange to provide, a copy of its most recent work

programme or of a standard which it produced. Any fees charged for this service shall, apart from the real cost of delivery, be the same for foreign and domestic parties.

Q. The standardizing body shall afford sympathetic consideration to, and adequate opportunity for, consultation regarding representations with respect to the operation of this Code presented by standardizing bodies that have accepted this Code of Good Practice. It shall make an objective effort to solve any complaints.

**Agreement on Implementation of Article VI of the
General Agreement on Tariffs and Trade 1994, 1994**

**AGREEMENT ON IMPLEMENTATION OF ARTICLE VI
OF THE GENERAL AGREEMENT ON TARIFFS AND TRADE 1994**

Members hereby agree as follows:

PART I

Article 1

Principles

An anti-dumping measure shall be applied only under the circumstances provided for in Article VI of GATT 1994 and pursuant to investigations initiated¹ and conducted in accordance with the provisions of this Agreement. The following provisions govern the application of Article VI of GATT 1994 in so far as action is taken under anti-dumping legislation or regulations.

Article 2

Determination of Dumping

2.1 For the purpose of this Agreement, a product is to be considered as being dumped, i.e. introduced into the commerce of another country at less than its normal value, if the export price of the product exported from one country to another is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country.

2.2 When there are no sales of the like product in the ordinary course of trade in the domestic market of the exporting country or when, because of the particular market situation or the low volume of the sales in the domestic market of the exporting country², such sales do not permit a proper comparison, the margin of dumping shall be determined by comparison with a comparable price of the like product when exported to an appropriate third country, provided that this price is representative, or with the cost of production in the country of origin plus a reasonable amount for administrative, selling and general costs and for profits.

2.2.1 Sales of the like product in the domestic market of the exporting country or sales to a third country at prices below per unit (fixed and variable) costs of production plus administrative, selling and general costs may be treated as not being in the ordinary course of trade by reason of price and may be disregarded in determining normal value only if the authorities³ determine that such sales are made within an extended period of time⁴ in substantial

¹ The term "initiated" as used in this Agreement means the procedural action by which a Member formally commences an investigation as provided in Article 5.

² Sales of the like product destined for consumption in the domestic market of the exporting country shall normally be considered a sufficient quantity for the determination of the normal value if such sales constitute 5 per cent or more of the sales of the product under consideration to the importing Member, provided that a lower ratio should be acceptable where the evidence demonstrates that domestic sales at such lower ratio are nonetheless of sufficient magnitude to provide for a proper comparison.

³ When in this Agreement the term "authorities" is used, it shall be interpreted as meaning authorities at an appropriate senior level.

⁴ The extended period of time should normally be one year but shall in no case be less than six months.

quantities⁵ and are at prices which do not provide for the recovery of all costs within a reasonable period of time. If prices which are below per unit costs at the time of sale are above weighted average per unit costs for the period of investigation, such prices shall be considered to provide for recovery of costs within a reasonable period of time.

2.2.1.1 For the purpose of paragraph 2, costs shall normally be calculated on the basis of records kept by the exporter or producer under investigation, provided that such records are in accordance with the generally accepted accounting principles of the exporting country and reasonably reflect the costs associated with the production and sale of the product under consideration. Authorities shall consider all available evidence on the proper allocation of costs, including that which is made available by the exporter or producer in the course of the investigation provided that such allocations have been historically utilized by the exporter or producer, in particular in relation to establishing appropriate amortization and depreciation periods and allowances for capital expenditures and other development costs. Unless already reflected in the cost allocations under this sub-paragraph, costs shall be adjusted appropriately for those non-recurring items of cost which benefit future and/or current production, or for circumstances in which costs during the period of investigation are affected by start-up operations.⁶

2.2.2 For the purpose of paragraph 2, the amounts for administrative, selling and general costs and for profits shall be based on actual data pertaining to production and sales in the ordinary course of trade of the like product by the exporter or producer under investigation. When such amounts cannot be determined on this basis, the amounts may be determined on the basis of:

- (i) the actual amounts incurred and realized by the exporter or producer in question in respect of production and sales in the domestic market of the country of origin of the same general category of products;
- (ii) the weighted average of the actual amounts incurred and realized by other exporters or producers subject to investigation in respect of production and sales of the like product in the domestic market of the country of origin;
- (iii) any other reasonable method, provided that the amount for profit so established shall not exceed the profit normally realized by other exporters or producers on sales of products of the same general category in the domestic market of the country of origin.

2.3 In cases where there is no export price or where it appears to the authorities concerned that the export price is unreliable because of association or a compensatory arrangement between the exporter and the importer or a third party, the export price may be constructed on the basis of the price at which the imported products are first resold to an independent buyer, or if the products are not

⁵ Sales below per unit costs are made in substantial quantities when the authorities establish that the weighted average selling price of the transactions under consideration for the determination of the normal value is below the weighted average per unit costs, or that the volume of sales below per unit costs represents not less than 20 per cent of the volume sold in transactions under consideration for the determination of the normal value.

⁶ The adjustment made for start-up operations shall reflect the costs at the end of the start-up period or, if that period extends beyond the period of investigation, the most recent costs which can reasonably be taken into account by the authorities during the investigation.

resold to an independent buyer, or not resold in the condition as imported, on such reasonable basis as the authorities may determine.

2.4 A fair comparison shall be made between the export price and the normal value. This comparison shall be made at the same level of trade, normally at the ex-factory level, and in respect of sales made at as nearly as possible the same time. Due allowance shall be made in each case, on its merits, for differences which affect price comparability, including differences in conditions and terms of sale, taxation, levels of trade, quantities, physical characteristics, and any other differences which are also demonstrated to affect price comparability.⁷ In the cases referred to in paragraph 3, allowances for costs, including duties and taxes, incurred between importation and resale, and for profits accruing, should also be made. If in these cases price comparability has been affected, the authorities shall establish the normal value at a level of trade equivalent to the level of trade of the constructed export price, or shall make due allowance as warranted under this paragraph. The authorities shall indicate to the parties in question what information is necessary to ensure a fair comparison and shall not impose an unreasonable burden of proof on those parties.

2.4.1 When the comparison under paragraph 4 requires a conversion of currencies, such conversion should be made using the rate of exchange on the date of sale⁸, provided that when a sale of foreign currency on forward markets is directly linked to the export sale involved, the rate of exchange in the forward sale shall be used. Fluctuations in exchange rates shall be ignored and in an investigation the authorities shall allow exporters at least 60 days to have adjusted their export prices to reflect sustained movements in exchange rates during the period of investigation.

2.4.2 Subject to the provisions governing fair comparison in paragraph 4, the existence of margins of dumping during the investigation phase shall normally be established on the basis of a comparison of a weighted average normal value with a weighted average of prices of all comparable export transactions or by a comparison of normal value and export prices on a transaction-to-transaction basis. A normal value established on a weighted average basis may be compared to prices of individual export transactions if the authorities find a pattern of export prices which differ significantly among different purchasers, regions or time periods, and if an explanation is provided as to why such differences cannot be taken into account appropriately by the use of a weighted average-to-weighted average or transaction-to-transaction comparison.

2.5 In the case where products are not imported directly from the country of origin but are exported to the importing Member from an intermediate country, the price at which the products are sold from the country of export to the importing Member shall normally be compared with the comparable price in the country of export. However, comparison may be made with the price in the country of origin, if, for example, the products are merely transhipped through the country of export, or such products are not produced in the country of export, or there is no comparable price for them in the country of export.

2.6 Throughout this Agreement the term "like product" ("produit similaire") shall be interpreted to mean a product which is identical, i.e. alike in all respects to the product under consideration, or in

⁷ It is understood that some of the above factors may overlap, and authorities shall ensure that they do not duplicate adjustments that have been already made under this provision.

⁸ Normally, the date of sale would be the date of contract, purchase order, order confirmation, or invoice, whichever establishes the material terms of sale.

the absence of such a product, another product which, although not alike in all respects, has characteristics closely resembling those of the product under consideration.

2.7 This Article is without prejudice to the second Supplementary Provision to paragraph 1 of Article VI in Annex I to GATT 1994.

Article 3

Determination of Injury⁹

3.1 A determination of injury for purposes of Article VI of GATT 1994 shall be based on positive evidence and involve an objective examination of both (a) the volume of the dumped imports and the effect of the dumped imports on prices in the domestic market for like products, and (b) the consequent impact of these imports on domestic producers of such products.

3.2 With regard to the volume of the dumped imports, the investigating authorities shall consider whether there has been a significant increase in dumped imports, either in absolute terms or relative to production or consumption in the importing Member. With regard to the effect of the dumped imports on prices, the investigating authorities shall consider whether there has been a significant price undercutting by the dumped imports as compared with the price of a like product of the importing Member, or whether the effect of such imports is otherwise to depress prices to a significant degree or prevent price increases, which otherwise would have occurred, to a significant degree. No one or several of these factors can necessarily give decisive guidance.

3.3 Where imports of a product from more than one country are simultaneously subject to anti-dumping investigations, the investigating authorities may cumulatively assess the effects of such imports only if they determine that (a) the margin of dumping established in relation to the imports from each country is more than *de minimis* as defined in paragraph 8 of Article 5 and the volume of imports from each country is not negligible and (b) a cumulative assessment of the effects of the imports is appropriate in light of the conditions of competition between the imported products and the conditions of competition between the imported products and the like domestic product.

3.4 The examination of the impact of the dumped imports on the domestic industry concerned shall include an evaluation of all relevant economic factors and indices having a bearing on the state of the industry, including actual and potential decline in sales, profits, output, market share, productivity, return on investments, or utilization of capacity; factors affecting domestic prices; the magnitude of the margin of dumping; actual and potential negative effects on cash flow, inventories, employment, wages, growth, ability to raise capital or investments. This list is not exhaustive, nor can one or several of these factors necessarily give decisive guidance.

3.5 It must be demonstrated that the dumped imports are, through the effects of dumping, as set forth in paragraphs 2 and 4, causing injury within the meaning of this Agreement. The demonstration of a causal relationship between the dumped imports and the injury to the domestic industry shall be based on an examination of all relevant evidence before the authorities. The authorities shall also examine any known factors other than the dumped imports which at the same time are injuring the domestic industry, and the injuries caused by these other factors must not be attributed to the dumped imports. Factors which may be relevant in this respect include, *inter alia*, the volume and prices of imports not sold at dumping prices, contraction in demand or changes in the patterns of consumption,

⁹ Under this Agreement the term "injury" shall, unless otherwise specified, be taken to mean material injury to a domestic industry, threat of material injury to a domestic industry or material retardation of the establishment of such an industry and shall be interpreted in accordance with the provisions of this Article.

trade restrictive practices of and competition between the foreign and domestic producers, developments in technology and the export performance and productivity of the domestic industry.

3.6 The effect of the dumped imports shall be assessed in relation to the domestic production of the like product when available data permit the separate identification of that production on the basis of such criteria as the production process, producers' sales and profits. If such separate identification of that production is not possible, the effects of the dumped imports shall be assessed by the examination of the production of the narrowest group or range of products, which includes the like product, for which the necessary information can be provided.

3.7 A determination of a threat of material injury shall be based on facts and not merely on allegation, conjecture or remote possibility. The change in circumstances which would create a situation in which the dumping would cause injury must be clearly foreseen and imminent.¹⁰ In making a determination regarding the existence of a threat of material injury, the authorities should consider, *inter alia*, such factors as:

- (i) a significant rate of increase of dumped imports into the domestic market indicating the likelihood of substantially increased importation;
- (ii) sufficient freely disposable, or an imminent, substantial increase in, capacity of the exporter indicating the likelihood of substantially increased dumped exports to the importing Member's market, taking into account the availability of other export markets to absorb any additional exports;
- (iii) whether imports are entering at prices that will have a significant depressing or suppressing effect on domestic prices, and would likely increase demand for further imports; and
- (iv) inventories of the product being investigated.

No one of these factors by itself can necessarily give decisive guidance but the totality of the factors considered must lead to the conclusion that further dumped exports are imminent and that, unless protective action is taken, material injury would occur.

3.8 With respect to cases where injury is threatened by dumped imports, the application of anti-dumping measures shall be considered and decided with special care.

Article 4

Definition of Domestic Industry

4.1 For the purposes of this Agreement, the term "domestic industry" shall be interpreted as referring to the domestic producers as a whole of the like products or to those of them whose collective output of the products constitutes a major proportion of the total domestic production of those products, except that:

(i) when producers are related¹¹ to the exporters or importers or are themselves importers of the allegedly dumped product, the term "domestic industry" may be interpreted as referring to the rest of the producers;

(ii) in exceptional circumstances the territory of a Member may, for the production in question, be divided into two or more competitive markets and the producers within each market may be regarded as a separate industry if (a) the producers within such market sell all or almost all of their production of the product in question in that market, and (b) the demand in that market is not to any substantial degree supplied by producers of the product in question located elsewhere in the territory. In such circumstances, injury may be found to exist even where a major portion of the total domestic industry is not injured, provided there is a concentration of dumped imports into such an isolated market and provided further that the dumped imports are causing injury to the producers of all or almost all of the production within such market.

4.2 When the domestic industry has been interpreted as referring to the producers in a certain area, i.e. a market as defined in paragraph 1(ii), anti-dumping duties shall be levied¹² only on the products in question consigned for final consumption to that area. When the constitutional law of the importing Member does not permit the levying of anti-dumping duties on such a basis, the importing Member may levy the anti-dumping duties without limitation only if (a) the exporters shall have been given an opportunity to cease exporting at dumped prices to the area concerned or otherwise give assurances pursuant to Article 8 and adequate assurances in this regard have not been promptly given, and (b) such duties cannot be levied only on products of specific producers which supply the area in question.

4.3 Where two or more countries have reached under the provisions of paragraph 8(a) of Article XXIV of GATT 1994 such a level of integration that they have the characteristics of a single, unified market, the industry in the entire area of integration shall be taken to be the domestic industry referred to in paragraph 1.

4.4 The provisions of paragraph 6 of Article 3 shall be applicable to this Article.

Article 5

Initiation and Subsequent Investigation

5.1 Except as provided for in paragraph 6, an investigation to determine the existence, degree and effect of any alleged dumping shall be initiated upon a written application by or on behalf of the domestic industry.

5.2 An application under paragraph 1 shall include evidence of (a) dumping, (b) injury within the meaning of Article VI of GATT 1994 as interpreted by this Agreement and (c) a causal link between the dumped imports and the alleged injury. Simple assertion, unsubstantiated by relevant evidence,

¹¹ For the purpose of this paragraph, producers shall be deemed to be related to exporters or importers only if (a) one of them directly or indirectly controls the other; or (b) both of them are directly or indirectly controlled by a third person; or (c) together they directly or indirectly control a third person, provided that there are grounds for believing or suspecting that the effect of the relationship is such as to cause the producer concerned to behave differently from non-related producers. For the purpose of this paragraph, one shall be deemed to control another when the former is legally or operationally in a position to exercise restraint or direction over the latter.

¹² As used in this Agreement "levy" shall mean the definitive or final legal assessment or collection of a duty or tax.

¹⁰ One example, though not an exclusive one, is that there is convincing reason to believe that there will be, in the near future, substantially increased importation of the product at dumped prices.

cannot be considered sufficient to meet the requirements of this paragraph. The application shall contain such information as is reasonably available to the applicant on the following:

- (i) the identity of the applicant and a description of the volume and value of the domestic production of the like product by the applicant. Where a written application is made on behalf of the domestic industry, the application shall identify the industry on behalf of which the application is made by a list of all known domestic producers of the like product (or associations of domestic producers of the like product) and, to the extent possible, a description of the volume and value of domestic production of the like product accounted for by such producers;
- (ii) a complete description of the allegedly dumped product, the names of the country or countries of origin or export in question, the identity of each known exporter or foreign producer and a list of known persons importing the product in question;
- (iii) information on prices at which the product in question is sold when destined for consumption in the domestic markets of the country or countries of origin or export (or, where appropriate, information on the prices at which the product is sold from the country or countries of origin or export to a third country or countries, or on the constructed value of the product) and information on export prices or, where appropriate, on the prices at which the product is first resold to an independent buyer in the territory of the importing Member;
- (iv) information on the evolution of the volume of the allegedly dumped imports, the effect of these imports on prices of the like product in the domestic market and the consequent impact of the imports on the domestic industry, as demonstrated by relevant factors and indices having a bearing on the state of the domestic industry, such as those listed in paragraphs 2 and 4 of Article 3.

5.3 The authorities shall examine the accuracy and adequacy of the evidence provided in the application to determine whether there is sufficient evidence to justify the initiation of an investigation.

5.4 An investigation shall not be initiated pursuant to paragraph 1 unless the authorities have determined, on the basis of an examination of the degree of support for, or opposition to, the application expressed¹³ by domestic producers of the like product, that the application has been made by or on behalf of the domestic industry.¹⁴ The application shall be considered to have been made "by or on behalf of the domestic industry" if it is supported by those domestic producers whose collective output constitutes more than 50 per cent of the total production of the like product produced by that portion of the domestic industry expressing either support for or opposition to the application. However, no investigation shall be initiated when domestic producers expressly supporting the application account for less than 25 per cent of total production of the like product produced by the domestic industry.

5.5 The authorities shall avoid, unless a decision has been made to initiate an investigation, any publicizing of the application for the initiation of an investigation. However, after receipt of a properly documented application and before proceeding to initiate an investigation, the authorities shall notify the government of the exporting Member concerned.

¹³ In the case of fragmented industries involving an exceptionally large number of producers, authorities may determine support and opposition by using statistically valid sampling techniques.

¹⁴ Members are aware that in the territory of certain Members employees of domestic producers of the like product or representatives of those employees may make or support an application for an investigation under paragraph 1.

5.6 If, in special circumstances, the authorities concerned decide to initiate an investigation without having received a written application by or on behalf of a domestic industry for the initiation of such investigation, they shall proceed only if they have sufficient evidence of dumping, injury and a causal link, as described in paragraph 2, to justify the initiation of an investigation.

5.7 The evidence of both dumping and injury shall be considered simultaneously (a) in the decision whether or not to initiate an investigation, and (b) thereafter, during the course of the investigation, starting on a date not later than the earliest date on which in accordance with the provisions of this Agreement provisional measures may be applied.

5.8 An application under paragraph 1 shall be rejected and an investigation shall be terminated promptly as soon as the authorities concerned are satisfied that there is not sufficient evidence of either dumping or of injury to justify proceeding with the case. There shall be immediate termination in cases where the authorities determine that the margin of dumping is *de minimis*, or that the volume of dumped imports, actual or potential, or the injury, is negligible. The margin of dumping shall be considered to be *de minimis* if this margin is less than 2 per cent, expressed as a percentage of the export price. The volume of dumped imports shall normally be regarded as negligible if the volume of dumped imports from a particular country is found to account for less than 3 per cent of imports of the like product in the importing Member, unless countries which individually account for less than 3 per cent of the imports of the like product in the importing Member collectively account for more than 7 per cent of imports of the like product in the importing Member.

5.9 An anti-dumping proceeding shall not hinder the procedures of customs clearance.

5.10 Investigations shall, except in special circumstances, be concluded within one year, and in no case more than 18 months, after their initiation.

Article 6

Evidence

6.1 All interested parties in an anti-dumping investigation shall be given notice of the information which the authorities require and ample opportunity to present in writing all evidence which they consider relevant in respect of the investigation in question.

6.1.1 Exporters or foreign producers receiving questionnaires used in an anti-dumping investigation shall be given at least 30 days for reply.¹⁵ Due consideration should be given to any request for an extension of the 30-day period and, upon cause shown, such an extension should be granted whenever practicable.

6.1.2 Subject to the requirement to protect confidential information, evidence presented in writing by one interested party shall be made available promptly to other interested parties participating in the investigation.

6.1.3 As soon as an investigation has been initiated, the authorities shall provide the full text of the written application received under paragraph 1 of Article 5

¹⁵ As a general rule, the time-limit for exporters shall be counted from the date of receipt of the questionnaire, which for this purpose shall be deemed to have been received one week from the date on which it was sent to the respondent or transmitted to the appropriate diplomatic representative of the exporting Member or, in the case of a separate customs territory Member of the WTO, an official representative of the exporting territory.

to the known exporters¹⁶ and to the authorities of the exporting Member and shall make it available, upon request, to other interested parties involved. Due regard shall be paid to the requirement for the protection of confidential information, as provided for in paragraph 5.

6.2 Throughout the anti-dumping investigation all interested parties shall have a full opportunity for the defence of their interests. To this end, the authorities shall, on request, provide opportunities for all interested parties to meet those parties with adverse interests, so that opposing views may be presented and rebuttal arguments offered. Provision of such opportunities must take account of the need to preserve confidentiality and of the convenience to the parties. There shall be no obligation on any party to attend a meeting, and failure to do so shall not be prejudicial to that party's case. Interested parties shall also have the right, on justification, to present other information orally.

6.3 Oral information provided under paragraph 2 shall be taken into account by the authorities only in so far as it is subsequently reproduced in writing and made available to other interested parties, as provided for in subparagraph 1.2.

6.4 The authorities shall whenever practicable provide timely opportunities for all interested parties to see all information that is relevant to the presentation of their cases, that is not confidential as defined in paragraph 5, and that is used by the authorities in an anti-dumping investigation, and to prepare presentations on the basis of this information.

6.5 Any information which is by nature confidential (for example, because its disclosure would be of significant competitive advantage to a competitor or because its disclosure would have a significantly adverse effect upon a person supplying the information or upon a person from whom that person acquired the information), or which is provided on a confidential basis by parties to an investigation shall, upon good cause shown, be treated as such by the authorities. Such information shall not be disclosed without specific permission of the party submitting it.¹⁷

6.5.1 The authorities shall require interested parties providing confidential information to furnish non-confidential summaries thereof. These summaries shall be in sufficient detail to permit a reasonable understanding of the substance of the information submitted in confidence. In exceptional circumstances, such parties may indicate that such information is not susceptible of summary. In such exceptional circumstances, a statement of the reasons why summarization is not possible must be provided.

6.5.2 If the authorities find that a request for confidentiality is not warranted and if the supplier of the information is either unwilling to make the information public or to authorize its disclosure in generalized or summary form, the authorities may disregard such information unless it can be demonstrated to their satisfaction from appropriate sources that the information is correct.¹⁸

6.6 Except in circumstances provided for in paragraph 8, the authorities shall during the course of an investigation satisfy themselves as to the accuracy of the information supplied by interested parties upon which their findings are based.

¹⁶ It being understood that, where the number of exporters involved is particularly high, the full text of the written application should instead be provided only to the authorities of the exporting Member or to the relevant trade association.

¹⁷ Members are aware that in the territory of certain Members disclosure pursuant to a narrowly-drawn protective order may be required.

¹⁸ Members agree that requests for confidentiality should not be arbitrarily rejected.

6.7 In order to verify information provided or to obtain further details, the authorities may carry out investigations in the territory of other Members as required, provided they obtain the agreement of the firms concerned and notify the representatives of the government of the Member in question, and unless that Member objects to the investigation. The procedures described in Annex I shall apply to investigations carried out in the territory of other Members. Subject to the requirement to protect confidential information, the authorities shall make the results of any such investigations available, or shall provide disclosure thereof pursuant to paragraph 9, to the firms to which they pertain and may make such results available to the applicants.

6.8 In cases in which any interested party refuses access to, or otherwise does not provide, necessary information within a reasonable period or significantly impedes the investigation, preliminary and final determinations, affirmative or negative, may be made on the basis of the facts available. The provisions of Annex II shall be observed in the application of this paragraph.

6.9 The authorities shall, before a final determination is made, inform all interested parties of the essential facts under consideration which form the basis for the decision whether to apply definitive measures. Such disclosure should take place in sufficient time for the parties to defend their interests.

6.10 The authorities shall, as a rule, determine an individual margin of dumping for each known exporter or producer concerned of the product under investigation. In cases where the number of exporters, producers, importers or types of products involved is so large as to make such a determination impracticable, the authorities may limit their examination either to a reasonable number of interested parties or products by using samples which are statistically valid on the basis of information available to the authorities at the time of the selection, or to the largest percentage of the volume of the exports from the country in question which can reasonably be investigated.

6.10.1 Any selection of exporters, producers, importers or types of products made under this paragraph shall preferably be chosen in consultation with and with the consent of the exporters, producers or importers concerned.

6.10.2 In cases where the authorities have limited their examination, as provided for in this paragraph, they shall nevertheless determine an individual margin of dumping for any exporter or producer not initially selected who submits the necessary information in time for that information to be considered during the course of the investigation, except where the number of exporters or producers is so large that individual examinations would be unduly burdensome to the authorities and prevent the timely completion of the investigation. Voluntary responses shall not be discouraged.

6.11 For the purposes of this Agreement, "interested parties" shall include:

- (i) an exporter or foreign producer or the importer of a product subject to investigation, or a trade or business association a majority of the members of which are producers, exporters or importers of such product;
- (ii) the government of the exporting Member; and
- (iii) a producer of the like product in the importing Member or a trade and business association a majority of the members of which produce the like product in the territory of the importing Member.

This list shall not preclude Members from allowing domestic or foreign parties other than those mentioned above to be included as interested parties.

6.12 The authorities shall provide opportunities for industrial users of the product under investigation, and for representative consumer organizations in cases where the product is commonly sold at the retail level, to provide information which is relevant to the investigation regarding dumping, injury and causality.

6.13 The authorities shall take due account of any difficulties experienced by interested parties, in particular small companies, in supplying information requested, and shall provide any assistance practicable.

6.14 The procedures set out above are not intended to prevent the authorities of a Member from proceeding expeditiously with regard to initiating an investigation, reaching preliminary or final determinations, whether affirmative or negative, or from applying provisional or final measures, in accordance with relevant provisions of this Agreement.

Article 7

Provisional Measures

7.1 Provisional measures may be applied only if:

- (i) an investigation has been initiated in accordance with the provisions of Article 5, a public notice has been given to that effect and interested parties have been given adequate opportunities to submit information and make comments;
- (ii) a preliminary affirmative determination has been made of dumping and consequent injury to a domestic industry; and
- (iii) the authorities concerned judge such measures necessary to prevent injury being caused during the investigation.

7.2 Provisional measures may take the form of a provisional duty or, preferably, a security - by cash deposit or bond - equal to the amount of the anti-dumping duty provisionally estimated, being not greater than the provisionally estimated margin of dumping. Withholding of appraisement is an appropriate provisional measure, provided that the normal duty and the estimated amount of the anti-dumping duty be indicated and as long as the withholding of appraisement is subject to the same conditions as other provisional measures.

7.3 Provisional measures shall not be applied sooner than 60 days from the date of initiation of the investigation.

7.4 The application of provisional measures shall be limited to as short a period as possible, not exceeding four months or, on decision of the authorities concerned, upon request by exporters representing a significant percentage of the trade involved, to a period not exceeding six months. When authorities, in the course of an investigation, examine whether a duty lower than the margin of dumping would be sufficient to remove injury, these periods may be six and nine months, respectively.

7.5 The relevant provisions of Article 9 shall be followed in the application of provisional measures.

Article 8

Price Undertakings

8.1 Proceedings may¹⁹ be suspended or terminated without the imposition of provisional measures or anti-dumping duties upon receipt of satisfactory voluntary undertakings from any exporter to revise its prices or to cease exports to the area in question at dumped prices so that the authorities are satisfied that the injurious effect of the dumping is eliminated. Price increases under such undertakings shall not be higher than necessary to eliminate the margin of dumping. It is desirable that the price increases be less than the margin of dumping if such increases would be adequate to remove the injury to the domestic industry.

8.2 Price undertakings shall not be sought or accepted from exporters unless the authorities of the importing Member have made a preliminary affirmative determination of dumping and injury caused by such dumping.

8.3 Undertakings offered need not be accepted if the authorities consider their acceptance impractical, for example, if the number of actual or potential exporters is too great, or for other reasons, including reasons of general policy. Should the case arise and where practicable, the authorities shall provide to the exporter the reasons which have led them to consider acceptance of an undertaking as inappropriate, and shall, to the extent possible, give the exporter an opportunity to make comments thereon.

8.4 If an undertaking is accepted, the investigation of dumping and injury shall nevertheless be completed if the exporter so desires or the authorities so decide. In such a case, if a negative determination of dumping or injury is made, the undertaking shall automatically lapse, except in cases where such a determination is due in large part to the existence of a price undertaking. In such cases, the authorities may require that an undertaking be maintained for a reasonable period consistent with the provisions of this Agreement. In the event that an affirmative determination of dumping and injury is made, the undertaking shall continue consistent with its terms and the provisions of this Agreement.

8.5 Price undertakings may be suggested by the authorities of the importing Member, but no exporter shall be forced to enter into such undertakings. The fact that exporters do not offer such undertakings, or do not accept an invitation to do so, shall in no way prejudice the consideration of the case. However, the authorities are free to determine that a threat of injury is more likely to be realized if the dumped imports continue.

8.6 Authorities of an importing Member may require any exporter from whom an undertaking has been accepted to provide periodically information relevant to the fulfilment of such an undertaking and to permit verification of pertinent data. In case of violation of an undertaking, the authorities of the importing Member may take, under this Agreement in conformity with its provisions, expeditious actions which may constitute immediate application of provisional measures using the best information available. In such cases, definitive duties may be levied in accordance with this Agreement on products entered for consumption not more than 90 days before the application of such provisional measures, except that any such retroactive assessment shall not apply to imports entered before the violation of the undertaking.

¹⁹ The word "may" shall not be interpreted to allow the simultaneous continuation of proceedings with the implementation of price undertakings except as provided in paragraph 4.

Article 9

Imposition and Collection of Anti-Dumping Duties

9.1 The decision whether or not to impose an anti-dumping duty in cases where all requirements for the imposition have been fulfilled, and the decision whether the amount of the anti-dumping duty to be imposed shall be the full margin of dumping or less, are decisions to be made by the authorities of the importing Member. It is desirable that the imposition be permissive in the territory of all Members, and that the duty be less than the margin if such lesser duty would be adequate to remove the injury to the domestic industry.

9.2 When an anti-dumping duty is imposed in respect of any product, such anti-dumping duty shall be collected in the appropriate amounts in each case, on a non-discriminatory basis on imports of such product from all sources found to be dumped and causing injury, except as to imports from those sources from which price undertakings under the terms of this Agreement have been accepted. The authorities shall name the supplier or suppliers of the product concerned. If, however, several suppliers from the same country are involved, and it is impracticable to name all these suppliers, the authorities may name the supplying country concerned. If several suppliers from more than one country are involved, the authorities may name either all the suppliers involved, or, if this is impracticable, all the supplying countries involved.

9.3 The amount of the anti-dumping duty shall not exceed the margin of dumping as established under Article 2.

9.3.1 When the amount of the anti-dumping duty is assessed on a retrospective basis, the determination of the final liability for payment of anti-dumping duties shall take place as soon as possible, normally within 12 months, and in no case more than 18 months, after the date on which a request for a final assessment of the amount of the anti-dumping duty has been made.²⁰ Any refund shall be made promptly and normally in not more than 90 days following the determination of final liability made pursuant to this sub-paragraph. In any case, where a refund is not made within 90 days, the authorities shall provide an explanation if so requested.

9.3.2 When the amount of the anti-dumping duty is assessed on a prospective basis, provision shall be made for a prompt refund, upon request, of any duty paid in excess of the margin of dumping. A refund of any such duty paid in excess of the actual margin of dumping shall normally take place within 12 months, and in no case more than 18 months, after the date on which a request for a refund, duly supported by evidence, has been made by an importer of the product subject to the anti-dumping duty. The refund authorized should normally be made within 90 days of the above-noted decision.

9.3.3 In determining whether and to what extent a reimbursement should be made when the export price is constructed in accordance with paragraph 3 of Article 2, authorities should take account of any change in normal value, any change in costs incurred between importation and resale, and any movement in the resale price which is duly reflected in subsequent selling prices, and should calculate the export price with no deduction for the amount of anti-dumping duties paid when conclusive evidence of the above is provided.

9.4 When the authorities have limited their examination in accordance with the second sentence of paragraph 10 of Article 6, any anti-dumping duty applied to imports from exporters or producers not included in the examination shall not exceed:

- (i) the weighted average margin of dumping established with respect to the selected exporters or producers or,
- (ii) where the liability for payment of anti-dumping duties is calculated on the basis of a prospective normal value, the difference between the weighted average normal value of the selected exporters or producers and the export prices of exporters or producers not individually examined,

provided that the authorities shall disregard for the purpose of this paragraph any zero and *de minimis* margins and margins established under the circumstances referred to in paragraph 8 of Article 6. The authorities shall apply individual duties or normal values to imports from any exporter or producer not included in the examination who has provided the necessary information during the course of the investigation, as provided for in subparagraph 10.2 of Article 6.

9.5 If a product is subject to anti-dumping duties in an importing Member, the authorities shall promptly carry out a review for the purpose of determining individual margins of dumping for any exporters or producers in the exporting country in question who have not exported the product to the importing Member during the period of investigation, provided that these exporters or producers can show that they are not related to any of the exporters or producers in the exporting country who are subject to the anti-dumping duties on the product. Such a review shall be initiated and carried out on an accelerated basis, compared to normal duty assessment and review proceedings in the importing Member. No anti-dumping duties shall be levied on imports from such exporters or producers while the review is being carried out. The authorities may, however, withhold appraisal and/or request guarantees to ensure that, should such a review result in a determination of dumping in respect of such producers or exporters, anti-dumping duties can be levied retroactively to the date of the initiation of the review.

Article 10

Retroactivity

10.1 Provisional measures and anti-dumping duties shall only be applied to products which enter for consumption after the time when the decision taken under paragraph 1 of Article 7 and paragraph 1 of Article 9, respectively, enters into force, subject to the exceptions set out in this Article.

10.2 Where a final determination of injury (but not of a threat thereof or of a material retardation of the establishment of an industry) is made or, in the case of a final determination of a threat of injury, where the effect of the dumped imports would, in the absence of the provisional measures, have led to a determination of injury, anti-dumping duties may be levied retroactively for the period for which provisional measures, if any, have been applied.

10.3 If the definitive anti-dumping duty is higher than the provisional duty paid or payable, or the amount estimated for the purpose of the security, the difference shall not be collected. If the definitive duty is lower than the provisional duty paid or payable, or the amount estimated for the purpose of the security, the difference shall be reimbursed or the duty recalculated, as the case may be.

²⁰ It is understood that the observance of the time-limits mentioned in this subparagraph and in subparagraph 3.2 may not be possible where the product in question is subject to judicial review proceedings.

10.4 Except as provided in paragraph 2, where a determination of threat of injury or material retardation is made (but no injury has yet occurred) a definitive anti-dumping duty may be imposed only from the date of the determination of threat of injury or material retardation, and any cash deposit made during the period of the application of provisional measures shall be refunded and any bonds released in an expeditious manner.

10.5 Where a final determination is negative, any cash deposit made during the period of the application of provisional measures shall be refunded and any bonds released in an expeditious manner.

10.6 A definitive anti-dumping duty may be levied on products which were entered for consumption not more than 90 days prior to the date of application of provisional measures, when the authorities determine for the dumped product in question that:

- (i) there is a history of dumping which caused injury or that the importer was, or should have been, aware that the exporter practises dumping and that such dumping would cause injury, and
- (ii) the injury is caused by massive dumped imports of a product in a relatively short time which in light of the timing and the volume of the dumped imports and other circumstances (such as a rapid build-up of inventories of the imported product) is likely to seriously undermine the remedial effect of the definitive anti-dumping duty to be applied, provided that the importers concerned have been given an opportunity to comment.

10.7 The authorities may, after initiating an investigation, take such measures as the withholding of appraisal or assessment as may be necessary to collect anti-dumping duties retroactively, as provided for in paragraph 6, once they have sufficient evidence that the conditions set forth in that paragraph are satisfied.

10.8 No duties shall be levied retroactively pursuant to paragraph 6 on products entered for consumption prior to the date of initiation of the investigation.

Article 11

Duration and Review of Anti-Dumping Duties and Price Undertakings

11.1 An anti-dumping duty shall remain in force only as long as and to the extent necessary to counteract dumping which is causing injury.

11.2 The authorities shall review the need for the continued imposition of the duty, where warranted, on their own initiative or, provided that a reasonable period of time has elapsed since the imposition of the definitive anti-dumping duty, upon request by any interested party which submits positive information substantiating the need for a review.²¹ Interested parties shall have the right to request the authorities to examine whether the continued imposition of the duty is necessary to offset dumping, whether the injury would be likely to continue or recur if the duty were removed or varied, or both. If, as a result of the review under this paragraph, the authorities determine that the anti-dumping duty is no longer warranted, it shall be terminated immediately.

²¹ A determination of final liability for payment of anti-dumping duties, as provided for in paragraph 3 of Article 9, does not by itself constitute a review within the meaning of this Article.

11.3 Notwithstanding the provisions of paragraphs 1 and 2, any definitive anti-dumping duty shall be terminated on a date not later than five years from its imposition (or from the date of the most recent review under paragraph 2 if that review has covered both dumping and injury, or under this paragraph), unless the authorities determine, in a review initiated before that date on their own initiative or upon a duly substantiated request made by or on behalf of the domestic industry within a reasonable period of time prior to that date, that the expiry of the duty would be likely to lead to continuation or recurrence of dumping and injury.²² The duty may remain in force pending the outcome of such a review.

11.4 The provisions of Article 6 regarding evidence and procedure shall apply to any review carried out under this Article. Any such review shall be carried out expeditiously and shall normally be concluded within 12 months of the date of initiation of the review.

11.5 The provisions of this Article shall apply *mutatis mutandis* to price undertakings accepted under Article 8.

Article 12

Public Notice and Explanation of Determinations

12.1 When the authorities are satisfied that there is sufficient evidence to justify the initiation of an anti-dumping investigation pursuant to Article 5, the Member or Members the products of which are subject to such investigation and other interested parties known to the investigating authorities to have an interest therein shall be notified and a public notice shall be given.

12.1.1 A public notice of the initiation of an investigation shall contain, or otherwise make available through a separate report²³, adequate information on the following:

- (i) the name of the exporting country or countries and the product involved;
- (ii) the date of initiation of the investigation;
- (iii) the basis on which dumping is alleged in the application;
- (iv) a summary of the factors on which the allegation of injury is based;
- (v) the address to which representations by interested parties should be directed;
- (vi) the time-limits allowed to interested parties for making their views known.

12.2 Public notice shall be given of any preliminary or final determination, whether affirmative or negative, of any decision to accept an undertaking pursuant to Article 8, of the termination of such an undertaking, and of the termination of a definitive anti-dumping duty. Each such notice shall set forth, or otherwise make available through a separate report, in sufficient detail the findings and conclusions reached on all issues of fact and law considered material by the investigating authorities. All such notices and reports shall be forwarded to the Member or Members the products of which are

²² When the amount of the anti-dumping duty is assessed on a retrospective basis, a finding in the most recent assessment proceeding under subparagraph 3.1 of Article 9 that no duty is to be levied shall not by itself require the authorities to terminate the definitive duty.

²³ Where authorities provide information and explanations under the provisions of this Article in a separate report, they shall ensure that such report is readily available to the public.

subject to such determination or undertaking and to other interested parties known to have an interest therein.

12.2.1

A public notice of the imposition of provisional measures shall set forth, or otherwise make available through a separate report, sufficiently detailed explanations for the preliminary determinations on dumping and injury and shall refer to the matters of fact and law which have led to arguments being accepted or rejected. Such a notice or report shall, due regard being paid to the requirement for the protection of confidential information, contain in particular:

- (i) the names of the suppliers, or when this is impracticable, the supplying countries involved;
- (ii) a description of the product which is sufficient for customs purposes;
- (iii) the margins of dumping established and a full explanation of the reasons for the methodology used in the establishment and comparison of the export price and the normal value under Article 2;
- (iv) considerations relevant to the injury determination as set out in Article 3;
- (v) the main reasons leading to the determination.

12.2.2

A public notice of conclusion or suspension of an investigation in the case of an affirmative determination providing for the imposition of a definitive duty or the acceptance of a price undertaking shall contain, or otherwise make available through a separate report, all relevant information on the matters of fact and law and reasons which have led to the imposition of final measures or the acceptance of a price undertaking, due regard being paid to the requirement for the protection of confidential information. In particular, the notice or report shall contain the information described in subparagraph 2.1, as well as the reasons for the acceptance or rejection of relevant arguments or claims made by the exporters and importers, and the basis for any decision made under subparagraph 10.2 of Article 6.

12.2.3

A public notice of the termination or suspension of an investigation following the acceptance of an undertaking pursuant to Article 8 shall include, or otherwise make available through a separate report, the non-confidential part of this undertaking.

12.3 The provisions of this Article shall apply *mutatis mutandis* to the initiation and completion of reviews pursuant to Article 11 and to decisions under Article 10 to apply duties retroactively.

Article 13

Judicial Review

Each Member whose national legislation contains provisions on anti-dumping measures shall maintain judicial, arbitral or administrative tribunals or procedures for the purpose, *inter alia*, of the prompt review of administrative actions relating to final determinations and reviews of determinations within the meaning of Article 11. Such tribunals or procedures shall be independent of the authorities responsible for the determination or review in question.

Article 14

Anti-Dumping Action on Behalf of a Third Country

14.1 An application for anti-dumping action on behalf of a third country shall be made by the authorities of the third country requesting action.

14.2 Such an application shall be supported by price information to show that the imports are being dumped and by detailed information to show that the alleged dumping is causing injury to the domestic industry concerned in the third country. The government of the third country shall afford all assistance to the authorities of the importing country to obtain any further information which the latter may require.

14.3 In considering such an application, the authorities of the importing country shall consider the effects of the alleged dumping on the industry concerned as a whole in the third country; that is to say, the injury shall not be assessed in relation only to the effect of the alleged dumping on the industry's exports to the importing country or even on the industry's total exports.

14.4 The decision whether or not to proceed with a case shall rest with the importing country. If the importing country decides that it is prepared to take action, the initiation of the approach to the Council for Trade in Goods seeking its approval for such action shall rest with the importing country.

Article 15

Developing Country Members

It is recognized that special regard must be given by developed country Members to the special situation of developing country Members when considering the application of anti-dumping measures under this Agreement. Possibilities of constructive remedies provided for by this Agreement shall be explored before applying anti-dumping duties where they would affect the essential interests of developing country Members.

PART II

Article 16

Committee on Anti-Dumping Practices

16.1 There is hereby established a Committee on Anti-Dumping Practices (referred to in this Agreement as the "Committee") composed of representatives from each of the Members. The Committee shall elect its own Chairman and shall meet not less than twice a year and otherwise as envisaged by relevant provisions of this Agreement at the request of any Member. The Committee shall carry out responsibilities as assigned to it under this Agreement or by the Members and it shall afford Members the opportunity of consulting on any matters relating to the operation of the Agreement or the furtherance of its objectives. The WTO Secretariat shall act as the secretariat to the Committee.

16.2 The Committee may set up subsidiary bodies as appropriate.

16.3 In carrying out their functions, the Committee and any subsidiary bodies may consult with and seek information from any source they deem appropriate. However, before the Committee or a

subsidiary body seeks such information from a source within the jurisdiction of a Member, it shall inform the Member involved. It shall obtain the consent of the Member and any firm to be consulted.

16.4 Members shall report without delay to the Committee all preliminary or final anti-dumping actions taken. Such reports shall be available in the Secretariat for inspection by other Members. Members shall also submit, on a semi-annual basis, reports of any anti-dumping actions taken within the preceding six months. The semi-annual reports shall be submitted on an agreed standard form.

16.5 Each Member shall notify the Committee (a) which of its authorities are competent to initiate and conduct investigations referred to in Article 5 and (b) its domestic procedures governing the initiation and conduct of such investigations.

Article 17

Consultation and Dispute Settlement

17.1 Except as otherwise provided herein, the Dispute Settlement Understanding is applicable to consultations and the settlement of disputes under this Agreement.

17.2 Each Member shall afford sympathetic consideration to, and shall afford adequate opportunity for consultation regarding, representations made by another Member with respect to any matter affecting the operation of this Agreement.

17.3 If any Member considers that any benefit accruing to it, directly or indirectly, under this Agreement is being nullified or impaired, or that the achievement of any objective is being impeded, by another Member or Members, it may, with a view to reaching a mutually satisfactory resolution of the matter, request in writing consultations with the Member or Members in question. Each Member shall afford sympathetic consideration to any request from another Member for consultation.

17.4 If the Member that requested consultations considers that the consultations pursuant to paragraph 3 have failed to achieve a mutually agreed solution, and if final action has been taken by the administering authorities of the importing Member to levy definitive anti-dumping duties or to accept price undertakings, it may refer the matter to the Dispute Settlement Body ("DSB"). When a provisional measure has a significant impact and the Member that requested consultations considers that the measure was taken contrary to the provisions of paragraph 1 of Article 7, that Member may also refer such matter to the DSB.

17.5 The DSB shall, at the request of the complaining party, establish a panel to examine the matter based upon:

- (i) a written statement of the Member making the request indicating how a benefit accruing to it, directly or indirectly, under this Agreement has been nullified or impaired, or that the achieving of the objectives of the Agreement is being impeded, and
- (ii) the facts made available in conformity with appropriate domestic procedures to the authorities of the importing Member.

17.6 In examining the matter referred to in paragraph 5:

- (i) in its assessment of the facts of the matter, the panel shall determine whether the authorities' establishment of the facts was proper and whether their evaluation of those facts was unbiased and objective. If the establishment of the facts was proper

and the evaluation was unbiased and objective, even though the panel might have reached a different conclusion, the evaluation shall not be overturned;

- (ii) the panel shall interpret the relevant provisions of the Agreement in accordance with customary rules of interpretation of public international law. Where the panel finds that a relevant provision of the Agreement admits of more than one permissible interpretation, the panel shall find the authorities' measure to be in conformity with the Agreement if it rests upon one of those permissible interpretations.

17.7 Confidential information provided to the panel shall not be disclosed without formal authorization from the person, body or authority providing such information. Where such information is requested from the panel but release of such information by the panel is not authorized, a non-confidential summary of the information, authorized by the person, body or authority providing the information, shall be provided.

PART III

Article 18

Final Provisions

18.1 No specific action against dumping of exports from another Member can be taken except in accordance with the provisions of GATT 1994, as interpreted by this Agreement.²⁴

18.2 Reservations may not be entered in respect of any of the provisions of this Agreement without the consent of the other Members.

18.3 Subject to subparagraphs 3.1 and 3.2, the provisions of this Agreement shall apply to investigations, and reviews of existing measures, initiated pursuant to applications which have been made on or after the date of entry into force for a Member of the WTO Agreement.

18.3.1 With respect to the calculation of margins of dumping in refund procedures under paragraph 3 of Article 9, the rules used in the most recent determination or review of dumping shall apply.

18.3.2 For the purposes of paragraph 3 of Article 11, existing anti-dumping measures shall be deemed to be imposed on a date not later than the date of entry into force for a Member of the WTO Agreement, except in cases in which the domestic legislation of a Member in force on that date already included a clause of the type provided for in that paragraph.

18.4 Each Member shall take all necessary steps, of a general or particular character, to ensure, not later than the date of entry into force of the WTO Agreement for it, the conformity of its laws, regulations and administrative procedures with the provisions of this Agreement as they may apply for the Member in question.

18.5 Each Member shall inform the Committee of any changes in its laws and regulations relevant to this Agreement and in the administration of such laws and regulations.

²⁴ This is not intended to preclude action under other relevant provisions of GATT 1994, as appropriate.

18.6 The Committee shall review annually the implementation and operation of this Agreement taking into account the objectives thereof. The Committee shall inform annually the Council for Trade in Goods of developments during the period covered by such reviews.

18.7 The Annexes to this Agreement constitute an integral part thereof.

ANNEX I

PROCEDURES FOR ON-THE-SPOT INVESTIGATIONS PURSUANT TO PARAGRAPH 7 OF ARTICLE 6

1. Upon initiation of an investigation, the authorities of the exporting Member and the firms known to be concerned should be informed of the intention to carry out on-the-spot investigations.
2. If in exceptional circumstances it is intended to include non-governmental experts in the investigating team, the firms and the authorities of the exporting Member should be so informed. Such non-governmental experts should be subject to effective sanctions for breach of confidentiality requirements.
3. It should be standard practice to obtain explicit agreement of the firms concerned in the exporting Member before the visit is finally scheduled.
4. As soon as the agreement of the firms concerned has been obtained, the investigating authorities should notify the authorities of the exporting Member of the names and addresses of the firms to be visited and the dates agreed.
5. Sufficient advance notice should be given to the firms in question before the visit is made.
6. Visits to explain the questionnaire should only be made at the request of an exporting firm. Such a visit may only be made if (a) the authorities of the importing Member notify the representatives of the Member in question and (b) the latter do not object to the visit.
7. As the main purpose of the on-the-spot investigation is to verify information provided or to obtain further details, it should be carried out after the response to the questionnaire has been received unless the firm agrees to the contrary and the government of the exporting Member is informed by the investigating authorities of the anticipated visit and does not object to it; further, it should be standard practice prior to the visit to advise the firms concerned of the general nature of the information to be verified and of any further information which needs to be provided, though this should not preclude requests to be made on the spot for further details to be provided in the light of information obtained.
8. Enquiries or questions put by the authorities or firms of the exporting Members and essential to a successful on-the-spot investigation should, whenever possible, be answered before the visit is made.

ANNEX II

BEST INFORMATION AVAILABLE IN TERMS OF PARAGRAPH 8 OF ARTICLE 6

1. As soon as possible after the initiation of the investigation, the investigating authorities should specify in detail the information required from any interested party, and the manner in which that information should be structured by the interested party in its response. The authorities should also ensure that the party is aware that if information is not supplied within a reasonable time, the

authorities will be free to make determinations on the basis of the facts available, including those contained in the application for the initiation of the investigation by the domestic industry.

2. The authorities may also request that an interested party provide its response in a particular medium (e.g. computer tape) or computer language. Where such a request is made, the authorities should consider the reasonable ability of the interested party to respond in the preferred medium or computer language, and should not request the party to use for its response a computer system other than that used by the party. The authority should not maintain a request for a computerized response if the interested party does not maintain computerized accounts and if presenting the response as requested would result in an unreasonable extra burden on the interested party, e.g. it would entail unreasonable additional cost and trouble. The authorities should not maintain a request for a response in a particular medium or computer language if the interested party does not maintain its computerized accounts in such medium or computer language and if presenting the response as requested would result in an unreasonable extra burden on the interested party, e.g. it would entail unreasonable additional cost and trouble.
3. All information which is verifiable, which is appropriately submitted so that it can be used in the investigation without undue difficulties, which is supplied in a timely fashion, and, where applicable, which is supplied in a medium or computer language requested by the authorities, should be taken into account when determinations are made. If a party does not respond in the preferred medium or computer language but the authorities find that the circumstances set out in paragraph 2 have been satisfied, the failure to respond in the preferred medium or computer language should not be considered to significantly impede the investigation.
4. Where the authorities do not have the ability to process information if provided in a particular medium (e.g. computer tape), the information should be supplied in the form of written material or any other form acceptable to the authorities.
5. Even though the information provided may not be ideal in all respects, this should not justify the authorities from disregarding it, provided the interested party has acted to the best of its ability.
6. If evidence or information is not accepted, the supplying party should be informed forthwith of the reasons therefor, and should have an opportunity to provide further explanations within a reasonable period, due account being taken of the time-limits of the investigation. If the explanations are considered by the authorities as not being satisfactory, the reasons for the rejection of such evidence or information should be given in any published determinations.
7. If the authorities have to base their findings, including those with respect to normal value, on information from a secondary source, including the information supplied in the application for the initiation of the investigation, they should do so with special circumspection. In such cases, the authorities should, where practicable, check the information from other independent sources at their disposal, such as published price lists, official import statistics and customs returns, and from the information obtained from other interested parties during the investigation. It is clear, however, that if an interested party does not cooperate and thus relevant information is being withheld from the authorities, this situation could lead to a result which is less favourable to the party than if the party did cooperate.

**Agreement on Subsidies and Countervailing
Measures, 1994**

AGREEMENT ON SUBSIDIES AND COUNTERVAILING MEASURES

Members hereby agree as follows:

PART I: GENERAL PROVISIONS

Article I

Definition of a Subsidy

1.1 For the purpose of this Agreement, a subsidy shall be deemed to exist if:

- (a)(1) there is a financial contribution by a government or any public body within the territory of a Member (referred to in this Agreement as "government"), i.e. where:
- (i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e.g. loan guarantees);
 - (ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits)¹;
 - (iii) a government provides goods or services other than general infrastructure, or purchases goods;
 - (iv) a government makes payments to a funding mechanism, or entrusts or directs a private body to carry out one or more of the type of functions illustrated in (i) to (iii) above which would normally be vested in the government and the practice, in no real sense, differs from practices normally followed by governments;

or

(a)(2) there is any form of income or price support in the sense of Article XVI of GATT 1994;

and

(b) a benefit is thereby conferred.

1.2 A subsidy as defined in paragraph 1 shall be subject to the provisions of Part II or shall be subject to the provisions of Part III or V only if such a subsidy is specific in accordance with the provisions of Article 2.

¹In accordance with the provisions of Article XVI of GATT 1994 (Note to Article XVI) and the provisions of Annexes I through III of this Agreement, the exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption, or the remission of such duties or taxes in amounts not in excess of those which have accrued, shall not be deemed to be a subsidy.

Article 2

Specificity

2.1 In order to determine whether a subsidy, as defined in paragraph 1 of Article 1, is specific to an enterprise or industry or group of enterprises or industries (referred to in this Agreement as "certain enterprises") within the jurisdiction of the granting authority, the following principles shall apply:

- (a) Where the granting authority, or the legislation pursuant to which the granting authority operates, explicitly limits access to a subsidy to certain enterprises, such subsidy shall be specific.
 - (b) Where the granting authority, or the legislation pursuant to which the granting authority operates, establishes objective criteria or conditions² governing the eligibility for, and the amount of, a subsidy, specificity shall not exist, provided that the eligibility is automatic and that such criteria and conditions are strictly adhered to. The criteria or conditions must be clearly spelled out in law, regulation, or other official document, so as to be capable of verification.
 - (c) If, notwithstanding any appearance of non-specificity resulting from the application of the principles laid down in subparagraphs (a) and (b), there are reasons to believe that the subsidy may in fact be specific, other factors may be considered. Such factors are: use of a subsidy programme by a limited number of certain enterprises, predominant use by certain enterprises, the granting of disproportionately large amounts of subsidy to certain enterprises, and the manner in which discretion has been exercised by the granting authority in the decision to grant a subsidy.³ In applying this subparagraph, account shall be taken of the extent of diversification of economic activities within the jurisdiction of the granting authority, as well as of the length of time during which the subsidy programme has been in operation.
- 2.2 A subsidy which is limited to certain enterprises located within a designated geographical region within the jurisdiction of the granting authority shall be specific. It is understood that the setting or change of generally applicable tax rates by all levels of government entitled to do so shall not be deemed to be a specific subsidy for the purposes of this Agreement.
- 2.3 Any subsidy falling under the provisions of Article 3 shall be deemed to be specific.
- 2.4 Any determination of specificity under the provisions of this Article shall be clearly substantiated on the basis of positive evidence.

²Objective criteria or conditions, as used herein, mean criteria or conditions which are neutral, which do not favour certain enterprises over others, and which are economic in nature and horizontal in application, such as number of employees or size of enterprise.

³In this regard, in particular, information on the frequency with which applications for a subsidy are refused or approved and the reasons for such decisions shall be considered.

PART II: PROHIBITED SUBSIDIES

*Article 3**Prohibition*

3.1 Except as provided in the Agreement on Agriculture, the following subsidies, within the meaning of Article 1, shall be prohibited:

- (a) subsidies contingent, in law or in fact⁴, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex F;
 - (b) subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods.
- 3.2 A Member shall neither grant nor maintain subsidies referred to in paragraph 1.

*Article 4**Remedies*

4.1 Whenever a Member has reason to believe that a prohibited subsidy is being granted or maintained by another Member, such Member may request consultations with such other Member.

4.2 A request for consultations under paragraph 1 shall include a statement of available evidence with regard to the existence and nature of the subsidy in question.

4.3 Upon request for consultations under paragraph 1, the Member believed to be granting or maintaining the subsidy in question shall enter into such consultations as quickly as possible. The purpose of the consultations shall be to clarify the facts of the situation and to arrive at a mutually agreed solution.

4.4 If no mutually agreed solution has been reached within 30 days⁶ of the request for consultations, any Member party to such consultations may refer the matter to the Dispute Settlement Body ("DSB") for the immediate establishment of a panel, unless the DSB decides by consensus not to establish a panel.

4.5 Upon its establishment, the panel may request the assistance of the Permanent Group of Experts⁷ (referred to in this Agreement as the "PGE") with regard to whether the measure in question is a prohibited subsidy. If so requested, the PGE shall immediately review the evidence with regard to

⁴This standard is met when the facts demonstrate that the granting of a subsidy, without having been made legally contingent upon export performance, is in fact tied to actual or anticipated exportation or export earnings. The mere fact that a subsidy is granted to enterprises which export shall not for that reason alone be considered to be an export subsidy within the meaning of this provision.

⁵Measures referred to in Annex 1 as not constituting export subsidies shall not be prohibited under this or any other provision of this Agreement.

⁶Any time-periods mentioned in this Article may be extended by mutual agreement.

⁷As established in Article 24.

the existence and nature of the measure in question and shall provide an opportunity for the Member applying or maintaining the measure to demonstrate that the measure in question is not a prohibited subsidy. The PGE shall report its conclusions to the panel within a time-limit determined by the panel. The PGE's conclusions on the issue of whether or not the measure in question is a prohibited subsidy shall be accepted by the panel without modification.

4.6 The panel shall submit its final report to the parties to the dispute. The report shall be circulated to all Members within 90 days of the date of the composition and the establishment of the panel's terms of reference.

4.7 If the measure in question is found to be a prohibited subsidy, the panel shall recommend that the subsidizing Member withdraw the subsidy without delay. In this regard, the panel shall specify in its recommendation the time-period within which the measure must be withdrawn.

4.8 Within 30 days of the issuance of the panel's report to all Members, the report shall be adopted by the DSB unless one of the parties to the dispute formally notifies the DSB of its decision to appeal or the DSB decides by consensus not to adopt the report.

4.9 Where a panel report is appealed, the Appellate Body shall issue its decision within 30 days from the date when the party to the dispute formally notifies its intention to appeal. When the Appellate Body considers that it cannot provide its report within 30 days, it shall inform the DSB in writing of the reasons for the delay together with an estimate of the period within which it will submit its report. In no case shall the proceedings exceed 60 days. The appellate report shall be adopted by the DSB and unconditionally accepted by the parties to the dispute unless the DSB decides by consensus not to adopt the appellate report within 20 days following its issuance to the Members.⁸

4.10 In the event the recommendation of the DSB is not followed within the time-period specified by the panel, which shall commence from the date of adoption of the panel's report or the Appellate Body's report, the DSB shall grant authorization to the complaining Member to take appropriate countermeasures, unless the DSB decides by consensus to reject the request.

4.11 In the event a party to the dispute requests arbitration under paragraph 6 of Article 22 of the Dispute Settlement Understanding ("DSU"), the arbitrator shall determine whether the countermeasures are appropriate.¹⁰

4.12 For purposes of disputes conducted pursuant to this Article, except for time-periods specifically prescribed in this Article, time-periods applicable under the DSU for the conduct of such disputes shall be half the time prescribed therein.

⁸If a meeting of the DSB is not scheduled during this period, such a meeting shall be held for this purpose.

⁹This expression is not meant to allow countermeasures that are disproportionate in light of the fact that the subsidies dealt with under these provisions are prohibited.

¹⁰This expression is not meant to allow countermeasures that are disproportionate in light of the fact that the subsidies dealt with under these provisions are prohibited.

PART III: ACTIONABLE SUBSIDIES

*Article 5**Adverse Effects*

No Member should cause, through the use of any subsidy referred to in paragraphs 1 and 2 of Article 1, adverse effects to the interests of other Members, i.e.:

- (a) injury to the domestic industry of another Member¹¹;
- (b) nullification or impairment of benefits accruing directly or indirectly to other Members under GATT 1994 in particular the benefits of concessions bound under Article II of GATT 1994¹²;
- (c) serious prejudice to the interests of another Member.¹³

This Article does not apply to subsidies maintained on agricultural products as provided in Article 13 of the Agreement on Agriculture.

*Article 6**Serious Prejudice*

6.1 Serious prejudice in the sense of paragraph (c) of Article 5 shall be deemed to exist in the case of:

- (a) the total ad valorem subsidization¹⁴ of a product exceeding 5 per cent¹⁵;
- (b) subsidies to cover operating losses sustained by an industry;
- (c) subsidies to cover operating losses sustained by an enterprise, other than one-time measures which are non-recurrent and cannot be repeated for that enterprise and which are given merely to provide time for the development of long-term solutions and to avoid acute social problems;

¹¹The term "injury to the domestic industry" is used here in the same sense as it is used in Part V.

¹²The term "nullification or impairment" is used in this Agreement in the same sense as it is used in the relevant provisions of GATT 1994, and the existence of such nullification or impairment shall be established in accordance with the practice of application of these provisions.

¹³The term "serious prejudice to the interests of another Member" is used in this Agreement in the same sense as it is used in paragraph 1 of Article XVI of GATT 1994, and includes threat of serious prejudice.

¹⁴The total ad valorem subsidization shall be calculated in accordance with the provisions of Annex IV.

¹⁵Since it is anticipated that civil aircraft will be subject to specific multilateral rules, the threshold in this subparagraph does not apply to civil aircraft.

- (d) direct forgiveness of debt, i.e. forgiveness of government-held debt, and grants to cover debt repayment.¹⁶

6.2 Notwithstanding the provisions of paragraph 1, serious prejudice shall not be found if the subsidizing Member demonstrates that the subsidy in question has not resulted in any of the effects enumerated in paragraph 3.

6.3 Serious prejudice in the sense of paragraph (c) of Article 5 may arise in any case where one or several of the following apply:

- (a) the effect of the subsidy is to displace or impede the imports of a like product of another Member into the market of the subsidizing Member;
- (b) the effect of the subsidy is to displace or impede the exports of a like product of another Member from a third country market;
- (c) the effect of the subsidy is a significant price undercutting by the subsidized product as compared with the price of a like product of another Member in the same market or significant price suppression, price depression or lost sales in the same market;
- (d) the effect of the subsidy is an increase in the world market share of the subsidizing Member in a particular subsidized primary product or commodity¹⁷ as compared to the average share it had during the previous period of three years and this increase follows a consistent trend over a period when subsidies have been granted.

6.4 For the purpose of paragraph 3(b), the displacement or impeding of exports shall include any case in which, subject to the provisions of paragraph 7, it has been demonstrated that there has been a change in relative shares of the market to the disadvantage of the non-subsidized like product (over an appropriately representative period sufficient to demonstrate clear trends in the development of the market for the product concerned, which, in normal circumstances, shall be at least one year). "Change in relative shares of the market" shall include any of the following situations: (a) there is an increase in the market share of the subsidized product; (b) the market share of the subsidized product remains constant in circumstances in which, in the absence of the subsidy, it would have declined; (c) the market share of the subsidized product declines, but at a slower rate than would have been the case in the absence of the subsidy.

6.5 For the purpose of paragraph 3(c), price undercutting shall include any case in which such price undercutting has been demonstrated through a comparison of prices of the subsidized product with prices of a non-subsidized like product supplied to the same market. The comparison shall be made at the same level of trade and at comparable times, due account being taken of any other factor affecting price comparability. However, if such a direct comparison is not possible, the existence of price undercutting may be demonstrated on the basis of export unit values.

6.6 Each Member in the market of which serious prejudice is alleged to have arisen shall, subject to the provisions of paragraph 3 of Annex V, make available to the parties to a dispute arising under Article 7, and to the panel established pursuant to paragraph 4 of Article 7, all relevant information

¹⁶Members recognize that where royalty-based financing for a civil aircraft programme is not being fully repaid due to the level of actual sales falling below the level of forecast sales, this does not in itself constitute serious prejudice for the purposes of this subparagraph.

¹⁷Unless other multilaterally agreed specific rules apply to the trade in the product or commodity in question.

that can be obtained as to the changes in market shares of the parties to the dispute as well as concerning prices of the products involved.

6.7 Displacement or impediment resulting in serious prejudice shall not arise under paragraph 3 where any of the following circumstances exist¹⁸ during the relevant period:

- (a) prohibition or restriction on exports of the like product from the complaining Member or on imports from the complaining Member into the third country market concerned;
- (b) decision by an importing government operating a monopoly of trade or state trading in the product concerned to shift, for non-commercial reasons, imports from the complaining Member to another country or countries;
- (c) natural disasters, strikes, transport disruptions or other *force majeure* substantially affecting production, qualities, quantities or prices of the product available for export from the complaining Member;
- (d) existence of arrangements limiting exports from the complaining Member;
- (e) voluntary decrease in the availability for export of the product concerned from the complaining Member (including, *inter alia*, a situation where firms in the complaining Member have been autonomously reallocating exports of this product to new markets);
- (f) failure to conform to standards and other regulatory requirements in the importing country.

6.8 In the absence of circumstances referred to in paragraph 7, the existence of serious prejudice should be determined on the basis of the information submitted to or obtained by the panel, including information submitted in accordance with the provisions of Annex V.

6.9 This Article does not apply to subsidies maintained on agricultural products as provided in Article 13 of the Agreement on Agriculture.

Article 7

Remedies

7.1 Except as provided in Article 13 of the Agreement on Agriculture, whenever a Member has reason to believe that any subsidy referred to in Article 1, granted or maintained by another Member, results in injury to its domestic industry, nullification or impairment or serious prejudice, such Member may request consultations with such other Member.

7.2 A request for consultations under paragraph 1 shall include a statement of available evidence with regard to (a) the existence and nature of the subsidy in question, and (b) the injury caused to the

domestic industry, or the nullification or impairment, or serious prejudice¹⁹ caused to the interests of the Member requesting consultations.

7.3 Upon request for consultations under paragraph 1, the Member believed to be granting or maintaining the subsidy practice in question shall enter into such consultations as quickly as possible. The purpose of the consultations shall be to clarify the facts of the situation and to arrive at a mutually agreed solution.

7.4 If consultations do not result in a mutually agreed solution within 60 days²⁰, any Member party to such consultations may refer the matter to the DSB for the establishment of a panel, unless the DSB decides by consensus not to establish a panel. The composition of the panel and its terms of reference shall be established within 15 days from the date when it is established.

7.5 The panel shall review the matter and shall submit its final report to the parties to the dispute. The report shall be circulated to all Members within 120 days of the date of the composition and establishment of the panel's terms of reference.

7.6 Within 30 days of the issuance of the panel's report to all Members, the report shall be adopted by the DSB²¹ unless one of the parties to the dispute formally notifies the DSB of its decision to appeal or the DSB decides by consensus not to adopt the report.

7.7 Where a panel report is appealed, the Appellate Body shall issue its decision within 60 days from the date when the party to the dispute formally notifies its intention to appeal. When the Appellate Body considers that it cannot provide its report within 60 days, it shall inform the DSB in writing of the reasons for the delay together with an estimate of the period within which it will submit its report. In no case shall the proceedings exceed 90 days. The appellate report shall be adopted by the DSB and unconditionally accepted by the parties to the dispute unless the DSB decides by consensus not to adopt the appellate report within 20 days following its issuance to the Members.²²

7.8 Where a panel report or an Appellate Body report is adopted in which it is determined that any subsidy has resulted in adverse effects to the interests of another Member within the meaning of Article 5, the Member granting or maintaining such subsidy shall take appropriate steps to remove the adverse effects or shall withdraw the subsidy.

7.9 In the event the Member has not taken appropriate steps to remove the adverse effects of the subsidy or withdraw the subsidy within six months from the date when the DSB adopts the panel report or the Appellate Body report, and in the absence of agreement on compensation, the DSB shall grant authorization to the complaining Member to take countermeasures, commensurate with the degree and nature of the adverse effects determined to exist, unless the DSB decides by consensus to reject the request.

¹⁹In the event that the request relates to a subsidy deemed to result in serious prejudice in terms of paragraph 1 of Article 6, the available evidence of serious prejudice may be limited to the available evidence as to whether the conditions of paragraph 1 of Article 6 have been met or not.

²⁰Any time-periods mentioned in this Article may be extended by mutual agreement.

²¹If a meeting of the DSB is not scheduled during this period, such a meeting shall be held for this purpose.

²²If a meeting of the DSB is not scheduled during this period, such a meeting shall be held for this purpose.

¹⁸The fact that certain circumstances are referred to in this paragraph does not, in itself, confer upon them any legal status in terms of either GATT 1994 or this Agreement. These circumstances must not be isolated, sporadic or otherwise insignificant.

7.10 In the event that a party to the dispute requests arbitration under paragraph 6 of Article 22 of the DSU, the arbitrator shall determine whether the countermeasures are commensurate with the degree and nature of the adverse effects determined to exist.

PART IV: NON-ACTIONABLE SUBSIDIES

Article 8

Identification of Non-Actionable Subsidies

8.1 The following subsidies shall be considered as non-actionable²³:

- (a) subsidies which are not specific within the meaning of Article 2;
- (b) subsidies which are specific within the meaning of Article 2 but which meet all of the conditions provided for in paragraphs 2(a), 2(b) or 2(c) below.

8.2 Notwithstanding the provisions of Parts III and V, the following subsidies shall be non-actionable:

- (a) assistance for research activities conducted by firms or by higher education or research establishments on a contract basis with firms if:^{24, 25, 26}
 - the assistance covers²⁷ not more than 75 per cent of the costs of industrial research²⁸ or 50 per cent of the costs of pre-competitive development activity^{29, 30};

²³It is recognized that government assistance for various purposes is widely provided by Members and that the mere fact that such assistance may not qualify for non-actionable treatment under the provisions of this Article does not in itself restrict the ability of Members to provide such assistance.

²⁴Since it is anticipated that civil aircraft will be subject to specific multilateral rules, the provisions of this subparagraph do not apply to that product.

²⁵Not later than 18 months after the date of entry into force of the WTO Agreement, the Committee on Subsidies and Countervailing Measures provided for in Article 24 (referred to in this Agreement as "the Committee") shall review the operation of the provisions of subparagraph 2(a) with a view to making all necessary modifications to improve the operation of those provisions. In its consideration of possible modifications, the Committee shall carefully review the definitions of the categories set forth in this subparagraph in the light of the experience of Members in the operation of research programmes and the work in other relevant international institutions.

²⁶The provisions of this Agreement do not apply to fundamental research activities independently conducted by higher education or research establishments. The term "fundamental research" means an enlargement of general scientific and technical knowledge not linked to industrial or commercial objectives.

²⁷The allowable levels of non-actionable assistance referred to in this subparagraph shall be established by reference to the total eligible costs incurred over the duration of an individual project.

²⁸The term "industrial research" means planned search or critical investigation aimed at discovery of new knowledge, with the objective that such knowledge may be useful in developing new products, processes or services, or in bringing about a significant improvement to existing products, processes or services.

²⁹The term "pre-competitive development activity" means the translation of industrial research findings into a plan, blueprint or design for new, modified or improved products, processes or services whether intended for sale or use, including the creation of a first prototype which would not be capable of commercial use. It may further include the conceptual formulation and design of products, processes or services alternatives and initial demonstration or pilot projects, provided that these same projects

and provided that such assistance is limited exclusively to:

- (i) costs of personnel (researchers, technicians and other supporting staff employed exclusively in the research activity);
 - (ii) costs of instruments, equipment, land and buildings used exclusively and permanently (except when disposed of on a commercial basis) for the research activity;
 - (iii) costs of consultancy and equivalent services used exclusively for the research activity, including bought-in research, technical knowledge, patents, etc.;
 - (iv) additional overhead costs incurred directly as a result of the research activity;
 - (v) other running costs (such as those of materials, supplies and the like), incurred directly as a result of the research activity.
- (b) assistance to disadvantaged regions within the territory of a Member given pursuant to a general framework of regional development³¹ and non-specific (within the meaning of Article 2) within eligible regions provided that:
- (i) each disadvantaged region must be a clearly designated contiguous geographical area with a definable economic and administrative identity;
 - (ii) the region is considered as disadvantaged on the basis of neutral and objective criteria³², indicating that the region's difficulties arise out of more than temporary circumstances; such criteria must be clearly spelled out in law, regulation, or other official document, so as to be capable of verification;
 - (iii) the criteria shall include a measurement of economic development which shall be based on at least one of the following factors:
 - one of either income per capita or household income per capita, or GDP per capita, which must not be above 85 per cent of the average for the territory concerned;

cannot be converted or used for industrial application or commercial exploitation. It does not include routine or periodic alterations to existing products, production lines, manufacturing processes, services, and other on-going operations even though those alterations may represent improvements.

³¹In the case of programmes which span industrial research and pre-competitive development activity, the allowable level of non-actionable assistance shall not exceed the simple average of the allowable levels of non-actionable assistance applicable to the above two categories, calculated on the basis of all eligible costs as set forth in items (i) to (v) of this subparagraph.

³²A "general framework of regional development" means that regional subsidy programmes are part of an internally consistent and generally applicable regional development policy and that regional development subsidies are not granted in isolated geographical points having no, or virtually no, influence on the development of a region.

³³Neutral and objective criteria" means criteria which do not favour certain regions beyond what is appropriate for the elimination or reduction of regional disparities within the framework of the regional development policy. In this regard, regional subsidy programmes shall include ceilings on the amount of assistance which can be granted to each subsidized project. Such ceilings must be differentiated according to the different levels of development of assisted regions and must be expressed in terms of investment costs or cost of job creation. Within such ceilings, the distribution of assistance shall be sufficiently broad and even to avoid the predominant use of a subsidy by, or the granting of disproportionately large amounts of subsidy to, certain enterprises as provided for in Article 2.

- unemployment rate, which must be at least 110 per cent of the average for the territory concerned;
 - as measured over a three-year period; such measurement, however, may be a composite one and may include other factors.
- (c) assistance to promote adaptation of existing facilities³³ to new environmental requirements imposed by law and/or regulations which result in greater constraints and financial burden on firms, provided that the assistance:
- (i) is a one-time non-recurring measure; and
 - (ii) is limited to 20 per cent of the cost of adaptation; and
 - (iii) does not cover the cost of replacing and operating the assisted investment, which must be fully borne by firms; and
 - (iv) is directly linked to and proportionate to a firm's planned reduction of nuisances and pollution, and does not cover any manufacturing cost savings which may be achieved; and
 - (v) is available to all firms which can adopt the new equipment and/or production processes.

8.3 A subsidy programme for which the provisions of paragraph 2 are invoked shall be notified in advance of its implementation to the Committee in accordance with the provisions of Part VII. Any such notification shall be sufficiently precise to enable other Members to evaluate the consistency of the programme with the conditions and criteria provided for in the relevant provisions of paragraph 2. Members shall also provide the Committee with yearly updates of such notifications, in particular by supplying information on global expenditure for each programme, and on any modification of the programme. Other Members shall have the right to request information about individual cases of subsidization under a notified programme.³⁴

8.4 Upon request of a Member, the Secretariat shall review a notification made pursuant to paragraph 3 and, where necessary, may require additional information from the subsidizing Member concerning the notified programme under review. The Secretariat shall report its findings to the Committee. The Committee shall, upon request, promptly review the findings of the Secretariat (or, if a review by the Secretariat has not been requested, the notification itself), with a view to determining whether the conditions and criteria laid down in paragraph 2 have not been met. The procedure provided for in this paragraph shall be completed at the latest at the first regular meeting of the Committee following the notification of a subsidy programme, provided that at least two months have elapsed between such notification and the regular meeting of the Committee. The review procedure described in this paragraph shall also apply, upon request, to substantial modifications of a programme notified in the yearly updates referred to in paragraph 3.

8.5 Upon the request of a Member, the determination by the Committee referred to in paragraph 4, or a failure by the Committee to make such a determination, as well as the violation, in individual cases,

³³The term "existing facilities" means facilities which have been in operation for at least two years at the time when new environmental requirements are imposed.

³⁴It is recognized that nothing in this notification provision requires the provision of confidential information, including confidential business information.

of the conditions set out in a notified programme, shall be submitted to binding arbitration. The arbitration body shall present its conclusions to the Members within 120 days from the date when the matter was referred to the arbitration body. Except as otherwise provided in this paragraph, the DSU shall apply to arbitrations conducted under this paragraph.

Article 9

Consultations and Authorized Remedies

9.1 If, in the course of implementation of a programme referred to in paragraph 2 of Article 8, notwithstanding the fact that the programme is consistent with the criteria laid down in that paragraph, a Member has reasons to believe that this programme has resulted in serious adverse effects to the domestic industry of that Member, such as to cause damage which would be difficult to repair, such Member may request consultations with the Member granting or maintaining the subsidy.

9.2 Upon request for consultations under paragraph 1, the Member granting or maintaining the subsidy programme in question shall enter into such consultations as quickly as possible. The purpose of the consultations shall be to clarify the facts of the situation and to arrive at a mutually acceptable solution.

9.3 If no mutually acceptable solution has been reached in consultations under paragraph 2 within 60 days of the request for such consultations, the requesting Member may refer the matter to the Committee.

9.4 Where a matter is referred to the Committee, the Committee shall immediately review the facts involved and the evidence of the effects referred to in paragraph 1. If the Committee determines that such effects exist, it may recommend to the subsidizing Member to modify this programme in such a way as to remove these effects. The Committee shall present its conclusions within 120 days from the date when the matter is referred to it under paragraph 3. In the event the recommendation is not followed within six months, the Committee shall authorize the requesting Member to take appropriate countermeasures commensurate with the nature and degree of the effects determined to exist.

PART V: COUNTERVAILING MEASURES

Article 10

Application of Article VI of GATT 1994³⁵

Members shall take all necessary steps to ensure that the imposition of a countervailing duty³⁶ on any product of the territory of any Member imported into the territory of another Member is in accordance with the provisions of Article VI of GATT 1994 and the terms of this Agreement. Countervailing duties may only be imposed pursuant to investigations initiated³⁷ and conducted in accordance with the provisions of this Agreement and the Agreement on Agriculture.

Article 11

Initiation and Subsequent Investigation

11.1 Except as provided in paragraph 6, an investigation to determine the existence, degree and effect of any alleged subsidy shall be initiated upon a written application by or on behalf of the domestic industry.

11.2 An application under paragraph 1 shall include sufficient evidence of the existence of (a) a subsidy and, if possible, its amount, (b) injury within the meaning of Article VI of GATT 1994 as interpreted by this Agreement, and (c) a causal link between the subsidized imports and the alleged injury. Simple assertion, unsubstantiated by relevant evidence, cannot be considered sufficient to meet the requirements of this paragraph. The application shall contain such information as is reasonably available to the applicant on the following:

- (i) the identity of the applicant and a description of the volume and value of the domestic production of the like product by the applicant. Where a written application is made on behalf of the domestic industry, the application shall identify the industry on behalf of which the application is made by a list of all known domestic producers of the like product (or associations of domestic producers of the like product) and, to the extent possible, a description of the volume and value of domestic production of the like product accounted for by such producers;

³⁵The provisions of Part II or III may be invoked in parallel with the provisions of Part V; however, with regard to the effects of a particular subsidy in the domestic market of the importing Member, only one form of relief (either a countervailing duty, if the requirements of Part V are met, or a countermeasure under Articles 4 or 7) shall be available. The provisions of Parts III and V shall not be invoked regarding measures considered non-actionable in accordance with the provisions of Part IV. However, measures referred to in paragraph 1(a) of Article 8 may be investigated in order to determine whether or not they are specific within the meaning of Article 2. In addition, in the case of a subsidy referred to in paragraph 2 of Article 8 conferred pursuant to a programme which has not been notified in accordance with paragraph 3 of Article 8, the provisions of Part III or V may be invoked, but such subsidy shall be treated as non-actionable if it is found to conform to the standards set forth in paragraph 2 of Article 8.

³⁶The term "countervailing duty" shall be understood to mean a special duty levied for the purpose of offsetting any subsidy bestowed directly or indirectly upon the manufacture, production or export of any merchandise, as provided for in paragraph 3 of Article VI of GATT 1994.

³⁷The term "initiated" as used hereinafter means procedural action by which a Member formally commences an investigation as provided in Article 11.

- (ii) a complete description of the allegedly subsidized product, the names of the country or countries of origin or export in question, the identity of each known exporter or foreign producer and a list of known persons importing the product in question;
- (iii) evidence with regard to the existence, amount and nature of the subsidy in question;
- (iv) evidence that alleged injury to a domestic industry is caused by subsidized imports through the effects of the subsidies; this evidence includes information on the evolution of the volume of the allegedly subsidized imports, the effect of these imports on prices of the like product in the domestic market and the consequent impact of the imports on the domestic industry, as demonstrated by relevant factors and indices having a bearing on the state of the domestic industry, such as those listed in paragraphs 2 and 4 of Article 15.

11.3 The authorities shall review the accuracy and adequacy of the evidence provided in the application to determine whether the evidence is sufficient to justify the initiation of an investigation.

11.4 An investigation shall not be initiated pursuant to paragraph 1 unless the authorities have determined, on the basis of an examination of the degree of support for, or opposition to, the application expressed³⁸ by domestic producers of the like product, that the application has been made by or on behalf of the domestic industry.³⁹ The application shall be considered to have been made "by or on behalf of the domestic industry" if it is supported by those domestic producers whose collective output constitutes more than 50 per cent of the total production of the like product produced by that portion of the domestic industry expressing either support for or opposition to the application. However, no investigation shall be initiated when domestic producers expressly supporting the application account for less than 25 per cent of total production of the like product produced by the domestic industry.

11.5 The authorities shall avoid, unless a decision has been made to initiate an investigation, any publicizing of the application for the initiation of an investigation.

11.6 If, in special circumstances, the authorities concerned decide to initiate an investigation without having received a written application by or on behalf of a domestic industry for the initiation of such investigation, they shall proceed only if they have sufficient evidence of the existence of a subsidy, injury and causal link, as described in paragraph 2, to justify the initiation of an investigation.

11.7 The evidence of both subsidy and injury shall be considered simultaneously (a) in the decision whether or not to initiate an investigation and (b) thereafter, during the course of the investigation, starting on a date not later than the earliest date on which in accordance with the provisions of this Agreement provisional measures may be applied.

11.8 In cases where products are not imported directly from the country of origin but are exported to the importing Member from an intermediate country, the provisions of this Agreement shall be fully applicable and the transaction or transactions shall, for the purposes of this Agreement, be regarded as having taken place between the country of origin and the importing Member.

11.9 An application under paragraph 1 shall be rejected and an investigation shall be terminated promptly as soon as the authorities concerned are satisfied that there is not sufficient evidence of either

³⁸In the case of fragmented industries involving an exceptionally large number of producers, authorities may determine support and opposition by using statistically valid sampling techniques.

³⁹Members are aware that in the territory of certain Members employees of domestic producers of the like product or representatives of those employees may make or support an application for an investigation under paragraph 1.

subsidization or of injury to justify proceeding with the case. There shall be immediate termination in cases where the amount of a subsidy is *de minimis*, or where the volume of subsidized imports, actual or potential, or the injury, is negligible. For the purpose of this paragraph, the amount of the subsidy shall be considered to be *de minimis* if the subsidy is less than 1 per cent *ad valorem*.

11.10 An investigation shall not hinder the procedures of customs clearance.

11.11 Investigations shall, except in special circumstances, be concluded within one year, and in no case more than 18 months, after their initiation.

Article 12

Evidence

12.1 Interested Members and all interested parties in a countervailing duty investigation shall be given notice of the information which the authorities require and ample opportunity to present in writing all evidence which they consider relevant in respect of the investigation in question.

12.1.1 Exporters, foreign producers or interested Members receiving questionnaires used in a countervailing duty investigation shall be given at least 30 days for reply.⁴⁰ Due consideration should be given to any request for an extension of the 30-day period and, upon cause shown, such an extension should be granted whenever practicable.

12.1.2 Subject to the requirement to protect confidential information, evidence presented in writing by one interested Member or interested party shall be made available promptly to other interested Members or interested parties participating in the investigation.

12.1.3 As soon as an investigation has been initiated, the authorities shall provide the full text of the written application received under paragraph 1 of Article 11 to the known exporters⁴¹ and to the authorities of the exporting Member and shall make it available, upon request, to other interested parties involved. Due regard shall be paid to the protection of confidential information, as provided for in paragraph 4.

12.2. Interested Members and interested parties also shall have the right, upon justification, to present information orally. Where such information is provided orally, the interested Members and interested parties subsequently shall be required to reduce such submissions to writing. Any decision of the investigating authorities can only be based on such information and arguments as were on the written record of this authority and which were available to interested Members and interested parties participating in the investigation, due account having been given to the need to protect confidential information.

12.3 The authorities shall whenever practicable provide timely opportunities for all interested Members and interested parties to see all information that is relevant to the presentation of their cases, that is

⁴⁰As a general rule, the time-limit for exporters shall be counted from the date of receipt of the questionnaire, which for this purpose shall be deemed to have been received one week from the date on which it was sent to the respondent or transmitted to the appropriate diplomatic representatives of the exporting Member or, in the case of a separate customs territory Member of the WTO, an official representative of the exporting territory.

⁴¹It being understood that where the number of exporters involved is particularly high, the full text of the application should instead be provided only to the authorities of the exporting Member or to the relevant trade association who then should forward copies to the exporters concerned.

not confidential as defined in paragraph 4, and that is used by the authorities in a countervailing duty investigation, and to prepare presentations on the basis of this information.

12.4 Any information which is by nature confidential (for example, because its disclosure would be of significant competitive advantage to a competitor or because its disclosure would have a significantly adverse effect upon a person supplying the information or upon a person from whom the supplier acquired the information), or which is provided on a confidential basis by parties to an investigation shall, upon good cause shown, be treated as such by the authorities. Such information shall not be disclosed without specific permission of the party submitting it.⁴²

12.4.1 The authorities shall require interested Members or interested parties providing confidential information to furnish non-confidential summaries thereof. These summaries shall be in sufficient detail to permit a reasonable understanding of the substance of the information submitted in confidence. In exceptional circumstances, such Members or parties may indicate that such information is not susceptible of summary. In such exceptional circumstances, a statement of the reasons why summarization is not possible must be provided.

12.4.2 If the authorities find that a request for confidentiality is not warranted and if the supplier of the information is either unwilling to make the information public or to authorize its disclosure in generalized or summary form, the authorities may disregard such information unless it can be demonstrated to their satisfaction from appropriate sources that the information is correct.⁴³

12.5 Except in circumstances provided for in paragraph 7, the authorities shall during the course of an investigation satisfy themselves as to the accuracy of the information supplied by interested Members or interested parties upon which their findings are based.

12.6 The investigating authorities may carry out investigations in the territory of other Members as required, provided that they have notified in good time the Member in question and unless that Member objects to the investigation. Further, the investigating authorities may carry out investigations on the premises of a firm and may examine the records of a firm if (a) the firm so agrees and (b) the Member in question is notified and does not object. The procedures set forth in Annex VI shall apply to investigations on the premises of a firm. Subject to the requirement to protect confidential information, the authorities shall make the results of any such investigations available, or shall provide disclosure thereof pursuant to paragraph 8, to the firms to which they pertain and may make such results available to the applicants.

12.7 In cases in which any interested Member or interested party refuses access to, or otherwise does not provide, necessary information within a reasonable period or significantly impedes the investigation, preliminary and final determinations, affirmative or negative, may be made on the basis of the facts available.

12.8 The authorities shall, before a final determination is made, inform all interested Members and interested parties of the essential facts under consideration which form the basis for the decision whether to apply definitive measures. Such disclosure should take place in sufficient time for the parties to defend their interests.

⁴²Members are aware that in the territory of certain Members disclosure pursuant to a narrowly-drawn protective order may be required.

⁴³Members agree that requests for confidentiality should not be arbitrarily rejected. Members further agree that the investigating authority may request the waiving of confidentiality only regarding information relevant to the proceedings.

12.9 For the purposes of this Agreement, "interested parties" shall include:

- (i) an exporter or foreign producer or the importer of a product subject to investigation, or a trade or business association a majority of the members of which are producers, exporters or importers of such product; and
- (ii) a producer of the like product in the importing Member or a trade and business association a majority of the members of which produce the like product in the territory of the importing Member.

This list shall not preclude Members from allowing domestic or foreign parties other than those mentioned above to be included as interested parties.

12.10 The authorities shall provide opportunities for industrial users of the product under investigation, and for representative consumer organizations in cases where the product is commonly sold at the retail level, to provide information which is relevant to the investigation regarding subsidization, injury and causality.

12.11 The authorities shall take due account of any difficulties experienced by interested parties, in particular small companies, in supplying information requested, and shall provide any assistance practicable.

12.12 The procedures set out above are not intended to prevent the authorities of a Member from proceeding expeditiously with regard to initiating an investigation, reaching preliminary or final determinations, whether affirmative or negative, or from applying provisional or final measures, in accordance with relevant provisions of this Agreement.

Article 13

Consultations

13.1 As soon as possible after an application under Article 11 is accepted, and in any event before the initiation of any investigation, Members the products of which may be subject to such investigation shall be invited for consultations with the aim of clarifying the situation as to the matters referred to in paragraph 2 of Article 11 and arriving at a mutually agreed solution.

13.2 Furthermore, throughout the period of investigation, Members the products of which are the subject of the investigation shall be afforded a reasonable opportunity to continue consultations, with a view to clarifying the factual situation and to arriving at a mutually agreed solution.⁴⁴

13.3 Without prejudice to the obligation to afford reasonable opportunity for consultation, these provisions regarding consultations are not intended to prevent the authorities of a Member from proceeding expeditiously with regard to initiating the investigation, reaching preliminary or final determinations, whether affirmative or negative, or from applying provisional or final measures, in accordance with the provisions of this Agreement.

13.4 The Member which intends to initiate any investigation or is conducting such an investigation shall permit, upon request, the Member or Members the products of which are subject to such

⁴⁴It is particularly important, in accordance with the provisions of this paragraph, that no affirmative determination whether preliminary or final be made without reasonable opportunity for consultations having been given. Such consultations may establish the basis for proceeding under the provisions of Part II, III or X.

investigation access to non-confidential evidence, including the non-confidential summary of confidential data being used for initiating or conducting the investigation.

Article 14

Calculation of the Amount of a Subsidy in Terms of the Benefit to the Recipient

For the purpose of Part V, any method used by the investigating authority to calculate the benefit to the recipient conferred pursuant to paragraph 1 of Article 1 shall be provided for in the national legislation or implementing regulations of the Member concerned and its application to each particular case shall be transparent and adequately explained. Furthermore, any such method shall be consistent with the following guidelines:

- (a) government provision of equity capital shall not be considered as conferring a benefit, unless the investment decision can be regarded as inconsistent with the usual investment practice (including for the provision of risk capital) of private investors in the territory of that Member;
- (b) a loan by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the loan pays on the government loan and the amount the firm would pay on a comparable commercial loan which the firm could actually obtain on the market. In this case the benefit shall be the difference between these two amounts;
- (c) a loan guaranteed by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the government and the amount that the firm would pay on a comparable commercial loan absent the government guarantee. In this case the benefit shall be the difference between these two amounts adjusted for any differences in fees;
- (d) the provision of goods or services or purchase of goods by a government shall not be considered as conferring a benefit unless the provision is made for less than adequate remuneration, or the purchase is made for more than adequate remuneration. The adequacy of remuneration shall be determined in relation to prevailing market conditions for the good or service in question in the country of provision or purchase (including price, quality, availability, marketability, transportation and other conditions of purchase or sale).

Article 15

Determination of Injury⁴⁵

15.1 A determination of injury for purposes of Article VI of GATT 1994 shall be based on positive evidence and involve an objective examination of both (a) the volume of the subsidized imports and

⁴⁵Under this Agreement the term "injury" shall, unless otherwise specified, be taken to mean material injury to a domestic industry, threat of material injury to a domestic industry or material retardation of the establishment of such an industry and shall be interpreted in accordance with the provisions of this Article.

the effect of the subsidized imports on prices in the domestic market for like products⁴⁶ and (b) the consequent impact of these imports on the domestic producers of such products.

15.2 With regard to the volume of the subsidized imports, the investigating authorities shall consider whether there has been a significant increase in subsidized imports, either in absolute terms or relative to production or consumption in the importing Member. With regard to the effect of the subsidized imports on prices, the investigating authorities shall consider whether there has been a significant price undercutting by the subsidized imports as compared with the price of a like product of the importing Member, or whether the effect of such imports is otherwise to depress prices to a significant degree or to prevent price increases, which otherwise would have occurred, to a significant degree. No one or several of these factors can necessarily give decisive guidance.

15.3 Where imports of a product from more than one country are simultaneously subject to countervailing duty investigations, the investigating authorities may cumulatively assess the effects of such imports only if they determine that (a) the amount of subsidization established in relation to the imports from each country is more than *de minimis* as defined in paragraph 9 of Article 11 and the volume of imports from each country is not negligible and (b) a cumulative assessment of the effects of the imports is appropriate in light of the conditions of competition between the imported products and the conditions of competition between the imported products and the like domestic product.

15.4 The examination of the impact of the subsidized imports on the domestic industry shall include an evaluation of all relevant economic factors and indices having a bearing on the state of the industry, including actual and potential decline in output, sales, market share, profits, productivity, return on investments, or utilization of capacity; factors affecting domestic prices; actual and potential negative effects on cash flow, inventories, employment, wages, growth, ability to raise capital or investments and, in the case of agriculture, whether there has been an increased burden on government support programmes. This list is not exhaustive, nor can one or several of these factors necessarily give decisive guidance.

15.5 It must be demonstrated that the subsidized imports are, through the effects⁴⁷ of subsidies, causing injury within the meaning of this Agreement. The demonstration of a causal relationship between the subsidized imports and the injury to the domestic industry shall be based on an examination of all relevant evidence before the authorities. The authorities shall also examine any known factors other than the subsidized imports which at the same time are injuring the domestic industry, and the injuries caused by these other factors must not be attributed to the subsidized imports. Factors which may be relevant in this respect include, *inter alia*, the volumes and prices of non-subsidized imports of the product in question, contraction in demand or changes in the patterns of consumption, trade restrictive practices of and competition between the foreign and domestic producers, developments in technology and the export performance and productivity of the domestic industry.

15.6 The effect of the subsidized imports shall be assessed in relation to the domestic production of the like product when available data permit the separate identification of that production on the basis of such criteria as the production process, producers' sales and profits. If such separate identification of that production is not possible, the effects of the subsidized imports shall be assessed by the examination of the production of the narrowest group or range of products, which includes the like product, for which the necessary information can be provided.

⁴⁶Throughout this Agreement the term "like product" ("produit similaire") shall be interpreted to mean a product which is identical, i.e. alike in all respects to the product under consideration, or in the absence of such a product, another product which, although not alike in all respects, has characteristics closely resembling those of the product under consideration.

⁴⁷As set forth in paragraphs 2 and 4.

15.7 A determination of a threat of material injury shall be based on facts and not merely on a allegation, conjecture or remote possibility. The change in circumstances which would create a situation in which the subsidy would cause injury must be clearly foreseen and imminent. In making a determination regarding the existence of a threat of material injury, the investigating authorities should consider, *inter alia*, such factors as:

- (i) nature of the subsidy or subsidies in question and the trade effects likely to arise therefrom;
- (ii) a significant rate of increase of subsidized imports into the domestic market indicating the likelihood of substantially increased importation;
- (iii) sufficient freely disposable, or an imminent, substantial increase in, capacity of the exporter indicating the likelihood of substantially increased subsidized exports to the importing Member's market, taking into account the availability of other export markets to absorb any additional exports;
- (iv) whether imports are entering at prices that will have a significant depressing or suppressing effect on domestic prices, and would likely increase demand for further imports; and
- (v) inventories of the product being investigated.

No one of these factors by itself can necessarily give decisive guidance but the totality of the factors considered must lead to the conclusion that further subsidized exports are imminent and that, unless protective action is taken, material injury would occur.

15.8 With respect to cases where injury is threatened by subsidized imports, the application of countervailing measures shall be considered and decided with special care.

Article 16

Definition of Domestic Industry

16.1 For the purposes of this Agreement, the term "domestic industry" shall, except as provided in paragraph 2, be interpreted as referring to the domestic producers as a whole of the like products or to those of them whose collective output of the products constitutes a major proportion of the total domestic production of those products, except that when producers are related⁴⁸ to the exporters or importers or are themselves importers of the allegedly subsidized product or a like product from other countries, the term "domestic industry" may be interpreted as referring to the rest of the producers.

16.2. In exceptional circumstances, the territory of a Member may, for the production in question, be divided into two or more competitive markets and the producers within each market may be regarded as a separate industry if (a) the producers within such market sell all or almost all of their production of the product in question in that market, and (b) the demand in that market is not to any substantial

⁴⁸For the purpose of this paragraph, producers shall be deemed to be related to exporters or importers only if (a) one of them directly or indirectly controls the other; or (b) both of them are directly or indirectly controlled by a third person; or (c) together they directly or indirectly control a third person, provided that there are grounds for believing or suspecting that the effect of the relationship is such as to cause the producer concerned to behave differently from non-related producers. For the purpose of this paragraph, one shall be deemed to control another when the former is legally or operationally in a position to exercise restraint or direction over the latter.

degree supplied by producers of the product in question located elsewhere in the territory. In such circumstances, injury may be found to exist even where a major portion of the total domestic industry is not injured, provided there is a concentration of subsidized imports into such an isolated market and provided further that the subsidized imports are causing injury to the producers of all or almost all of the production within such market.

16.3 When the domestic industry has been interpreted as referring to the producers in a certain area, i.e. a market as defined in paragraph 2, countervailing duties shall be levied only on the products in question consigned for final consumption to that area. When the constitutional law of the importing Member does not permit the levying of countervailing duties on such a basis, the importing Member may levy the countervailing duties without limitation only if (a) the exporters shall have been given an opportunity to cease exporting at subsidized prices to the area concerned or otherwise give assurances pursuant to Article 18, and adequate assurances in this regard have not been promptly given, and (b) such duties cannot be levied only on products of specific producers which supply the area in question.

16.4 Where two or more countries have reached under the provisions of paragraph 8(a) of Article XXIV of GATT 1994 such a level of integration that they have the characteristics of a single, unified market, the industry in the entire area of integration shall be taken to be the domestic industry referred to in paragraphs 1 and 2.

16.5 The provisions of paragraph 6 of Article 15 shall be applicable to this Article.

Article 17

Provisional Measures

17.1 Provisional measures may be applied only if:

- (a) an investigation has been initiated in accordance with the provisions of Article 11, a public notice has been given to that effect and interested Members and interested parties have been given adequate opportunities to submit information and make comments;
- (b) a preliminary affirmative determination has been made that a subsidy exists and that there is injury to a domestic industry caused by subsidized imports; and
- (c) the authorities concerned judge such measures necessary to prevent injury being caused during the investigation.

17.2 Provisional measures may take the form of provisional countervailing duties guaranteed by cash deposits or bonds equal to the amount of the provisionally calculated amount of subsidization.

17.3 Provisional measures shall not be applied sooner than 60 days from the date of initiation of the investigation.

17.4 The application of provisional measures shall be limited to as short a period as possible, not exceeding four months.

17.5 The relevant provisions of Article 19 shall be followed in the application of provisional measures.

Article 18

Undertakings

18.1 Proceedings may⁴⁹ be suspended or terminated without the imposition of provisional measures or countervailing duties upon receipt of satisfactory voluntary undertakings under which:

- (a) the government of the exporting Member agrees to eliminate or limit the subsidy or take other measures concerning its effects; or
- (b) the exporter agrees to revise its prices so that the investigating authorities are satisfied that the injurious effect of the subsidy is eliminated. Price increases under such undertakings shall not be higher than necessary to eliminate the amount of the subsidy. It is desirable that the price increases be less than the amount of the subsidy if such increases would be adequate to remove the injury to the domestic industry.

18.2 Undertakings shall not be sought or accepted unless the authorities of the importing Member have made a preliminary affirmative determination of subsidization and injury caused by such subsidization and, in case of undertakings from exporters, have obtained the consent of the exporting Member.

18.3 Undertakings offered need not be accepted if the authorities of the importing Member consider their acceptance impractical, for example if the number of actual or potential exporters is too great, or for other reasons, including reasons of general policy. Should the case arise and where practicable, the authorities shall provide to the exporter the reasons which have led them to consider acceptance of an undertaking as inappropriate, and shall, to the extent possible, give the exporter an opportunity to make comments thereon.

18.4 If an undertaking is accepted, the investigation of subsidization and injury shall nevertheless be completed if the exporting Member so desires or the importing Member so decides. In such a case, if a negative determination of subsidization or injury is made, the undertaking shall automatically lapse, except in cases where such a determination is due in large part to the existence of an undertaking. In such cases, the authorities concerned may require that an undertaking be maintained for a reasonable period consistent with the provisions of this Agreement. In the event that an affirmative determination of subsidization and injury is made, the undertaking shall continue consistent with its terms and the provisions of this Agreement.

18.5 Price undertakings may be suggested by the authorities of the importing Member, but no exporter shall be forced to enter into such undertakings. The fact that governments or exporters do not offer such undertakings, or do not accept an invitation to do so, shall in no way prejudice the consideration of the case. However, the authorities are free to determine that a threat of injury is more likely to be realized if the subsidized imports continue.

18.6 Authorities of an importing Member may require any government or exporter from whom an undertaking has been accepted to provide periodically information relevant to the fulfillment of such an undertaking, and to permit verification of pertinent data. In case of violation of an undertaking, the authorities of the importing Member may take, under this Agreement in conformity with its provisions, expeditious actions which may constitute immediate application of provisional measures using the best information available. In such cases, definitive duties may be levied in accordance with

⁴⁹The word "may" shall not be interpreted to allow the simultaneous continuation of proceedings with the implementation of undertakings, except as provided in paragraph 4.

this Agreement on products entered for consumption not more than 90 days before the application of such provisional measures, except that any such retroactive assessment shall not apply to imports entered before the violation of the undertaking.

Article 19

Imposition and Collection of Countervailing Duties

19.1 If, after reasonable efforts have been made to complete consultations, a Member makes a final determination of the existence and amount of the subsidy and that, through the effects of the subsidy, the subsidized imports are causing injury, it may impose a countervailing duty in accordance with the provisions of this Article unless the subsidy or subsidies are withdrawn.

19.2 The decision whether or not to impose a countervailing duty in cases where all requirements for the imposition have been fulfilled, and the decision whether the amount of the countervailing duty to be imposed shall be the full amount of the subsidy or less, are decisions to be made by the authorities of the importing Member. It is desirable that the imposition should be permissive in the territory of all Members, that the duty should be less than the total amount of the subsidy if such lesser duty would be adequate to remove the injury to the domestic industry, and that procedures should be established which would allow the authorities concerned to take due account of representations made by domestic interested parties⁵⁰ whose interests might be adversely affected by the imposition of a countervailing duty.

19.3 When a countervailing duty is imposed in respect of any product, such countervailing duty shall be levied, in the appropriate amounts in each case, on a non-discriminatory basis on imports of such product from all sources found to be subsidized and causing injury, except as to imports from those sources which have renounced any subsidies in question or from which undertakings under the terms of this Agreement have been accepted. Any exporter whose exports are subject to a definitive countervailing duty but who was not actually investigated for reasons other than a refusal to cooperate, shall be entitled to an expedited review in order that the investigating authorities promptly establish an individual countervailing duty rate for that exporter.

19.4 No countervailing duty shall be levied⁵¹ on any imported product in excess of the amount of the subsidy found to exist, calculated in terms of subsidization per unit of the subsidized and exported product.

Article 20

Retroactivity

20.1 Provisional measures and countervailing duties shall only be applied to products which enter for consumption after the time when the decision under paragraph 1 of Article 17 and paragraph 1 of Article 19, respectively, enters into force, subject to the exceptions set out in this Article.

20.2 Where a final determination of injury (but not of a threat thereof or of a material retardation of the establishment of an industry) is made or, in the case of a final determination of a threat of injury,

⁵⁰For the purpose of this paragraph, the term "domestic interested parties" shall include consumers and industrial users of the imported product subject to investigation.

⁵¹As used in this Agreement "levy" shall mean the definitive or final legal assessment or collection of a duty or tax.

where the effect of the subsidized imports would, in the absence of the provisional measures, have led to a determination of injury, countervailing duties may be levied retroactively for the period for which provisional measures, if any, have been applied.

20.3 If the definitive countervailing duty is higher than the amount guaranteed by the cash deposit or bond, the difference shall not be collected. If the definitive duty is less than the amount guaranteed by the cash deposit or bond, the excess amount shall be reimbursed or the bond released in an expeditious manner.

20.4 Except as provided in paragraph 2, where a determination of threat of injury or material retardation is made (but no injury has yet occurred) a definitive countervailing duty may be imposed only from the date of the determination of threat of injury or material retardation, and any cash deposit made during the period of the application of provisional measures shall be refunded and any bonds released in an expeditious manner.

20.5 Where a final determination is negative, any cash deposit made during the period of the application of provisional measures shall be refunded and any bonds released in an expeditious manner.

20.6 In critical circumstances where for the subsidized product in question the authorities find that injury which is difficult to repair is caused by massive imports in a relatively short period of a product benefiting from subsidies paid or bestowed inconsistently with the provisions of GATT 1994 and of this Agreement and where it is deemed necessary, in order to preclude the recurrence of such injury, to assess countervailing duties retroactively on those imports, the definitive countervailing duties may be assessed on imports which were entered for consumption not more than 90 days prior to the date of application of provisional measures.

Article 21

Duration and Review of Countervailing Duties and Undertakings

21.1 A countervailing duty shall remain in force only as long as and to the extent necessary to counteract subsidization which is causing injury.

21.2 The authorities shall review the need for the continued imposition of the duty, where warranted, on their own initiative or, provided that a reasonable period of time has elapsed since the imposition of the definitive countervailing duty, upon request by any interested party which submits positive information substantiating the need for a review. Interested parties shall have the right to request the authorities to examine whether the continued imposition of the duty is necessary to offset subsidization, whether the injury would be likely to continue or recur if the duty were removed or varied, or both. If, as a result of the review under this paragraph, the authorities determine that the countervailing duty is no longer warranted, it shall be terminated immediately.

21.3 Notwithstanding the provisions of paragraphs 1 and 2, any definitive countervailing duty shall be terminated on a date not later than five years from its imposition (or from the date of the most recent review under paragraph 2 if that review has covered both subsidization and injury, or under this paragraph), unless the authorities determine, in a review initiated before that date on their own initiative or upon a duly substantiated request made by or on behalf of the domestic industry within a reasonable period of time prior to that date, that the expiry of the duty would be likely to lead to continuation

22.4 A public notice of the imposition of provisional measures shall set forth, or otherwise make available through a separate report, sufficiently detailed explanations for the preliminary determinations on the existence of a subsidy and injury and shall refer to the matters of fact and law which have led to arguments being accepted or rejected. Such a notice or report shall, due regard being paid to the requirement for the protection of confidential information, contain in particular:

- (i) the names of the suppliers or, when this is impracticable, the supplying countries involved;
- (ii) a description of the product which is sufficient for customs purposes;
- (iii) the amount of subsidy established and the basis on which the existence of a subsidy has been determined;
- (iv) considerations relevant to the injury determination as set out in Article 15;
- (v) the main reasons leading to the determination.

22.5 A public notice of conclusion or suspension of an investigation in the case of an affirmative determination providing for the imposition of a definitive duty or the acceptance of an undertaking shall contain, or otherwise make available through a separate report, all relevant information on the matters of fact and law and reasons which have led to the imposition of final measures or the acceptance of an undertaking, due regard being paid to the requirement for the protection of confidential information. In particular, the notice or report shall contain the information described in paragraph 4, as well as the reasons for the acceptance or rejection of relevant arguments or claims made by interested Members and by the exporters and importers.

22.6 A public notice of the termination or suspension of an investigation following the acceptance of an undertaking pursuant to Article 18 shall include, or otherwise make available through a separate report, the non-confidential part of this undertaking.

22.7 The provisions of this Article shall apply *mutatis mutandis* to the initiation and completion of reviews pursuant to Article 21 and to decisions under Article 20 to apply duties retroactively.

Article 23

Judicial Review

Each Member whose national legislation contains provisions on countervailing duty measures shall maintain judicial, arbitral or administrative tribunals or procedures for the purpose, *inter alia*, of the prompt review of administrative actions relating to final determinations and reviews of determinations within the meaning of Article 21. Such tribunals or procedures shall be independent of the authorities responsible for the determination or review in question, and shall provide all interested parties who participated in the administrative proceeding and are directly and individually affected by the administrative actions with access to review.

or recurrence of subsidization and injury.⁵² The duty may remain in force pending the outcome of such a review.

21.4 The provisions of Article 12 regarding evidence and procedure shall apply to any review carried out under this Article. Any such review shall be carried out expeditiously and shall normally be concluded within 12 months of the date of initiation of the review.

21.5 The provisions of this Article shall apply *mutatis mutandis* to undertakings accepted under Article 18.

Article 22

Public Notice and Explanation of Determinations

22.1 When the authorities are satisfied that there is sufficient evidence to justify the initiation of an investigation pursuant to Article 11, the Member or Members the products of which are subject to such investigation and other interested parties known to the investigating authorities to have an interest therein shall be notified and a public notice shall be given.

22.2 A public notice of the initiation of an investigation shall contain, or otherwise make available through a separate report⁵³, adequate information on the following:

- (i) the name of the exporting country or countries and the product involved;
- (ii) the date of initiation of the investigation;
- (iii) a description of the subsidy practice or practices to be investigated;
- (iv) a summary of the factors on which the allegation of injury is based;
- (v) the address to which representations by interested Members and interested parties should be directed; and
- (vi) the time-limits allowed to interested Members and interested parties for making their views known.

22.3 Public notice shall be given of any preliminary or final determination, whether affirmative or negative, of any decision to accept an undertaking pursuant to Article 18, of the termination of such an undertaking, and of the termination of a definitive countervailing duty. Each such notice shall set forth, or otherwise make available through a separate report, in sufficient detail the findings and conclusions reached on all issues of fact and law considered material by the investigating authorities. All such notices and reports shall be forwarded to the Member or Members the products of which are subject to such determination or undertaking and to other interested parties known to have an interest therein.

⁵²When the amount of the countervailing duty is assessed on a retrospective basis, a finding in the most recent assessment proceeding that no duty is to be levied shall not by itself require the authorities to terminate the definitive duty.

⁵³Where authorities provide information and explanations under the provisions of this Article in a separate report, they shall ensure that such report is readily available to the public.

PART VI: INSTITUTIONS

*Article 24**Committee on Subsidies and Countervailing Measures and Subsidiary Bodies*

24.1 There is hereby established a Committee on Subsidies and Countervailing Measures composed of representatives from each of the Members. The Committee shall elect its own Chairman and shall meet not less than twice a year and otherwise as envisaged by relevant provisions of this Agreement at the request of any Member. The Committee shall carry out responsibilities as assigned to it under this Agreement or by the Members and it shall afford Members the opportunity of consulting on any matter relating to the operation of the Agreement or the furtherance of its objectives. The WTO Secretariat shall act as the secretariat to the Committee.

24.2 The Committee may set up subsidiary bodies as appropriate.

24.3 The Committee shall establish a Permanent Group of Experts composed of five independent persons, highly qualified in the fields of subsidies and trade relations. The experts will be elected by the Committee and one of them will be replaced every year. The PGE may be requested to assist a panel, as provided for in paragraph 5 of Article 4. The Committee may also seek an advisory opinion on the existence and nature of any subsidy.

24.4 The PGE may be consulted by any Member and may give advisory opinions on the nature of any subsidy proposed to be introduced or currently maintained by that Member. Such advisory opinions will be confidential and may not be invoked in proceedings under Article 7.

24.5 In carrying out their functions, the Committee and any subsidiary bodies may consult with and seek information from any source they deem appropriate. However, before the Committee or a subsidiary body seeks such information from a source within the jurisdiction of a Member, it shall inform the Member involved.

PART VII: NOTIFICATION AND SURVEILLANCE

*Article 25**Notifications*

25.1 Members agree that, without prejudice to the provisions of paragraph 1 of Article XVI of GATT 1994, their notifications of subsidies shall be submitted not later than 30 June of each year and shall conform to the provisions of paragraphs 2 through 6.

25.2 Members shall notify any subsidy as defined in paragraph 1 of Article 1, which is specific within the meaning of Article 2, granted or maintained within their territories.

25.3 The content of notifications should be sufficiently specific to enable other Members to evaluate the trade effects and to understand the operation of notified subsidy programmes. In this connection,

and without prejudice to the contents and form of the questionnaire on subsidies⁵⁴, Members shall ensure that their notifications contain the following information:

- (i) form of a subsidy (i.e. grant, loan, tax concession, etc.);
- (ii) subsidy per unit or, in cases where this is not possible, the total amount or the annual amount budgeted for that subsidy (indicating, if possible, the average subsidy per unit in the previous year);
- (iii) policy objective and/or purpose of a subsidy;
- (iv) duration of a subsidy and/or any other time-limits attached to it;
- (v) statistical data permitting an assessment of the trade effects of a subsidy.

25.4 Where specific points in paragraph 3 have not been addressed in a notification, an explanation shall be provided in the notification itself.

25.5 If subsidies are granted to specific products or sectors, the notifications should be organized by product or sector.

25.6 Members which consider that there are no measures in their territories requiring notification under paragraph 1 of Article XVI of GATT 1994 and this Agreement shall so inform the Secretariat in writing.

25.7 Members recognize that notification of a measure does not prejudice either its legal status under GATT 1994 and this Agreement, the effects under this Agreement, or the nature of the measure itself.

25.8 Any Member may, at any time, make a written request for information on the nature and extent of any subsidy granted or maintained by another Member (including any subsidy referred to in Part IV), or for an explanation of the reasons for which a specific measure has been considered as not subject to the requirement of notification.

25.9 Members so requested shall provide such information as quickly as possible and in a comprehensive manner, and shall be ready, upon request, to provide additional information to the requesting Member. In particular, they shall provide sufficient details to enable the other Member to assess their compliance with the terms of this Agreement. Any Member which considers that such information has not been provided may bring the matter to the attention of the Committee.

25.10 Any Member which considers that any measure of another Member having the effects of a subsidy has not been notified in accordance with the provisions of paragraph 1 of Article XVI of GATT 1994 and this Article may bring the matter to the attention of such other Member. If the alleged subsidy is not thereafter notified promptly, such Member may itself bring the alleged subsidy in question to the notice of the Committee.

25.11 Members shall report without delay to the Committee all preliminary or final actions taken with respect to countervailing duties. Such reports shall be available in the Secretariat for inspection by other Members. Members shall also submit, on a semi-annual basis, reports on any countervailing duty actions taken within the preceding six months. The semi-annual reports shall be submitted on an agreed standard form.

⁵⁴The Committee shall establish a Working Party to review the contents and form of the questionnaire as contained in BISD 9S/193-194.

25.12 Each Member shall notify the Committee (a) which of its authorities are competent to initiate and conduct investigations referred to in Article 11 and (b) its domestic procedures governing the initiation and conduct of such investigations.

Article 26

Surveillance

26.1 The Committee shall examine new and full notifications submitted under paragraph 1 of Article XVI of GATT 1994 and paragraph 1 of Article 25 of this Agreement at special sessions held every third year. Notifications submitted in the intervening years (updating notifications) shall be examined at each regular meeting of the Committee.

26.2 The Committee shall examine reports submitted under paragraph 11 of Article 25 at each regular meeting of the Committee.

PART VIII: DEVELOPING COUNTRY MEMBERS

Article 27

Special and Differential Treatment of Developing Country Members

27.1 Members recognize that subsidies may play an important role in economic development programmes of developing country Members.

27.2 The prohibition of paragraph 1(a) of Article 3 shall not apply to:

- (a) developing country Members referred to in Annex VII.
- (b) other developing country Members for a period of eight years from the date of entry into force of the WTO Agreement, subject to compliance with the provisions in paragraph 4.

27.3 The prohibition of paragraph 1(b) of Article 3 shall not apply to developing country Members for a period of five years, and shall not apply to least developed country Members for a period of eight years, from the date of entry into force of the WTO Agreement.

27.4 Any developing country Member referred to in paragraph 2(b) shall phase out its export subsidies within the eight-year period, preferably in a progressive manner. However, a developing country Member shall not increase the level of its export subsidies⁵⁵, and shall eliminate them within a period shorter than that provided for in this paragraph when the use of such export subsidies is inconsistent with its development needs. If a developing country Member deems it necessary to apply such subsidies beyond the 8-year period, it shall not later than one year before the expiry of this period enter into consultation with the Committee, which will determine whether an extension of this period is justified, after examining all the relevant economic, financial and development needs of the developing country Member in question. If the Committee determines that the extension is justified, the developing country Member concerned shall hold annual consultations with the Committee to determine the necessity of

⁵⁵For a developing country Member not granting export subsidies as of the date of entry into force of the WTO Agreement, this paragraph shall apply on the basis of the level of export subsidies granted in 1986.

maintaining the subsidies. If no such determination is made by the Committee, the developing country Member shall phase out the remaining export subsidies within two years from the end of the last authorized period.

27.5 A developing country Member which has reached export competitiveness in any given product shall phase out its export subsidies for such product(s) over a period of two years. However, for a developing country Member which is referred to in Annex VII and which has reached export competitiveness in one or more products, export subsidies on such products shall be gradually phased out over a period of eight years.

27.6 Export competitiveness in a product exists if a developing country Member's exports of that product have reached a share of at least 3.25 per cent in world trade of that product for two consecutive calendar years. Export competitiveness shall exist either (a) on the basis of notification by the developing country Member having reached export competitiveness, or (b) on the basis of a computation undertaken by the Secretariat at the request of any Member. For the purpose of this paragraph, a product is defined as a section heading of the Harmonized System Nomenclature. The Committee shall review the operation of this provision five years from the date of the entry into force of the WTO Agreement.

27.7 The provisions of Article 4 shall not apply to a developing country Member in the case of export subsidies which are in conformity with the provisions of paragraphs 2 through 5. The relevant provisions in such a case shall be those of Article 7.

27.8 There shall be no presumption in terms of paragraph 1 of Article 6 that a subsidy granted by a developing country Member results in serious prejudice, as defined in this Agreement. Such serious prejudice, where applicable under the terms of paragraph 9, shall be demonstrated by positive evidence, in accordance with the provisions of paragraphs 3 through 8 of Article 6.

27.9 Regarding actionable subsidies granted or maintained by a developing country Member other than those referred to in paragraph 1 of Article 6, action may not be authorized or taken under Article 7 unless nullification or impairment of tariff concessions or other obligations under GATT 1994 is found to exist as a result of such a subsidy, in such a way as to displace or impede imports of a like product of another Member into the market of the subsidizing developing country Member or unless injury to a domestic industry in the market of an importing Member occurs.

27.10 Any countervailing duty investigation of a product originating in a developing country Member shall be terminated as soon as the authorities concerned determine that:

- (a) the overall level of subsidies granted upon the product in question does not exceed 2 per cent of its value calculated on a per unit basis; or
- (b) the volume of the subsidized imports represents less than 4 per cent of the total imports of the like product in the importing Member, unless imports from developing country Members whose individual shares of total imports represent less than 4 per cent collectively account for more than 9 per cent of the total imports of the like product in the importing Member.

27.11 For those developing country Members within the scope of paragraph 2(b) which have eliminated export subsidies prior to the expiry of the period of eight years from the date of entry into force of the WTO Agreement, and for those developing country Members referred to in Annex VII, the number in paragraph 10(a) shall be 3 per cent rather than 2 per cent. This provision shall apply from the date that the elimination of export subsidies is notified to the Committee, and for so long as export subsidies are not granted by the notifying developing country Member. This provision shall expire eight years from the date of entry into force of the WTO Agreement.

(a) Subsidy programmes falling within the scope of paragraph 1(d) of Article 6 shall not be actionable under Article 7;

(b) With respect to other actionable subsidies, the provisions of paragraph 9 of Article 27 shall apply.

29.3 Subsidy programmes falling within the scope of Article 3 shall be notified to the Committee by the earliest practicable date after the date of entry into force of the WTO Agreement. Further notifications of such subsidies may be made up to two years after the date of entry into force of the WTO Agreement.

29.4 In exceptional circumstances Members referred to in paragraph 1 may be given departures from their notified programmes and measures and their time-frame by the Committee if such departures are deemed necessary for the process of transformation.

PART X: DISPUTE SETTLEMENT

Article 30

The provisions of Articles XXII and XXIII of GATT 1994 as elaborated and applied by the Dispute Settlement Understanding shall apply to consultations and the settlement of disputes under this Agreement, except as otherwise specifically provided herein.

PART XI: FINAL PROVISIONS

Article 31

Provisional Application

The provisions of paragraph 1 of Article 6 and the provisions of Article 8 and Article 9 shall apply for a period of five years, beginning with the date of entry into force of the WTO Agreement. Not later than 180 days before the end of this period, the Committee shall review the operation of those provisions, with a view to determining whether to extend their application, either as presently drafted or in a modified form, for a further period.

Article 32

Other Final Provisions

32.1 No specific action against a subsidy of another Member can be taken except in accordance with the provisions of GATT 1994, as interpreted by this Agreement.⁶⁶

32.2 Reservations may not be entered in respect of any of the provisions of this Agreement without the consent of the other Members.

⁶⁶This paragraph is not intended to preclude action under other relevant provisions of GATT 1994, where appropriate.

27.12 The provisions of paragraphs 10 and 11 shall govern any determination of *de minimis* under paragraph 3 of Article 15.

27.13 The provisions of Part III shall not apply to direct forgiveness of debts, subsidies to cover social costs, in whatever form, including relinquishment of government revenue and other transfer of liabilities when such subsidies are granted within and directly linked to a privatization programme of a developing country Member, provided that both such programme and the subsidies involved are granted for a limited period and notified to the Committee and that the programme results in eventual privatization of the enterprise concerned.

27.14 The Committee shall, upon request by an interested Member, undertake a review of a specific export subsidy practice of a developing country Member to examine whether the practice is in conformity with its development needs.

27.15 The Committee shall, upon request by an interested developing country Member, undertake a review of a specific countervailing measure to examine whether it is consistent with the provisions of paragraphs 10 and 11 as applicable to the developing country Member in question.

PART IX: TRANSITIONAL ARRANGEMENTS

Article 28

Existing Programmes

28.1 Subsidy programmes which have been established within the territory of any Member before the date on which such a Member signed the WTO Agreement and which are inconsistent with the provisions of this Agreement shall be:

(a) notified to the Committee not later than 90 days after the date of entry into force of the WTO Agreement for such Member; and

(b) brought into conformity with the provisions of this Agreement within three years of the date of entry into force of the WTO Agreement for such Member and until then shall not be subject to Part II.

28.2 No Member shall extend the scope of any such programme, nor shall such a programme be renewed upon its expiry.

Article 29

Transformation into a Market Economy

29.1 Members in the process of transformation from a centrally-planned into a market, free-enterprise economy may apply programmes and measures necessary for such a transformation.

29.2 For such Members, subsidy programmes falling within the scope of Article 3, and notified according to paragraph 3, shall be phased out or brought into conformity with Article 3 within a period of seven years from the date of entry into force of the WTO Agreement. In such a case, Article 4 shall not apply. In addition during the same period:

32.3 Subject to paragraph 4, the provisions of this Agreement shall apply to investigations, and reviews of existing measures, initiated pursuant to applications which have been made on or after the date of entry into force for a Member of the WTO Agreement.

32.4 For the purposes of paragraph 3 of Article 21, existing countervailing measures shall be deemed to be imposed on a date not later than the date of entry into force for a Member of the WTO Agreement, except in cases in which the domestic legislation of a Member in force at that date already included a clause of the type provided for in that paragraph.

32.5 Each Member shall take all necessary steps, of a general or particular character, to ensure, not later than the date of entry into force of the WTO Agreement for it, the conformity of its laws, regulations and administrative procedures with the provisions of this Agreement as they may apply to the Member in question.

32.6 Each Member shall inform the Committee of any changes in its laws and regulations relevant to this Agreement and in the administration of such laws and regulations.

32.7 The Committee shall review annually the implementation and operation of this Agreement, taking into account the objectives thereof. The Committee shall inform annually the Council for Trade in Goods of developments during the period covered by such reviews.

32.8 The Annexes to this Agreement constitute an integral part thereof.

ANNEX I

ILLUSTRATIVE LIST OF EXPORT SUBSIDIES

- (a) The provision by governments of direct subsidies to a firm or an industry contingent upon export performance.
- (b) Currency retention schemes or any similar practices which involve a bonus on exports.
- (c) Internal transport and freight charges on export shipments, provided or mandated by governments, on terms more favourable than for domestic shipments.
- (d) The provision by governments or their agencies either directly or indirectly through government-mandated schemes, of imported or domestic products or services for use in the production of exported goods, on terms or conditions more favourable than for provision of like or directly competitive products or services for use in the production of goods for domestic consumption, if (in the case of products) such terms or conditions are more favourable than those commercially available⁵⁷ on world markets to their exporters.
- (e) The full or partial exemption remission, or deferral specifically related to exports, of direct taxes⁵⁸ or social welfare charges paid or payable by industrial or commercial enterprises.⁵⁹
- (f) The allowance of special deductions directly related to exports or export performance, over and above those granted in respect to production for domestic consumption, in the calculation of the base on which direct taxes are charged.

⁵⁷The term "commercially available" means that the choice between domestic and imported products is unrestricted and depends only on commercial considerations.

⁵⁸For the purpose of this Agreement:

The term "direct taxes" shall mean taxes on wages, profits, interests, rents, royalties, and all other forms of income, and taxes on the ownership of real property;

The term "import charges" shall mean tariffs, duties, and other fiscal charges not elsewhere enumerated in this note that are levied on imports;

The term "indirect taxes" shall mean sales, excise, turnover, value added, franchise, stamp, transfer, inventory and equipment taxes, border taxes and all taxes other than direct taxes and import charges;

"Prior-stage" indirect taxes are those levied on goods or services used directly or indirectly in making the product;

"Cumulative" indirect taxes are multi-staged taxes levied where there is no mechanism for subsequent crediting of the tax if the goods or services subject to tax at one stage of production are used in a succeeding stage of production;

"Remission" of taxes includes the refund or rebate of taxes;

"Remission or drawback" includes the full or partial exemption or deferral of import charges.

⁵⁹The Members recognize that deferral need not amount to an export subsidy where, for example, appropriate interest charges are collected. The Members reaffirm the principle that prices for goods in transactions between exporting enterprises and foreign buyers under their or under the same control should for tax purposes be the prices which would be charged between independent enterprises acting at arm's length. Any Member may draw the attention of another Member to administrative or other practices which may contravene this principle and which result in a significant saving of direct taxes in export transactions. In such circumstances the Members shall normally attempt to resolve their differences using the facilities of existing bilateral tax treaties or other specific international mechanisms, without prejudice to the rights and obligations of Members under GATT 1994, including the right of consultation created in the preceding sentence.

Paragraph (e) is not intended to limit a Member from taking measures to avoid the double taxation of foreign-source income earned by its enterprises or the enterprises of another Member.

- (g) The exemption or remission, in respect of the production and distribution of exported products, of indirect taxes⁵⁸ in excess of those levied in respect of the production and distribution of like products when sold for domestic consumption.
- (h) The exemption, remission or deferral of prior-stage cumulative indirect taxes⁵⁸ on goods or services used in the production of exported products in excess of the exemption, remission or deferral of like prior-stage cumulative indirect taxes on goods or services used in the production of like products when sold for domestic consumption; provided, however, that prior-stage cumulative indirect taxes may be exempted, remitted or deferred on exported products even when not exempted, remitted or deferred on like products when sold for domestic consumption, if the prior-stage cumulative indirect taxes are levied on inputs that are consumed in the production of the exported product (making normal allowance for waste).⁶⁰ This item shall be interpreted in accordance with the guidelines on consumption of inputs in the production process contained in Annex II.
- (i) The remission or drawback of import charges⁵⁸ in excess of those levied on imported inputs that are consumed in the production of the exported product (making normal allowance for waste); provided, however, that in particular cases a firm may use a quantity of home market inputs equal to, and having the same quality and characteristics as, the imported inputs as a substitute for them in order to benefit from this provision if the import and the corresponding export operations both occur within a reasonable time period, not to exceed two years. This item shall be interpreted in accordance with the guidelines on consumption of inputs in the production process contained in Annex II and the guidelines in the determination of substitution drawback systems as export subsidies contained in Annex III.
- (j) The provision by governments (or special institutions controlled by governments) of export credit guarantee or insurance programmes, of insurance or guarantee programmes against increases in the cost of exported products or of exchange risk programmes, at premium rates which are inadequate to cover the long-term operating costs and losses of the programmes.
- (k) The grant by governments (or special institutions controlled by and/or acting under the authority of governments) of export credits at rates below those which they actually have to pay for the funds so employed (or would have to pay if they borrowed on international capital markets in order to obtain funds of the same maturity and other credit terms and denominated in the same currency as the export credit), or the payment by them of all or part of the costs incurred by exporters or financial institutions in obtaining credits, in so far as they are used to secure a material advantage in the field of export credit terms.
- Provided, however, that if a Member is a party to an international undertaking on official export credits to which at least twelve original Members to this Agreement are parties as of 1 January 1979 (or a successor undertaking which has been adopted by those original Members), or if in practice a Member applies the interest rates provisions of the relevant undertaking, an export credit practice which is in conformity with those provisions shall not be considered an export subsidy prohibited by this Agreement.
- (l) Any other charge on the public account constituting an export subsidy in the sense of Article XVI of GATT 1994.

⁶⁰Paragraph (h) does not apply to value-added tax systems and border-tax adjustment in lieu thereof; the problem of the excessive remission of value-added taxes is exclusively covered by paragraph (g).

ANNEX II

GUIDELINES ON CONSUMPTION OF INPUTS IN THE PRODUCTION PROCESS⁶¹

I

- Indirect tax rebate schemes can allow for exemption, remission or deferral of prior-stage cumulative indirect taxes levied on inputs that are consumed in the production of the exported product (making normal allowance for waste). Similarly, drawback schemes can allow for the remission or drawback of import charges levied on inputs that are consumed in the production of the exported product (making normal allowance for waste).
- The Illustrative List of Export Subsidies in Annex I of this Agreement makes reference to the term "inputs that are consumed in the production of the exported product" in paragraphs (h) and (i). Pursuant to paragraph (h), indirect tax rebate schemes can constitute an export subsidy to the extent that they result in exemption, remission or deferral of prior-stage cumulative indirect taxes in excess of the amount of such taxes actually levied on inputs that are consumed in the production of the exported product. Pursuant to paragraph (i), drawback schemes can constitute an export subsidy to the extent that they result in a remission or drawback of import charges in excess of those actually levied on inputs that are consumed in the production of the exported product. Both paragraphs stipulate that normal allowance for waste must be made in findings regarding consumption of inputs in the production of the exported product. Paragraph (i) also provides for substitution, where appropriate.

II

- In examining whether inputs are consumed in the production of the exported product, as part of a countervailing duty investigation pursuant to this Agreement, investigating authorities should proceed on the following basis:
- Where it is alleged that an indirect tax rebate scheme, or a drawback scheme, conveys a subsidy by reason of over-rebate or excess drawback of indirect taxes or import charges on inputs consumed in the production of the exported product, the investigating authorities should first determine whether the government of the exporting Member has in place and applies a system or procedure to confirm which inputs are consumed in the production of the exported product and in what amounts. Where such a system or procedure is determined to be applied, the investigating authorities should then examine the system or procedure to see whether it is reasonable, effective for the purpose intended, and based on generally accepted commercial practices in the country of export. The investigating authorities may deem it necessary to carry out, in accordance with paragraph 6 of Article 12, certain practical tests in order to verify information or to satisfy themselves that the system or procedure is being effectively applied.
 - Where there is no such system or procedure, where it is not reasonable, or where it is instituted and considered reasonable but is found not to be applied or not to be applied effectively, a further examination by the exporting Member based on the actual inputs involved would need to be carried out in the context of determining whether an excess payment occurred. If the investigating authorities deemed it necessary, a further examination would be carried out in accordance with paragraph 1.

⁶¹Inputs consumed in the production process are inputs physically incorporated, energy, fuels and oil used in the production process and catalysts which are consumed in the course of their use to obtain the exported product.

3. Investigating authorities should treat inputs as physically incorporated if such inputs are used in the production process and are physically present in the product exported. The Members note that an input need not be present in the final product in the same form in which it entered the production process.

4. In determining the amount of a particular input that is consumed in the production of the exported product, a "normal allowance for waste" should be taken into account, and such waste should be treated as consumed in the production of the exported product. The term "waste" refers to that portion of a given input which does not serve an independent function in the production process, is not consumed in the production of the exported product (for reasons such as inefficiencies) and is not recovered, used or sold by the same manufacturer.

5. The investigating authority's determination of whether the claimed allowance for waste is "normal" should take into account the production process, the average experience of the industry in the country of export, and other technical factors, as appropriate. The investigating authority should bear in mind that an important question is whether the authorities in the exporting Member have reasonably calculated the amount of waste, when such an amount is intended to be included in the tax or duty rebate or remission.

ANNEX III

GUIDELINES IN THE DETERMINATION OF SUBSTITUTION DRAWBACK SYSTEMS AS EXPORT SUBSIDIES

I

Drawback systems can allow for the refund or drawback of import charges on inputs which are consumed in the production process of another product and where the export of this latter product contains domestic inputs having the same quality and characteristics as those substituted for the imported inputs. Pursuant to paragraph (i) of the Illustrative List of Export Subsidies in Annex I, substitution drawback systems can constitute an export subsidy to the extent that they result in an excess drawback of the import charges levied initially on the imported inputs for which drawback is being claimed.

II

In examining any substitution drawback system as part of a countervailing duty investigation pursuant to this Agreement, investigating authorities should proceed on the following basis:

1. Paragraph (i) of the Illustrative List stipulates that home market inputs may be substituted for imported inputs in the production of a product for export provided such inputs are equal in quantity to, and have the same quality and characteristics as, the imported inputs being substituted. The existence of a verification system or procedure is important because it enables the government of the exporting Member to ensure and demonstrate that the quantity of inputs for which drawback is claimed does not exceed the quantity of similar products exported, in whatever form, and that there is not drawback of import charges in excess of those originally levied on the imported inputs in question.
2. Where it is alleged that a substitution drawback system conveys a subsidy, the investigating authorities should first proceed to determine whether the government of the exporting Member has in place and applies a verification system or procedure. Where such a system or procedure is determined to be applied, the investigating authorities should then examine the verification procedures to see whether they are reasonable, effective for the purpose intended, and based on generally accepted commercial practices in the country of export. To the extent that the procedures are determined to meet this test and are effectively applied, no subsidy should be presumed to exist. It may be deemed necessary by the investigating authorities to carry out, in accordance with paragraph 6 of Article 12, certain practical tests in order to verify information or to satisfy themselves that the verification procedures are being effectively applied.
3. Where there are no verification procedures, where they are not reasonable, or where such procedures are instituted and considered reasonable but are found not to be actually applied or not applied effectively, there may be a subsidy. In such cases a further examination by the exporting Member based on the actual transactions involved would need to be carried out to determine whether an excess payment occurred. If the investigating authorities deemed it necessary, a further examination would be carried out in accordance with paragraph 2.
4. The existence of a substitution drawback provision under which exporters are allowed to select particular import shipments on which drawback is claimed should not of itself be considered to convey a subsidy.

5. An excess drawback of import charges in the sense of paragraph (i) would be deemed to exist where governments paid interest on any monies refunded under their drawback schemes, to the extent of the interest actually paid or payable.

ANNEX IV
CALCULATION OF THE TOTAL AD VALOREM SUBSIDIZATION
(PARAGRAPH 1(A) OF ARTICLE 6)⁶²

1. Any calculation of the amount of a subsidy for the purpose of paragraph 1(a) of Article 6 shall be done in terms of the cost to the granting government.
2. Except as provided in paragraphs 3 through 5, in determining whether the overall rate of subsidization exceeds 5 per cent of the value of the product, the value of the product shall be calculated as the total value of the recipient firm's⁶³ sales in the most recent 12-month period, for which sales data is available, preceding the period in which the subsidy is granted.⁶⁴
3. Where the subsidy is tied to the production or sale of a given product, the value of the product shall be calculated as the total value of the recipient firm's sales of that product in the most recent 12-month period, for which sales data is available, preceding the period in which the subsidy is granted.
4. Where the recipient firm is in a start-up situation, serious prejudice shall be deemed to exist if the overall rate of subsidization exceeds 15 per cent of the total funds invested. For purposes of this paragraph, a start-up period will not extend beyond the first year of production.⁶⁵
5. Where the recipient firm is located in an inflationary economy country, the value of the product shall be calculated as the recipient firm's total sales (or sales of the relevant product, if the subsidy is tied) in the preceding calendar year indexed by the rate of inflation experienced in the 12 months preceding the month in which the subsidy is to be given.
6. In determining the overall rate of subsidization in a given year, subsidies given under different programmes and by different authorities in the territory of a Member shall be aggregated.
7. Subsidies granted prior to the date of entry into force of the WTO Agreement, the benefits of which are allocated to future production, shall be included in the overall rate of subsidization.
8. Subsidies which are non-actionable under relevant provisions of this Agreement shall not be included in the calculation of the amount of a subsidy for the purpose of paragraph 1(a) of Article 6.

⁶²An understanding among Members should be developed, as necessary, on matters which are not specified in this Annex or which need further clarification for the purposes of paragraph 1(a) of Article 6.

⁶³The recipient firm is a firm in the territory of the subsidizing Member.

⁶⁴In the case of tax-related subsidies the value of the product shall be calculated as the total value of the recipient firm's sales in the fiscal year in which the tax-related measure was earned.

⁶⁵Start-up situations include instances where financial commitments for product development or construction of facilities to manufacture products benefiting from the subsidy have been made, even though production has not begun.

ANNEX V

PROCEDURES FOR DEVELOPING INFORMATION CONCERNING SERIOUS PREJUDICE

1. Every Member shall cooperate in the development of evidence to be examined by a panel in procedures under paragraphs 4 through 6 of Article 7. The parties to the dispute and any third-country Member concerned shall notify to the DSB, as soon as the provisions of paragraph 4 of Article 7 have been invoked, the organization responsible for administration of this provision within its territory and the procedures to be used to comply with requests for information.
2. In cases where matters are referred to the DSB under paragraph 4 of Article 7, the DSB shall, upon request, initiate the procedure to obtain such information from the government of the subsidizing Member as necessary to establish the existence and amount of subsidization, the value of total sales of the subsidized firms, as well as information necessary to analyze the adverse effects caused by the subsidized product.⁶⁶ This process may include, where appropriate, presentation of questions to the government of the subsidizing Member and of the complaining Member to collect information, as well as to clarify and obtain elaboration of information available to the parties to a dispute through the notification procedures set forth in Part VII.⁶⁷
3. In the case of effects in third-country markets, a party to a dispute may collect information, including through the use of questions to the government of the third-country Member, necessary to analyse adverse effects, which is not otherwise reasonably available from the complaining Member or the subsidizing Member. This requirement should be administered in such a way as not to impose an unreasonable burden on the third-country Member. In particular, such a Member is not expected to make a market or price analysis specially for that purpose. The information to be supplied is that which is already available or can be readily obtained by this Member (e.g. most recent statistics which have already been gathered by relevant statistical services but which have not yet been published, customs data concerning imports and declared values of the products concerned, etc.). However, if a party to a dispute undertakes a detailed market analysis at its own expense, the task of the person or firm conducting such an analysis shall be facilitated by the authorities of the third-country Member and such a person or firm shall be given access to all information which is not normally maintained confidential by the government.

4. The DSB shall designate a representative to serve the function of facilitating the information-gathering process. The sole purpose of the representative shall be to ensure the timely development of the information necessary to facilitate expeditious subsequent multilateral review of the dispute. In particular, the representative may suggest ways to most efficiently solicit necessary information as well as encourage the cooperation of the parties.

5. The information-gathering process outlined in paragraphs 2 through 4 shall be completed within 60 days of the date on which the matter has been referred to the DSB under paragraph 4 of Article 7. The information obtained during this process shall be submitted to the panel established by the DSB in accordance with the provisions of Part X. This information should include, *inter alia*, data concerning the amount of the subsidy in question (and, where appropriate, the value of total sales of the subsidized firms), prices of the subsidized product, prices of the non-subsidized product, prices of other suppliers to the market, changes in the supply of the subsidized product to the market in question and changes

⁶⁶In cases where the existence of serious prejudice has to be demonstrated.

⁶⁷The information-gathering process by the DSB shall take into account the need to protect information which is by nature confidential or which is provided on a confidential basis by any Member involved in this process.

in market shares. It should also include rebuttal evidence, as well as such supplemental information as the panel deems relevant in the course of reaching its conclusions.

6. If the subsidizing and/or third-country Member fail to cooperate in the information-gathering process, the complaining Member will present its case of serious prejudice, based on evidence available to it, together with facts and circumstances of the non-cooperation of the subsidizing and/or third-country Member. Where information is unavailable due to non-cooperation by the subsidizing and/or third-country Member, the panel may complete the record as necessary relying on best information otherwise available.
7. In making its determination, the panel should draw adverse inferences from instances of non-cooperation by any party involved in the information-gathering process.
8. In making a determination to use either best information available or adverse inferences, the panel shall consider the advice of the DSB representative nominated under paragraph 4 as to the reasonableness of any requests for information and the efforts made by parties to comply with these requests in a cooperative and timely manner.
9. Nothing in the information-gathering process shall limit the ability of the panel to seek such additional information it deems essential to a proper resolution to the dispute, and which was not adequately sought or developed during that process. However, ordinarily the panel should not request additional information to complete the record where the information would support a particular party's position and the absence of that information in the record is the result of unreasonable non-cooperation by that party in the information-gathering process.

ANNEX VI

PROCEDURES FOR ON-THE-SPOT INVESTIGATIONS PURSUANT TO
PARAGRAPH 6 OF ARTICLE 12

1. Upon initiation of an investigation, the authorities of the exporting Member and the firms known to be concerned should be informed of the intention to carry out on-the-spot investigations.
2. If in exceptional circumstances it is intended to include non-governmental experts in the investigating team, the firms and the authorities of the exporting Member should be so informed. Such non-governmental experts should be subject to effective sanctions for breach of confidentiality requirements.
3. It should be standard practice to obtain explicit agreement of the firms concerned in the exporting Member before the visit is finally scheduled.
4. As soon as the agreement of the firms concerned has been obtained, the investigating authorities should notify the authorities of the exporting Member of the names and addresses of the firms to be visited and the dates agreed.
5. Sufficient advance notice should be given to the firms in question before the visit is made.
6. Visits to explain the questionnaire should only be made at the request of an exporting firm. In case of such a request the investigating authorities may place themselves at the disposal of the firm; such a visit may only be made if (a) the authorities of the importing Member notify the representatives of the government of the Member in question and (b) the latter do not object to the visit.
7. As the main purpose of the on-the-spot investigation is to verify information provided or to obtain further details, it should be carried out after the response to the questionnaire has been received unless the firm agrees to the contrary and the government of the exporting Member is informed by the investigating authorities of the anticipated visit and does not object to it; further, it should be standard practice prior to the visit to advise the firms concerned of the general nature of the information to be verified and of any further information which needs to be provided, though this should not preclude requests to be made on the spot for further details to be provided in the light of information obtained.
8. Enquiries or questions put by the authorities or firms of the exporting Members and essential to a successful on-the-spot investigation should, whenever possible, be answered before the visit is made.

ANNEX VII

DEVELOPING COUNTRY MEMBERS REFERRED TO
IN PARAGRAPH 2(A) OF ARTICLE 27

The developing country Members not subject to the provisions of paragraph 1(a) of Article 3 under the terms of paragraph 2(a) of Article 27 are:

- (a) Least-developed countries designated as such by the United Nations which are Members of the WTO.
- (b) Each of the following developing countries which are Members of the WTO shall be subject to the provisions which are applicable to other developing country Members according to paragraph 2(b) of Article 27 when GNP per capita has reached \$1,000 per annum⁶⁸: Bolivia, Cameroon, Congo, Côte d'Ivoire, Dominican Republic, Egypt, Ghana, Guatemala, Guyana, India, Indonesia, Kenya, Morocco, Nicaragua, Nigeria, Pakistan, Philippines, Senegal, Sri Lanka and Zimbabwe.

⁶⁸The inclusion of developing country Members in the list in paragraph (b) is based on the most recent data from the World Bank on GNP per capita.

Agreement on Safeguards, 1994

AGREEMENT ON SAFEGUARDS

Members,

Having in mind the overall objective of the Members to improve and strengthen the international trading system based on GATT 1994;

Recognizing the need to clarify and reinforce the disciplines of GATT 1994, and specifically those of its Article XIX (Emergency Action on Imports of Particular Products), to re-establish multilateral control over safeguards and eliminate measures that escape such control;

Recognizing the importance of structural adjustment and the need to enhance rather than limit competition in international markets; and

Recognizing further that, for these purposes, a comprehensive agreement, applicable to all Members and based on the basic principles of GATT 1994, is called for;

Hereby *agree* as follows:

Article 1

General Provision

This Agreement establishes rules for the application of safeguard measures which shall be understood to mean those measures provided for in Article XIX of GATT 1994.

Article 2

Conditions

1. A Member¹ may apply a safeguard measure to a product only if that Member has determined, pursuant to the provisions set out below, that such product is being imported into its territory in such increased quantities, absolute or relative to domestic production, and under such conditions as to cause or threaten to cause serious injury to the domestic industry that produces like or directly competitive products.

2. Safeguard measures shall be applied to a product being imported irrespective of its source.

Article 3

Investigation

¹ A customs union may apply a safeguard measure as a single unit or on behalf of a member State. When a customs union applies a safeguard measure as a single unit, all the requirements for the determination of serious injury or threat thereof under this Agreement shall be based on the conditions existing in the customs union as a whole. When a safeguard measure is applied on behalf of a member State, all the requirements for the determination of serious injury or threat thereof shall be based on the conditions existing in that member State and the measure shall be limited to that member State. Nothing in this Agreement prejudices the interpretation of the relationship between Article XIX and paragraph 8 of Article XXIV of GATT 1994.

1. A Member may apply a safeguard measure only following an investigation by the competent authorities of that Member pursuant to procedures previously established and made public in consonance with Article X of GATT 1994. This investigation shall include reasonable public notice to all interested parties and public hearings or other appropriate means in which importers, exporters and other interested parties could present evidence and their views, including the opportunity to respond to the presentations of other parties and to submit their views, *inter alia*, as to whether or not the application of a safeguard measure would be in the public interest. The competent authorities shall publish a report setting forth their findings and reasoned conclusions reached on all pertinent issues of fact and law.

2. Any information which is by nature confidential or which is provided on a confidential basis shall, upon cause being shown, be treated as such by the competent authorities. Such information shall not be disclosed without permission of the party submitting it. Parties providing confidential information may be requested to furnish non-confidential summaries thereof or, if such parties indicate that such information cannot be summarized, the reasons why a summary cannot be provided. However, if the competent authorities find that a request for confidentiality is not warranted and if the party concerned is either unwilling to make the information public or to authorize its disclosure in generalized or summary form, the authorities may disregard such information unless it can be demonstrated to their satisfaction from appropriate sources that the information is correct.

Article 4

Determination of Serious Injury or Threat Thereof

1. For the purposes of this Agreement:

- (a) "serious injury" shall be understood to mean a significant overall impairment in the position of a domestic industry;
- (b) "threat of serious injury" shall be understood to mean serious injury that is clearly imminent, in accordance with the provisions of paragraph 2. A determination of the existence of a threat of serious injury shall be based on facts and not merely on allegation, conjecture or remote possibility; and
- (c) in determining injury or threat thereof, a "domestic industry" shall be understood to mean the producers as a whole of the like or directly competitive products operating within the territory of a Member, or those whose collective output of the like or directly competitive products constitutes a major proportion of the total domestic production of those products.

2. (a) In the investigation to determine whether increased imports have caused or are threatening to cause serious injury to a domestic industry under the terms of this Agreement, the competent authorities shall evaluate all relevant factors of an objective and quantifiable nature having a bearing on the situation of that industry, in particular, the rate and amount of the increase in imports of the product concerned in absolute and relative terms, the share of the domestic market taken by increased imports, changes in the level of sales, production, productivity, capacity utilization, profits and losses, and employment.

(b) The determination referred to in subparagraph (a) shall not be made unless this investigation demonstrates, on the basis of objective evidence, the existence of the causal link between increased imports of the product concerned and serious injury or threat thereof. When factors other than increased imports are causing injury to the

domestic industry at the same time, such injury shall not be attributed to increased imports.

- (c) The competent authorities shall publish promptly, in accordance with the provisions of Article 3, a detailed analysis of the case under investigation as well as a demonstration of the relevance of the factors examined.

Article 5

Application of Safeguard Measures

1. A Member shall apply safeguard measures only to the extent necessary to prevent or remedy serious injury and to facilitate adjustment. If a quantitative restriction is used, such a measure shall not reduce the quantity of imports below the level of a recent period which shall be the average of imports in the last three representative years for which statistics are available, unless clear justification is given that a different level is necessary to prevent or remedy serious injury. Members should choose measures most suitable for the achievement of these objectives.
2. (a) In cases in which a quota is allocated among supplying countries, the Member applying the restrictions may seek agreement with respect to the allocation of shares in the quota with all other Members having a substantial interest in supplying the product concerned. In cases in which this method is not reasonably practicable, the Member concerned shall allot to Members having a substantial interest in supplying the product shares based upon the proportions, supplied by such Members during a previous representative period, of the total quantity or value of imports of the product, due account being taken of any special factors which may have affected or may be affecting the trade in the product.

- (b) A Member may depart from the provisions in subparagraph (a) provided that consultations under paragraph 3 of Article 12 are conducted under the auspices of the Committee on Safeguards provided for in paragraph 1 of Article 13 and that clear demonstration is provided to the Committee that (i) imports from certain Members have increased in disproportionate percentage in relation to the total increase of imports of the product concerned in the representative period, (ii) the reasons for the departure from the provisions in subparagraph (a) are justified, and (iii) the conditions of such departure are equitable to all suppliers of the product concerned. The duration of any such measure shall not be extended beyond the initial period under paragraph 1 of Article 7. The departure referred to above shall not be permitted in the case of threat of serious injury.

Article 6

Provisional Safeguard Measures

In critical circumstances where delay would cause damage which it would be difficult to repair, a Member may take a provisional safeguard measure pursuant to a preliminary determination that there is clear evidence that increased imports have caused or are threatening to cause serious injury. The duration of the provisional measure shall not exceed 200 days, during which period the pertinent requirements of Articles 2 through 7 and 12 shall be met. Such measures should take the form of tariff increases to be promptly refunded if the subsequent investigation referred to in paragraph 2 of Article 4 does not determine that increased imports have caused or threatened to cause

serious injury to a domestic industry. The duration of any such provisional measure shall be counted as a part of the initial period and any extension referred to in paragraphs 1, 2 and 3 of Article 7.

Article 7

Duration and Review of Safeguard Measures

1. A Member shall apply safeguard measures only for such period of time as may be necessary to prevent or remedy serious injury and to facilitate adjustment. The period shall not exceed four years, unless it is extended under paragraph 2.
2. The period mentioned in paragraph 1 may be extended provided that the competent authorities of the importing Member have determined, in conformity with the procedures set out in Articles 2, 3, 4 and 5, that the safeguard measure continues to be necessary to prevent or remedy serious injury and that there is evidence that the industry is adjusting, and provided that the pertinent provisions of Articles 8 and 12 are observed.
3. The total period of application of a safeguard measure including the period of application of any provisional measure, the period of initial application and any extension thereof, shall not exceed eight years.
4. In order to facilitate adjustment in a situation where the expected duration of a safeguard measure as notified under the provisions of paragraph 1 of Article 12 is over one year, the Member applying the measure shall progressively liberalize it at regular intervals during the period of application. If the duration of the measure exceeds three years, the Member applying such a measure shall review the situation not later than the mid-term of the measure and, if appropriate, withdraw it or increase the pace of liberalization. A measure extended under paragraph 2 shall not be more restrictive than it was at the end of the initial period, and should continue to be liberalized.
5. No safeguard measure shall be applied again to the import of a product which has been subject to such a measure, taken after the date of entry into force of the WTO Agreement, for a period of time equal to that during which such measure had been previously applied, provided that the period of non-application is at least two years.
6. Notwithstanding the provisions of paragraph 5, a safeguard measure with a duration of 180 days or less may be applied again to the import of a product if:

- (a) at least one year has elapsed since the date of introduction of a safeguard measure on the import of that product; and
- (b) such a safeguard measure has not been applied on the same product more than twice in the five-year period immediately preceding the date of introduction of the measure.

Article 8

Level of Concessions and Other Obligations

1. A Member proposing to apply a safeguard measure or seeking an extension of a safeguard measure shall endeavour to maintain a substantially equivalent level of concessions and other obligations to that existing under GATT 1994 between it and the exporting Members which would be affected by such a measure, in accordance with the provisions of paragraph 3 of Article 12. To

achieve this objective, the Members concerned may agree on any adequate means of trade compensation for the adverse effects of the measure on their trade.

2. If no agreement is reached within 30 days in the consultations under paragraph 3 of Article 12, then the affected exporting Members shall be free, not later than 90 days after the measure is applied, to suspend, upon the expiration of 30 days from the day on which written notice of such suspension is received by the Council for Trade in Goods, the application of substantially equivalent concessions or other obligations under GATT 1994, to the trade of the Member applying the safeguard measure, the suspension of which the Council for Trade in Goods does not disapprove.

3. The right of suspension referred to in paragraph 2 shall not be exercised for the first three years that a safeguard measure is in effect, provided that the safeguard measure has been taken as a result of an absolute increase in imports and that such a measure conforms to the provisions of this Agreement.

Article 9

Developing Country Members

1. Safeguard measures shall not be applied against a product originating in a developing country Member as long as its share of imports of the product concerned in the importing Member does not exceed 3 per cent, provided that developing country Members with less than 3 per cent import share collectively account for not more than 9 per cent of total imports of the product concerned.²

2. A developing country Member shall have the right to extend the period of application of a safeguard measure for a period of up to two years beyond the maximum period provided for in paragraph 3 of Article 7. Notwithstanding the provisions of paragraph 5 of Article 7, a developing country Member shall have the right to apply a safeguard measure again to the import of a product which has been subject to such a measure, taken after the date of entry into force of the WTO Agreement, after a period of time equal to half that during which such a measure has been previously applied, provided that the period of non-application is at least two years.

Article 10

Pre-existing Article XIX Measures

Members shall terminate all safeguard measures taken pursuant to Article XIX of GATT 1947 that were in existence on the date of entry into force of the WTO Agreement not later than eight years after the date on which they were first applied or five years after the date of entry into force of the WTO Agreement, whichever comes later.

Article 11

Prohibition and Elimination of Certain Measures

1. (a) A Member shall not take or seek any emergency action on imports of particular products as set forth in Article XIX of GATT 1994 unless such action conforms with the provisions of that Article applied in accordance with this Agreement.

² A Member shall immediately notify an action taken under paragraph 1 of Article 9 to the Committee on Safeguards.

(b) Furthermore, a Member shall not seek, take or maintain any voluntary export restraints, orderly marketing arrangements or any other similar measures on the export or the import side.^{3, 4} These include actions taken by a single Member as well as actions under agreements, arrangements and understandings entered into by two or more Members. Any such measure in effect on the date of entry into force of the WTO Agreement shall be brought into conformity with this Agreement or phased out in accordance with paragraph 2.

(c) This Agreement does not apply to measures sought, taken or maintained by a Member pursuant to provisions of GATT 1994 other than Article XIX, and Multilateral Trade Agreements in Annex 1A other than this Agreement, or pursuant to protocols and agreements or arrangements concluded within the framework of GATT 1994.

2. The phasing out of measures referred to in paragraph 1(b) shall be carried out according to timetables to be presented to the Committee on Safeguards by the Members concerned not later than 180 days after the date of entry into force of the WTO Agreement. These timetables shall provide for all measures referred to in paragraph 1 to be phased out or brought into conformity with this Agreement within a period not exceeding four years after the date of entry into force of the WTO Agreement, subject to not more than one specific measure per importing Member⁵, the duration of which shall not extend beyond 31 December 1999. Any such exception must be mutually agreed between the Members directly concerned and notified to the Committee on Safeguards for its review and acceptance within 90 days of the entry into force of the WTO Agreement. The Annex to this Agreement indicates a measure which has been agreed as falling under this exception.

3. Members shall not encourage or support the adoption or maintenance by public and private enterprises of non-governmental measures equivalent to those referred to in paragraph 1.

Article 12

Notification and Consultation

1. A Member shall immediately notify the Committee on Safeguards upon:

- (a) initiating an investigatory process relating to serious injury or threat thereof and the reasons for it;
- (b) making a finding of serious injury or threat thereof caused by increased imports; and
- (c) taking a decision to apply or extend a safeguard measure.

2. In making the notifications referred to in paragraphs 1(b) and 1(c), the Member proposing to apply or extend a safeguard measure shall provide the Committee on Safeguards with all pertinent information, which shall include evidence of serious injury or threat thereof caused by increased

³ An import quota applied as a safeguard measure in conformity with the relevant provisions of GATT 1994 and this Agreement may, by mutual agreement, be administered by the exporting Member.

⁴ Examples of similar measures include export moderation, export-price or import-price monitoring systems, export or import surveillance, compulsory import cartels and discretionary export or import licensing schemes, any of which afford protection.

⁵ The only such exception to which the European Communities is entitled is indicated in the Annex to this Agreement.

imports, precise description of the product involved and the proposed measure, proposed date of introduction, expected duration and timetable for progressive liberalization. In the case of an extension of a measure, evidence that the industry concerned is adjusting shall also be provided. The Council for Trade in Goods or the Committee on Safeguards may request such additional information as they may consider necessary from the Member proposing to apply or extend the measure.

3. A Member proposing to apply or extend a safeguard measure shall provide adequate opportunity for prior consultations with those Members having a substantial interest as exporters of the product concerned, with a view to, *inter alia*, reviewing the information provided under paragraph 2, exchanging views on the measure and reaching an understanding on ways to achieve the objective set out in paragraph 1 of Article 8.

4. A Member shall make a notification to the Committee on Safeguards before taking a provisional safeguard measure referred to in Article 6. Consultations shall be initiated immediately after the measure is taken.

5. The results of the consultations referred to in this Article, as well as the results of mid-term reviews referred to in paragraph 4 of Article 7, any form of compensation referred to in paragraph 1 of Article 8, and proposed suspensions of concessions and other obligations referred to in paragraph 2 of Article 8, shall be notified immediately to the Council for Trade in Goods by the Members concerned.

6. Members shall notify promptly the Committee on Safeguards of their laws, regulations and administrative procedures relating to safeguard measures as well as any modifications made to them.

7. Members maintaining measures described in Article 10 and paragraph 1 of Article 11 which exist on the date of entry into force of the WTO Agreement shall notify such measures to the Committee on Safeguards not later than 60 days after the date of entry into force of the WTO Agreement.

8. Any Member may notify the Committee on Safeguards of all laws, regulations, administrative procedures and any measures or actions dealt with in this Agreement that have not been notified by other Members that are required by this Agreement to make such notifications.

9. Any Member may notify the Committee on Safeguards of any non-governmental measures referred to in paragraph 3 of Article 11.

10. All notifications to the Council for Trade in Goods referred to in this Agreement shall normally be made through the Committee on Safeguards.

11. The provisions on notification in this Agreement shall not require any Member to disclose confidential information the disclosure of which would impede law enforcement or otherwise be contrary to the public interest or would prejudice the legitimate commercial interests of particular enterprises, public or private.

1. A Committee on Safeguards is hereby established, under the authority of the Council for Trade in Goods, which shall be open to the participation of any Member indicating its wish to serve on it. The Committee will have the following functions:

Article 13

Surveillance

(a) to monitor, and report annually to the Council for Trade in Goods on, the general implementation of this Agreement and make recommendations towards its improvement;

(b) to find, upon request of an affected Member, whether or not the procedural requirements of this Agreement have been complied with in connection with a safeguard measure, and report its findings to the Council for Trade in Goods;

(c) to assist Members, if they so request, in their consultations under the provisions of this Agreement;

(d) to examine measures covered by Article 10 and paragraph 1 of Article 11, monitor the phase-out of such measures and report as appropriate to the Council for Trade in Goods;

(e) to review, at the request of the Member taking a safeguard measure, whether proposals to suspend concessions or other obligations are "substantially equivalent", and report as appropriate to the Council for Trade in Goods;

(f) to receive and review all notifications provided for in this Agreement and report as appropriate to the Council for Trade in Goods; and

(g) to perform any other function connected with this Agreement that the Council for Trade in Goods may determine.

2. To assist the Committee in carrying out its surveillance function, the Secretariat shall prepare annually a factual report on the operation of this Agreement based on notifications and other reliable information available to it.

Article 14

Dispute Settlement

The provisions of Articles XXII and XXIII of GATT 1994 as elaborated and applied by the Dispute Settlement Understanding shall apply to consultations and the settlement of disputes arising under this Agreement.

ANNEX

EXCEPTION REFERRED TO IN PARAGRAPH 2 OF ARTICLE 11

Members concerned	Product	Termination
EC/Japan	Passenger cars, off road light commercial vehicles, light trucks (up to 5 tonnes), and the same vehicles in wholly knocked-down form (CKD sets).	31 December 1999

**Understanding on Rules and Procedures Governing
the Settlement of Disputes, 1994**

UNDERSTANDING ON RULES AND PROCEDURES GOVERNING THE SETTLEMENT OF DISPUTES

("Dispute Settlement Understanding" or "DSU")

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Members hereby agree as follows:

Article 1: Coverage and Application

1. The rules and procedures of this Understanding shall apply to disputes brought pursuant to the consultation and dispute settlement provisions of the agreements listed in Appendix 1 to this Understanding (referred to in this Understanding as the "covered agreements"). The rules and procedures of this Understanding shall also apply to consultations and the settlement of disputes between Members concerning their rights and obligations under the provisions of the Agreement Establishing the World Trade Organization (referred to in this Understanding as the "WTO Agreement") and of this Understanding taken in isolation or in combination with any other covered agreement.
2. The rules and procedures of this Understanding shall apply subject to such special or additional rules and procedures on dispute settlement contained in the covered agreements as are identified in Appendix 2 to this Understanding. To the extent that there is a difference between the rules and procedures of this Understanding and the special or additional rules and procedures set forth in Appendix 2, the special or additional rules and procedures in Appendix 2 shall prevail. In disputes involving rules and procedures under more than one covered agreement, if there is a conflict between special or additional rules and procedures of such agreements under review, and where the parties to the dispute cannot agree on rules and procedures within 20 days of the establishment of the panel, the Chairman of the Dispute Settlement Body provided for in paragraph 1 of Article 2 (referred to in this Understanding as the "DSB"), in consultation with the parties to the dispute, shall determine the rules and procedures to be followed within 10 days after a request by either Member. The Chairman shall be guided by the principle that special or additional rules and procedures should be used where possible, and the rules and procedures set out in this Understanding should be used to the extent necessary to avoid conflict.

Article 2: Administration

1. The Dispute Settlement Body is hereby established to administer these rules and procedures and, except as otherwise provided in a covered agreement, the consultation and dispute settlement provisions of the covered agreements. Accordingly, the DSB shall have the authority to establish panels, adopt panel and Appellate Body reports, maintain surveillance of implementation of rulings and recommendations, and authorize suspension of concessions and other obligations under the covered agreements. With respect to disputes arising under a covered agreement which is a Plurilateral Trade Agreement, the term "Member" as used herein shall refer only to those Members that are parties to the relevant Plurilateral Trade Agreement. Where the DSB administers the dispute settlement provisions of a Plurilateral Trade Agreement, only those Members that are parties to that Agreement may participate in decisions or actions taken by the DSB with respect to that dispute.
2. The DSB shall inform the relevant WTO Councils and Committees of any developments in disputes related to provisions of the respective covered agreements.

3. The DSB shall meet as often as necessary to carry out its functions within the time-frames provided in this Understanding.
4. Where the rules and procedures of this Understanding provide for the DSB to take a decision, it shall do so by consensus.¹

Article 3: General Provisions

1. Members affirm their adherence to the principles for the management of disputes heretofore applied under Articles XXII and XXIII of GATT 1947, and the rules and procedures as further elaborated and modified herein.

2. The dispute settlement system of the WTO is a central element in providing security and predictability to the multilateral trading system. The Members recognize that it serves to preserve the rights and obligations of Members under the covered agreements, and to clarify the existing provisions of those agreements in accordance with customary rules of interpretation of public international law. Recommendations and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements.

3. The prompt settlement of situations in which a Member considers that any benefits accruing to it directly or indirectly under the covered agreements are being impaired by measures taken by another Member is essential to the effective functioning of the WTO and the maintenance of a proper balance between the rights and obligations of Members.

4. Recommendations or rulings made by the DSB shall be aimed at achieving a satisfactory settlement of the matter in accordance with the rights and obligations under this Understanding and under the covered agreements.

5. All solutions to matters formally raised under the consultation and dispute settlement provisions of the covered agreements, including arbitration awards, shall be consistent with those agreements and shall not nullify or impair benefits accruing to any Member under those agreements, nor impede the attainment of any objective of those agreements.

6. Mutually agreed solutions to matters formally raised under the consultation and dispute settlement provisions of the covered agreements shall be notified to the DSB and the relevant Councils and Committees, where any Member may raise any point relating thereto.

7. Before bringing a case, a Member shall exercise its judgement as to whether action under these procedures would be fruitful. The aim of the dispute settlement mechanism is to secure a positive solution to a dispute. A solution mutually acceptable to the parties to a dispute and consistent with the covered agreements is clearly to be preferred. In the absence of a mutually agreed solution, the first objective of the dispute settlement mechanism is usually to secure the withdrawal of the measures concerned if these are found to be inconsistent with the provisions of any of the covered agreements. The provision of compensation should be resorted to only if the immediate withdrawal of the measure is impracticable and as a temporary measure pending the withdrawal of the measure which is inconsistent with a covered agreement. The last resort which this Understanding provides to the Member invoking the

dispute settlement procedures is the possibility of suspending the application of concessions or other obligations under the covered agreements on a discriminatory basis vis-à-vis the other Member, subject to authorization by the DSB of such measures.

8. In cases where there is an infringement of the obligations assumed under a covered agreement, the action is considered *prima facie* to constitute a case of nullification or impairment. This means that there is normally a presumption that a breach of the rules has an adverse impact on other Members parties to that covered agreement, and in such cases, it shall be up to the Member against whom the complaint has been brought to rebut the charge.

9. The provisions of this Understanding are without prejudice to the rights of Members to seek authoritative interpretation of provisions of a covered agreement through decision-making under the WTO Agreement or a covered agreement which is a Plurilateral Trade Agreement.

10. It is understood that requests for conciliation and the use of the dispute settlement procedures should not be intended or considered as contentious acts and that, if a dispute arises, all Members will engage in these procedures in good faith in an effort to resolve the dispute. It is also understood that complaints and counter-complaints in regard to distinct matters should not be linked.

11. This Understanding shall be applied only with respect to new requests for consultations under the consultation provisions of the covered agreements made on or after the date of entry into force of the WTO Agreement. With respect to disputes for which the request for consultations was made under GATT 1947 or under any other predecessor agreement to the covered agreements before the date of entry into force of the WTO Agreement, the relevant dispute settlement rules and procedures in effect immediately prior to the date of entry into force of the WTO Agreement shall continue to apply.²

12. Notwithstanding paragraph 11, if a complaint based on any of the covered agreements is brought by a developing country Member against a developed country Member, the complaining party shall have the right to invoke, as an alternative to the provisions contained in Articles 4, 5, 6 and 12 of this Understanding, the corresponding provisions of the Decision of 5 April 1966 (BISD 14S/18), except that where the Panel considers that the time-frame provided for in paragraph 7 of that Decision is insufficient to provide its report and with the agreement of the complaining party, that time-frame may be extended. To the extent that there is a difference between the rules and procedures of Articles 4, 5, 6 and 12 and the corresponding rules and procedures of the Decision, the latter shall prevail.

Article 4: Consultations

1. Members affirm their resolve to strengthen and improve the effectiveness of the consultation procedures employed by Members.
2. Each Member undertakes to accord sympathetic consideration to and afford adequate opportunity for consultation regarding any representations made by another Member

¹The DSB shall be deemed to have decided by consensus on a matter submitted for its consideration, if no Member, present at the meeting of the DSB when the decision is taken, formally objects to the proposed decision.

²This paragraph shall also be applied to disputes on which panel reports have not been adopted or fully implemented.

concerning measures affecting the operation of any covered agreement taken within the territory of the former.³

3. If a request for consultations is made pursuant to a covered agreement, the Member to which the request is made shall, unless otherwise mutually agreed, reply to the request within 10 days after the date of its receipt and shall enter into consultations in good faith within a period of no more than 30 days after the date of receipt of the request, with a view to reaching a mutually satisfactory solution. If the Member does not respond within 10 days after the date of receipt of the request, or does not enter into consultations within a period of no more than 30 days, or a period otherwise mutually agreed, after the date of receipt of the request, then the Member that requested the holding of consultations may proceed directly to request the establishment of a panel.
4. All such requests for consultations shall be notified to the DSB and the relevant Councils and Committees by the Member which requests consultations. Any request for consultations shall be submitted in writing and shall give the reasons for the request, including identification of the measures at issue and an indication of the legal basis for the complaint.
5. In the course of consultations in accordance with the provisions of a covered agreement, before resorting to further action under this Understanding, Members should attempt to obtain satisfactory adjustment of the matter.
6. Consultations shall be confidential, and without prejudice to the rights of any Member in any further proceedings.

7. If the consultations fail to settle a dispute within 60 days after the date of receipt of the request for consultations, the complaining party may request the establishment of a panel. The complaining party may request a panel during the 60-day period if the consulting parties jointly consider that consultations have failed to settle the dispute.

8. In cases of urgency, including those which concern perishable goods, Members shall enter into consultations within a period of no more than 10 days after the date of receipt of the request. If the consultations have failed to settle the dispute within a period of 20 days after the date of receipt of the request, the complaining party may request the establishment of a panel.

9. In cases of urgency, including those which concern perishable goods, the parties to the dispute, panels and the Appellate Body shall make every effort to accelerate the proceedings to the greatest extent possible.

10. During consultations Members should give special attention to the particular problems and interests of developing country Members.

11. Whenever a Member other than the consulting Members considers that it has a substantial trade interest in consultations being held pursuant to paragraph 1 of Article XXII of GATT 1994, paragraph 1 of Article XXII of GATS, or the corresponding provisions in other covered agreements⁴, such Member may notify the consulting Members and the DSB, within

³Where the provisions of any other covered agreement concerning measures taken by regional or local governments or authorities within the territory of a Member contain provisions different from the provisions of this paragraph, the provisions of such other covered agreement shall prevail.

⁴The corresponding consultation provisions in the covered agreements are listed hereunder: Agreement on Agriculture, Article 19; Agreement on the Application of Sanitary and Phytosanitary Measures, paragraph 1 of Article 11; Agreement on Textiles and Clothing, paragraph 4 of Article 8; Agreement on Technical Barriers to Trade, paragraph 1 of Article 14; Agreement on Trade-Related Investment

10 days after the date of the circulation of the request for consultations under said Article, of its desire to be joined in the consultations. Such Member shall be joined in the consultations, provided that the Member to which the request for consultations was addressed agrees that the claim of substantial interest is well-founded. In that event they shall so inform the DSB. If the request to be joined in the consultations is not accepted, the applicant Member shall be free to request consultations under paragraph 1 of Article XXII or paragraph 1 of Article XXIII of GATT 1994, paragraph 1 of Article XXII or paragraph 1 of Article XXIII of GATS, or the corresponding provisions in other covered agreements.

Article 5: Good Offices, Conciliation and Mediation

1. Good offices, conciliation and mediation are procedures that are undertaken voluntarily if the parties to the dispute so agree.
2. Proceedings involving good offices, conciliation and mediation, and in particular positions taken by the parties to the dispute during these proceedings, shall be confidential, and without prejudice to the rights of either party in any further proceedings under these procedures.
3. Good offices, conciliation or mediation may be requested at any time by any party to a dispute. They may begin at any time and be terminated at any time. Once procedures for good offices, conciliation or mediation are terminated, a complaining party may then proceed with a request for the establishment of a panel.
4. When good offices, conciliation or mediation are entered into within 60 days after the date of receipt of a request for consultations, the complaining party must allow a period of 60 days after the date of receipt of the request for consultations before requesting the establishment of a panel. The complaining party may request the establishment of a panel during the 60-day period if the parties to the dispute jointly consider that the good offices, conciliation or mediation process has failed to settle the dispute.
5. If the parties to a dispute agree, procedures for good offices, conciliation or mediation may continue while the panel process proceeds.
6. The Director-General may, acting in an *ex officio* capacity, offer good offices, conciliation or mediation with the view to assisting Members to settle a dispute.

Article 6: Establishment of Panels

1. If the complaining party so requests, a panel shall be established at the latest at the DSB meeting following that at which the request first appears as an item on the DSB's agenda, unless at that meeting the DSB decides by consensus not to establish a panel.⁵

Measures, Article 8; Agreement on Implementation of Article VI of GATT 1994, paragraph 2 of Article 17; Agreement on Implementation of Article VII of GATT 1994, paragraph 2 of Article 19; Agreement on Preshipment Inspection, Article 7; Agreement on Rules of Origin, Article 7; Agreement on Import Licensing Procedures, Article 6; Agreement on Subsidies and Countervailing Measures, Article 30; Agreement on Safeguards, Article 14; Agreement on Trade-Related Aspects of Intellectual Property Rights, Article 64.1; and any corresponding consultation provisions in Plurilateral Trade Agreements as determined by the competent bodies of each Agreement and as notified to the DSB.

⁵If the complaining party so requests, a meeting of the DSB shall be convened for this purpose within 15 days of the request, provided that at least 10 days' advance notice of the meeting is given.

2. The request for the establishment of a panel shall be made in writing. It shall indicate whether consultations were held, identify the specific measures at issue and provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly. In case the applicant requests the establishment of a panel with other than standard terms of reference, the written request shall include the proposed text of special terms of reference.

Article 7: Terms of Reference of Panels

1. Panels shall have the following terms of reference unless the parties to the dispute agree otherwise within 20 days from the establishment of the panel:

"To examine, in the light of the relevant provisions in (name of the covered agreement(s) cited by the parties to the dispute), the matter referred to the DSB by (name of party) in document ... and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in that/those agreement(s)."

2. Panels shall address the relevant provisions in any covered agreement or agreements cited by the parties to the dispute.

3. In establishing a panel, the DSB may authorize its Chairman to draw up the terms of reference of the panel in consultation with the parties to the dispute, subject to the provisions of paragraph 1. The terms of reference thus drawn up shall be circulated to all Members. If other than standard terms of reference are agreed upon, any Member may raise any point relating thereto in the DSB.

4. To assist in the selection of panelists, the Secretariat shall maintain an indicative list of governmental and non-governmental individuals possessing the qualifications outlined in paragraph 1, from which panelists may be drawn as appropriate. That list shall include the roster of non-governmental panelists established on 30 November 1984 (BISD 31S/9), and other rosters and indicative lists established under any of the covered agreements, and shall retain the names of persons on those rosters and indicative lists at the time of entry into force of the WTO Agreement. Members may periodically suggest names of governmental and non-governmental individuals for inclusion on the indicative list, providing relevant information on their knowledge of international trade and of the sectors or subject matter of the covered agreements, and those names shall be added to the list upon approval by the DSB. For each of the individuals on the list, the list shall indicate specific areas of experience or expertise of the individuals in the sectors or subject matter of the covered agreements.

5. Panels shall be composed of three panelists unless the parties to the dispute agree, within 10 days from the establishment of the panel, to a panel composed of five panelists. Members shall be informed promptly of the composition of the panel.

6. The Secretariat shall propose nominations for the panel to the parties to the dispute. The parties to the dispute shall not oppose nominations except for compelling reasons.

7. If there is no agreement on the panelists within 20 days after the date of the establishment of a panel, at the request of either party, the Director-General, in consultation with the Chairman of the DSB and the Chairman of the relevant Council or Committee, shall determine the composition of the panel by appointing the panelists whom the Director-General considers most appropriate in accordance with any relevant special or additional rules or procedures of the covered agreement or covered agreements which are at issue in the dispute, after consulting with the parties to the dispute. The Chairman of the DSB shall inform the Members of the composition of the panel thus formed no later than 10 days after the date the Chairman receives such a request.

8. Members shall undertake, as a general rule, to permit their officials to serve as panelists.

9. Panelists shall serve in their individual capacities and not as government representatives, nor as representatives of any organization. Members shall therefore not give them instructions nor seek to influence them as individuals with regard to matters before a panel.

10. When a dispute is between a developing country Member and a developed country Member the panel shall, if the developing country Member so requests, include at least one panelist from a developing country Member.

11. Panelists' expenses, including travel and subsistence allowance, shall be met from the WTO budget in accordance with criteria to be adopted by the General Council, based on recommendations of the Committee on Budget, Finance and Administration.

Article 8: Composition of Panels

1. Panels shall be composed of well-qualified governmental and/or non-governmental individuals, including persons who have served on or presented a case to a panel, served as a representative of a Member or of a contracting party to GATT 1947 or as a representative to the Council or Committee of any covered agreement or its predecessor agreement, or in the Secretariat, taught or published on international trade law or policy, or served as a senior trade policy official of a Member.

2. Panel members should be selected with a view to ensuring the independence of the members, a sufficiently diverse background and a wide spectrum of experience.

3. Citizens of Members whose governments⁶ are parties to the dispute or third parties as defined in paragraph 2 of Article 10 shall not serve on a panel concerned with that dispute, unless the parties to the dispute agree otherwise.

⁶In the case where customs unions or common markets are parties to a dispute, this provision applies to citizens of all member countries of the customs unions or common markets.

Article 9: Procedures for Multiple Complainants

1. Where more than one Member requests the establishment of a panel related to the same matter, a single panel may be established to examine these complaints taking into account the rights of all Members concerned. A single panel should be established to examine such complaints whenever feasible.
2. The single panel shall organize its examination and present its findings to the DSB in such a manner that the rights which the parties to the dispute would have enjoyed had separate panels examined the complaints are in no way impaired. If one of the parties to the dispute so requests, the panel shall submit separate reports on the dispute concerned. The written submissions by each of the complainants shall be made available to the other complainants, and each complainant shall have the right to be present when any one of the other complainants presents its views to the panel.
3. If more than one panel is established to examine the complaints related to the same matter, to the greatest extent possible the same persons shall serve as panelists on each of the separate panels and the timetable for the panel process in such disputes shall be harmonized.

Article 10: Third Parties

1. The interests of the parties to a dispute and those of other Members under a covered agreement at issue in the dispute shall be fully taken into account during the panel process.
2. Any Member having a substantial interest in a matter before a panel and having notified its interest to the DSB (referred to in this Understanding as a "third party") shall have an opportunity to be heard by the panel and to make written submissions to the panel. These submissions shall also be given to the parties to the dispute and shall be reflected in the panel report.
3. Third parties shall receive the submissions of the parties to the dispute to the first meeting of the panel.

4. If a third party considers that a measure already the subject of a panel proceeding nullifies or impairs benefits accruing to it under any covered agreement, that Member may have recourse to normal dispute settlement procedures under this Understanding. Such a dispute shall be referred to the original panel wherever possible.

Article 11: Function of Panels

The function of panels is to assist the DSB in discharging its responsibilities under this Understanding and the covered agreements. Accordingly, a panel should make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements, and make such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the covered agreements. Panels should consult regularly with the parties to the dispute and give them adequate opportunity to develop a mutually satisfactory solution.

Article 12: Panel Procedures

1. Panels shall follow the Working Procedures in Appendix 3 unless the panel decides otherwise after consulting the parties to the dispute.
2. Panel procedures should provide sufficient flexibility so as to ensure high-quality panel reports, while not unduly delaying the panel process.
3. After consulting the parties to the dispute, the panelists shall, as soon as practicable and whenever possible within one week after the composition and terms of reference of the panel have been agreed upon, fix the timetable for the panel process, taking into account the provisions of paragraph 9 of Article 4, if relevant.
4. In determining the timetable for the panel process, the panel shall provide sufficient time for the parties to the dispute to prepare their submissions.
5. Panels should set precise deadlines for written submissions by the parties and the parties should respect those deadlines.
6. Each party to the dispute shall deposit its written submissions with the Secretariat for immediate transmission to the panel and to the other party or parties to the dispute. The complaining party shall submit its first submission in advance of the responding party's first submission unless the panel decides, in fixing the timetable referred to in paragraph 3 and after consultations with the parties to the dispute, that the parties should submit their first submissions simultaneously. When there are sequential arrangements for the deposit of first submissions, the panel shall establish a firm time-period for receipt of the responding party's submission. Any subsequent written submissions shall be submitted simultaneously.
7. Where the parties to the dispute have failed to develop a mutually satisfactory solution, the panel shall submit its findings in the form of a written report to the DSB. In such cases, the report of a panel shall set out the findings of fact, the applicability of relevant provisions and the basic rationale behind any findings and recommendations that it makes. Where a settlement of the matter among the parties to the dispute has been found, the report of the panel shall be confined to a brief description of the case and to reporting that a solution has been reached.
8. In order to make the procedures more efficient, the period in which the panel shall conduct its examination, from the date that the composition and terms of reference of the panel have been agreed upon until the date the final report is issued to the parties to the dispute, shall, as a general rule, not exceed six months. In cases of urgency, including those relating to perishable goods, the panel shall aim to issue its report to the parties to the dispute within three months.
9. When the panel considers that it cannot issue its report within six months, or within three months in cases of urgency, it shall inform the DSB in writing of the reasons for the delay together with an estimate of the period within which it will issue its report. In no case should the period from the establishment of the panel to the circulation of the report to the Members exceed nine months.
10. In the context of consultations involving a measure taken by a developing country Member, the parties may agree to extend the periods established in paragraphs 7 and 8 of

Article 4. If, after the relevant period has elapsed, the consulting parties cannot agree that the consultations have concluded, the Chairman of the DSB shall decide, after consultation with the parties, whether to extend the relevant period and, if so, for how long. In addition, in examining a complaint against a developing country Member, the panel shall accord sufficient time for the developing country Member to prepare and present its argumentation. The provisions of paragraph 1 of Article 20 and paragraph 4 of Article 21 are not affected by any action pursuant to this paragraph.

11. Where one or more of the parties is a developing country Member, the panel's report shall explicitly indicate the form in which account has been taken of relevant provisions on differential and more-favourable treatment for developing country Members that form part of the covered agreements which have been raised by the developing country Member in the course of the dispute settlement procedures.

12. The panel may suspend its work at any time at the request of the complaining party for a period not to exceed 12 months. In the event of such a suspension, the time-frames set out in paragraphs 8 and 9 of this Article, paragraph 1 of Article 20, and paragraph 4 of Article 21 shall be extended by the amount of time that the work was suspended. If the work of the panel has been suspended for more than 12 months, the authority for establishment of the panel shall lapse.

Article 13: Right to Seek Information

1. Each panel shall have the right to seek information and technical advice from any individual or body which it deems appropriate. However, before a panel seeks such information or advice from any individual or body within the jurisdiction of a Member it shall inform the authorities of that Member. A Member should respond promptly and fully to any request by a panel for such information as the panel considers necessary and appropriate. Confidential information which is provided shall not be revealed without formal authorization from the individual, body, or authorities of the Member providing the information.

2. Panels may seek information from any relevant source and may consult experts to obtain their opinion on certain aspects of the matter. With respect to a factual issue concerning a scientific or other technical matter raised by a party to a dispute, a panel may request an advisory report in writing from an expert review group. Rules for the establishment of such a group and its procedures are set forth in Appendix 4.

Article 14: Confidentiality

1. Panel deliberations shall be confidential.
2. The reports of panels shall be drafted without the presence of the parties to the dispute in the light of the information provided and the statements made.
3. Opinions expressed in the panel report by individual panelists shall be anonymous.

Article 15: Interim Review Stage

1. Following the consideration of rebuttal submissions and oral arguments, the panel shall issue the descriptive (factual and argument) sections of its draft report to the parties to the dispute. Within a period of time set by the panel, the parties shall submit their comments in writing.

2. Following the expiration of the set period of time for receipt of comments from the parties to the dispute, the panel shall issue an interim report to the parties, including both the descriptive sections and the panel's findings and conclusions. Within a period of time set by the panel, a party may submit a written request for the panel to review precise aspects of the interim report prior to circulation of the final report to the Members. At the request of a party, the panel shall hold a further meeting with the parties on the issues identified in the written comments. If no comments are received from any party within the comment period, the interim report shall be considered the final panel report and circulated promptly to the Members.

3. The findings of the final panel report shall include a discussion of the arguments made at the interim review stage. The interim review stage shall be conducted within the time-period set out in paragraph 8 of Article 12.

Article 16: Adoption of Panel Reports

1. In order to provide sufficient time for the Members to consider panel reports, the reports shall not be considered for adoption by the DSB until 20 days after the date they have been circulated to the Members.

2. Members having objections to a panel report shall give written reasons to explain their objections for circulation at least 10 days prior to the DSB meeting at which the panel report will be considered.

3. The parties to a dispute shall have the right to participate fully in the consideration of the panel report by the DSB, and their views shall be fully recorded.

4. Within 60 days after the date of circulation of a panel report to the Members, the report shall be adopted at a DSB meeting⁷ unless a party to the dispute formally notifies the DSB of its decision to appeal or the DSB decides by consensus not to adopt the report. If a party has notified its decision to appeal, the report by the panel shall not be considered for adoption by the DSB until after completion of the appeal. This adoption procedure is without prejudice to the right of Members to express their views on a panel report.

⁷If a meeting of the DSB is not scheduled within this period at a time that enables the requirements of paragraphs 1 and 4 of Article 16 to be met, a meeting of the DSB shall be held for this purpose.

Article 17: Appellate Review

Standing Appellate Body

1. A standing Appellate Body shall be established by the DSB. The Appellate Body shall hear appeals from panel cases. It shall be composed of seven persons, three of whom shall serve on any one case. Persons serving on the Appellate Body shall serve in rotation. Such rotation shall be determined in the working procedures of the Appellate Body.
2. The DSB shall appoint persons to serve on the Appellate Body for a four-year term, and each person may be reappointed once. However, the terms of three of the seven persons appointed immediately after the entry into force of the WTO Agreement shall expire at the end of two years, to be determined by lot. Vacancies shall be filled as they arise. A person appointed to replace a person whose term of office has not expired shall hold office for the remainder of the predecessor's term.
3. The Appellate Body shall comprise persons of recognized authority, with demonstrated expertise in law, international trade and the subject matter of the covered agreements generally. They shall be unaffiliated with any government. The Appellate Body membership shall be broadly representative of membership in the WTO. All persons serving on the Appellate Body shall be available at all times and on short notice, and shall stay abreast of dispute settlement activities and other relevant activities of the WTO. They shall not participate in the consideration of any disputes that would create a direct or indirect conflict of interest.
4. Only parties to the dispute, not third parties, may appeal a panel report. Third parties which have notified the DSB of a substantial interest in the matter pursuant to paragraph 2 of Article 10 may make written submissions to, and be given an opportunity to be heard by, the Appellate Body.
5. As a general rule, the proceedings shall not exceed 60 days from the date a party to the dispute formally notifies its decision to appeal to the date the Appellate Body circulates its report. In fixing its timetable the Appellate Body shall take into account the provisions of paragraph 9 of Article 4, if relevant. When the Appellate Body considers that it cannot provide its report within 60 days, it shall inform the DSB in writing of the reasons for the delay together with an estimate of the period within which it will submit its report. In no case shall the proceedings exceed 90 days.

6. An appeal shall be limited to issues of law covered in the panel report and legal interpretations developed by the panel.

7. The Appellate Body shall be provided with appropriate administrative and legal support as it requires.

8. The expenses of persons serving on the Appellate Body, including travel and subsistence allowance, shall be met from the WTO budget in accordance with criteria to be adopted by the General Council, based on recommendations of the Committee on Budget, Finance and Administration.

Procedures for Appellate Review

9. Working procedures shall be drawn up by the Appellate Body in consultation with the Chairman of the DSB and the Director-General, and communicated to the Members for their information.
10. The proceedings of the Appellate Body shall be confidential. The reports of the Appellate Body shall be drafted without the presence of the parties to the dispute and in the light of the information provided and the statements made.
11. Opinions expressed in the Appellate Body report by individuals serving on the Appellate Body shall be anonymous.
12. The Appellate Body shall address each of the issues raised in accordance with paragraph 6 during the appellate proceeding.
13. The Appellate Body may uphold, modify or reverse the legal findings and conclusions of the panel.

Adoption of Appellate Body Reports

14. An Appellate Body report shall be adopted by the DSB and unconditionally accepted by the parties to the dispute unless the DSB decides by consensus not to adopt the Appellate Body report within 30 days following its circulation to the Members.⁸ This adoption procedure is without prejudice to the right of Members to express their views on an Appellate Body report.

Article 18: Communications with the Panel or Appellate Body

1. There shall be no *ex parte* communications with the panel or Appellate Body concerning matters under consideration by the panel or Appellate Body.
2. Written submissions to the panel or the Appellate Body shall be treated as confidential, but shall be made available to the parties to the dispute. Nothing in this Understanding shall preclude a party to a dispute from disclosing statements of its own positions to the public. Members shall treat as confidential information submitted by another Member to the panel or the Appellate Body which that Member has designated as confidential. A party to a dispute shall also, upon request of a Member, provide a non-confidential summary of the information contained in its written submissions that could be disclosed to the public.

Article 19: Panel and Appellate Body Recommendations

1. Where a panel or the Appellate Body concludes that a measure is inconsistent with a covered agreement, it shall recommend that the Member concerned⁹ bring the measure into conformity with that agreement.¹⁰ In addition to its recommendations, the panel or Appellate Body may suggest ways in which the Member concerned could implement the recommendations.

⁸If a meeting of the DSB is not scheduled during this period, such a meeting of the DSB shall be held for this purpose.

⁹The "Member concerned" is the party to the dispute to which the panel or Appellate Body recommendations are directed.

¹⁰With respect to recommendations in cases not involving a violation of GATT 1994 or any other covered agreement, see Article 26.

2. In accordance with paragraph 2 of Article 3, in their findings and recommendations, the panel and Appellate Body cannot add to or diminish the rights and obligations provided in the covered agreements.

Article 20: Time-frame for DSB Decisions

Unless otherwise agreed to by the parties to the dispute, the period from the date of establishment of the panel by the DSB until the date the DSB considers the panel or appellate report for adoption shall as a general rule not exceed nine months where the panel report is not appealed or 12 months where the report is appealed. Where either the panel or the Appellate Body has acted, pursuant to paragraph 9 of Article 12 or paragraph 5 of Article 17, to extend the time for providing its report, the additional time taken shall be added to the above periods.

Article 21: Surveillance of Implementation of Recommendations and Rulings

1. Prompt compliance with recommendations or rulings of the DSB is essential in order to ensure effective resolution of disputes to the benefit of all Members.
2. Particular attention should be paid to matters affecting the interests of developing country Members with respect to measures which have been subject to dispute settlement.
3. At a DSB meeting held within 30 days¹¹ after the date of adoption of the panel or Appellate Body report, the Member concerned shall inform the DSB of its intentions in respect of implementation of the recommendations and rulings of the DSB. If it is impracticable to comply immediately with the recommendations and rulings, the Member concerned shall have a reasonable period of time in which to do so. The reasonable period of time shall be:

- (a) the period of time proposed by the Member concerned, provided that such period is approved by the DSB; or, in the absence of such approval,
- (b) a period of time mutually agreed by the parties to the dispute within 45 days after the date of adoption of the recommendations and rulings; or, in the absence of such agreement,
- (c) a period of time determined through binding arbitration within 90 days after the date of adoption of the recommendations and rulings.¹² In such arbitration, a guideline for the arbitrator¹³ should be that the reasonable period of time to implement panel or Appellate Body recommendations should not exceed 15 months from the date of adoption of a panel or Appellate Body report. However, that time may be shorter or longer, depending upon the particular circumstances.

¹¹If a meeting of the DSB is not scheduled during this period, such a meeting of the DSB shall be held for this purpose.

¹²If the parties cannot agree on an arbitrator within ten days after referring the matter to arbitration, the arbitrator shall be appointed by the Director-General within ten days, after consulting the parties.

¹³The expression "arbitrator" shall be interpreted as referring either to an individual or a group.

4. Except where the panel or the Appellate Body has extended, pursuant to paragraph 9 of Article 12 or paragraph 5 of Article 17, the time of providing its report, the period from the date of establishment of the panel by the DSB until the date of determination of the reasonable period of time shall not exceed 15 months unless the parties to the dispute agree otherwise. Where either the panel or the Appellate Body has acted to extend the time of providing its report, the additional time taken shall be added to the 15-month period; provided that unless the parties to the dispute agree that there are exceptional circumstances, the total time shall not exceed 18 months.

5. Where there is disagreement as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations and rulings such dispute shall be decided through recourse to these dispute settlement procedures, including wherever possible resort to the original panel. The panel shall circulate its report within 90 days after the date of referral of the matter to it. When the panel considers that it cannot provide its report within this time frame, it shall inform the DSB in writing of the reasons for the delay together with an estimate of the period within which it will submit its report.

6. The DSB shall keep under surveillance the implementation of adopted recommendations or rulings. The issue of implementation of the recommendations or rulings may be raised at the DSB by any Member at any time following their adoption. Unless the DSB decides otherwise, the issue of implementation of the recommendations or rulings shall be placed on the agenda of the DSB meeting after six months following the date of establishment of the reasonable period of time pursuant to paragraph 3 and shall remain on the DSB's agenda until the issue is resolved. At least 10 days prior to each such DSB meeting, the Member concerned shall provide the DSB with a status report in writing of its progress in the implementation of the recommendations or rulings.

7. If the matter is one which has been raised by a developing country Member, the DSB shall consider what further action it might take which would be appropriate to the circumstances.

8. If the case is one brought by a developing country Member, in considering what appropriate action might be taken, the DSB shall take into account not only the trade coverage of measures complained of, but also their impact on the economy of developing country Members concerned.

Article 22: Compensation and the Suspension of Concessions

1. Compensation and the suspension of concessions or other obligations are temporary measures available in the event that the recommendations and rulings are not implemented within a reasonable period of time. However, neither compensation nor the suspension of concessions or other obligations is preferred to full implementation of a recommendation to bring a measure into conformity with the covered agreements. Compensation is voluntary and, if granted, shall be consistent with the covered agreements.

2. If the Member concerned fails to bring the measure found to be inconsistent with a covered agreement into compliance therewith or otherwise comply with the recommendations and rulings within the reasonable period of time determined pursuant to paragraph 3 of Article 21, such Member shall, if so requested, and no later than the expiry of the reasonable period of time, enter into negotiations with any party having invoked the dispute settlement procedures,

with a view to developing mutually acceptable compensation. If no satisfactory compensation has been agreed within 20 days after the date of expiry of the reasonable period of time, any party having invoked the dispute settlement procedures may request authorization from the DSB to suspend the application to the Member concerned of concessions or other obligations under the covered agreements.

3. In considering what concessions or other obligations to suspend, the complaining party shall apply the following principles and procedures:

- (a) the general principle is that the complaining party should first seek to suspend concessions or other obligations with respect to the same sector(s) as that in which the panel or Appellate Body has found a violation or other nullification or impairment;
- (b) if that party considers that it is not practicable or effective to suspend concessions or other obligations with respect to the same sector(s), it may seek to suspend concessions or other obligations in other sectors under the same agreement;
- (c) if that party considers that it is not practicable or effective to suspend concessions or other obligations with respect to other sectors under the same agreement, and that the circumstances are serious enough, it may seek to suspend concessions or other obligations under another covered agreement;
- (d) in applying the above principles, that party shall take into account:
 - (i) the trade in the sector or under the agreement under which the panel or Appellate Body has found a violation or other nullification or impairment, and the importance of such trade to that party;
 - (ii) the broader economic elements related to the nullification or impairment and the broader economic consequences of the suspension of concessions or other obligations;
- (e) if that party decides to request authorization to suspend concessions or other obligations pursuant to subparagraphs (b) or (c), it shall state the reasons therefor in its request. At the same time as the request is forwarded to the DSB, it also shall be forwarded to the relevant Councils and also, in the case of a request pursuant to subparagraph (b), the relevant sectoral bodies;
- (f) for purposes of this paragraph, "sector" means:
 - (i) with respect to goods, all goods;
 - (ii) with respect to services, a principal sector as identified in the current "Services Sectoral Classification List" which identifies such sectors;¹⁴
 - (iii) with respect to trade-related intellectual property rights, each of the categories of intellectual property rights covered in Section 1, or

¹⁴The list in document MTN.GNS/W/120 identifies eleven sectors.

Section 2, or Section 3, or Section 4, or Section 5, or Section 6, or Section 7 of Part II, or the obligations under Part III, or Part IV of the Agreement on TRIPS;

(g) for purposes of this paragraph, "agreement" means:

- (i) with respect to goods, the agreements listed in Annex 1A of the WTO Agreement, taken as a whole as well as the Plurilateral Trade Agreements in so far as the relevant parties to the dispute are parties to these agreements;
- (ii) with respect to services, the GATS;
- (iii) with respect to intellectual property rights, the Agreement on TRIPS.

4. The level of the suspension of concessions or other obligations authorized by the DSB shall be equivalent to the level of the nullification or impairment.

5. The DSB shall not authorize suspension of concessions or other obligations if a covered agreement prohibits such suspension.

6. When the situation described in paragraph 2 occurs, the DSB, upon request, shall grant authorization to suspend concessions or other obligations within 30 days of the expiry of the reasonable period of time unless the DSB decides by consensus to reject the request. However, if the Member concerned objects to the level of suspension proposed, or claims that the principles and procedures set forth in paragraph 3 have not been followed where a complaining party has requested authorization to suspend concessions or other obligations pursuant to paragraph 3(b) or (c), the matter shall be referred to arbitration. Such arbitration shall be carried out by the original panel, if members are available, or by an arbitrator¹⁵ appointed by the Director-General and shall be completed within 60 days after the date of expiry of the reasonable period of time. Concessions or other obligations shall not be suspended during the course of the arbitration.

7. The arbitrator¹⁶ acting pursuant to paragraph 6 shall not examine the nature of the concessions or other obligations to be suspended but shall determine whether the level of such suspension is equivalent to the level of nullification or impairment. The arbitrator may also determine if the proposed suspension of concessions or other obligations is allowed under the covered agreement. However, if the matter referred to arbitration includes a claim that the principles and procedures set forth in paragraph 3 have not been followed, the arbitrator shall examine that claim. In the event the arbitrator determines that those principles and procedures have not been followed, the complaining party shall apply them consistent with paragraph 3. The parties shall accept the arbitrator's decision as final and the parties concerned shall not seek a second arbitration. The DSB shall be informed promptly of the decision of the arbitrator and shall upon request, grant authorization to suspend concessions or other obligations where the request is consistent with the decision of the arbitrator, unless the DSB decides by consensus to reject the request.

¹⁵The expression "arbitrator" shall be interpreted as referring either to an individual or a group.

¹⁶The expression "arbitrator" shall be interpreted as referring either to an individual or a group or to the members of the original panel when serving in the capacity of arbitrator.

8. The suspension of concessions or other obligations shall be temporary and shall only be applied until such time as the measure found to be inconsistent with a covered agreement has been removed, or the Member that must implement recommendations or rulings provides a solution to the nullification or impairment of benefits, or a mutually satisfactory solution is reached. In accordance with paragraph 6 of Article 21, the DSB shall continue to keep under surveillance the implementation of adopted recommendations or rulings, including those cases where compensation has been provided or concessions or other obligations have been suspended but the recommendations to bring a measure into conformity with the covered agreements have not been implemented.

9. The dispute settlement provisions of the covered agreements may be invoked in respect of measures affecting their observance taken by regional or local governments or authorities within the territory of a Member. When the DSB has ruled that a provision of a covered agreement has not been observed, the responsible Member shall take such reasonable measures as may be available to it to ensure its observance. The provisions of the covered agreements and this Understanding relating to compensation and suspension of concessions or other obligations apply in cases where it has not been possible to secure such observance.¹⁷

Article 23: Strengthening of the Multilateral System

1. When Members seek the redress of a violation of obligations or other nullification or impairment of benefits under the covered agreements or an impediment to the attainment of any objective of the covered agreements, they shall have recourse to, and abide by, the rules and procedures of this Understanding.

2. In such cases, Members shall:

- (a) not make a determination to the effect that a violation has occurred, that benefits have been nullified or impaired or that the attainment of any objective of the covered agreements has been impeded, except through recourse to dispute settlement in accordance with the rules and procedures of this Understanding, and shall make any such determination consistent with the findings contained in the panel or Appellate Body report adopted by the DSB or an arbitration award rendered under this Understanding;
- (b) follow the procedures set forth in Article 21 to determine the reasonable period of time for the Member concerned to implement the recommendations and rulings; and
- (c) follow the procedures set forth in Article 22 to determine the level of suspension of concessions or other obligations and obtain DSB authorization in accordance with those procedures before suspending concessions or other obligations under the covered agreements in response to the failure of the Member concerned to implement the recommendations and rulings within that reasonable period of time.

¹⁷Where the provisions of any covered agreement concerning measures taken by regional or local governments or authorities within the territory of a Member contain provisions different from the provisions of this paragraph, the provisions of such covered agreement shall prevail.

Article 24: Special Procedures Involving Least-Developed Country Members

1. At all stages of the determination of the causes of a dispute and of dispute settlement procedures involving a least-developed country Member, particular consideration shall be given to the special situation of least-developed country Members. In this regard, Members shall exercise due restraint in raising matters under these procedures involving a least-developed country Member. If nullification or impairment is found to result from a measure taken by a least-developed country Member, complaining parties shall exercise due restraint in asking for compensation or seeking authorization to suspend the application of concessions or other obligations pursuant to these procedures.

2. In dispute settlement cases involving a least-developed country Member, where a satisfactory solution has not been found in the course of consultations the Director-General or the Chairman of the DSB shall, upon request by a least-developed country Member offer their good offices, conciliation and mediation with a view to assisting the parties to settle the dispute, before a request for a panel is made. The Director-General or the Chairman of the DSB, in providing the above assistance, may consult any source which either deems appropriate.

Article 25: Arbitration

1. Expeditious arbitration within the WTO as an alternative means of dispute settlement can facilitate the solution of certain disputes that concern issues that are clearly defined by both parties.

2. Except as otherwise provided in this Understanding, resort to arbitration shall be subject to mutual agreement of the parties which shall agree on the procedures to be followed. Agreements to resort to arbitration shall be notified to all Members sufficiently in advance of the actual commencement of the arbitration process.

3. Other Members may become party to an arbitration proceeding only upon the agreement of the parties which have agreed to have recourse to arbitration. The parties to the proceeding shall agree to abide by the arbitration award. Arbitration awards shall be notified to the DSB and the Council or Committee of any relevant agreement where any Member may raise any point relating thereto.

4. Articles 21 and 22 of this Understanding shall apply *mutatis mutandis* to arbitration awards.

Article 26

1. Non-Violation Complaints of the Type Described in Paragraph 1(b) of Article XXIII of GATT 1994

Where the provisions of paragraph 1(b) of Article XXIII of GATT 1994 are applicable to a covered agreement, a panel or the Appellate Body may only make rulings and

recommendations where a party to the dispute considers that any benefit accruing to it directly or indirectly under the relevant covered agreement is being nullified or impaired or the attainment of any objective of that Agreement is being impeded as a result of the application by a Member of any measure, whether or not it conflicts with the provisions of that Agreement. Where and to the extent that such party considers and a panel or the Appellate Body determines that a case concerns a measure that does not conflict with the provisions of a covered agreement to which the provisions of paragraph 1(b) of Article XXIII of GATT 1994 are applicable, the procedures in this Understanding shall apply, subject to the following:

- (a) the complaining party shall present a detailed justification in support of any complaint relating to a measure which does not conflict with the relevant covered agreement;
- (b) where a measure has been found to nullify or impair benefits under, or impede the attainment of objectives, of the relevant covered agreement without violation thereof, there is no obligation to withdraw the measure. However, in such cases, the panel or the Appellate Body shall recommend that the Member concerned make a mutually satisfactory adjustment;
- (c) notwithstanding the provisions of Article 21, the arbitration provided for in paragraph 3 of Article 21, upon request of either party, may include a determination of the level of benefits which have been nullified or impaired, and may also suggest ways and means of reaching a mutually satisfactory adjustment; such suggestions shall not be binding upon the parties to the dispute;
- (d) notwithstanding the provisions of paragraph 1 of Article 22, compensation may be part of a mutually satisfactory adjustment as final settlement of the dispute.

2. Complaints of the Type Described in Paragraph 1(c) of Article XXIII of GATT 1994

Where the provisions of paragraph 1(c) of Article XXIII of GATT 1994 are applicable to a covered agreement, a panel may only make rulings and recommendations where a party considers that any benefit accruing to it directly or indirectly under the relevant covered agreement is being nullified or impaired or the attainment of any objective of that Agreement is being impeded as a result of the existence of any situation other than those to which the provisions of paragraphs 1(a) and 1(b) of Article XXIII of GATT 1994 are applicable. Where and to the extent that such party considers and a panel determines that the matter is covered by this paragraph, the procedures of this Understanding shall apply only up to and including the point in the proceedings where the panel report has been circulated to the Members. The dispute settlement rules and procedures contained in the Decision of 12 April 1989 (BISD 36S/61-67) shall apply to consideration for adoption, and surveillance and implementation of recommendations and rulings. The following shall also apply:

- (a) the complaining party shall present a detailed justification in support of any argument made with respect to issues covered under this paragraph;
- (b) in cases involving matters covered by this paragraph, if a panel finds that cases also involve dispute settlement matters other than those covered by this

paragraph, the panel shall circulate a report to the DSB addressing any such matters and a separate report on matters falling under this paragraph.

Article 27: Responsibilities of the Secretariat

1. The Secretariat shall have the responsibility of assisting panels, especially on the legal, historical and procedural aspects of the matters dealt with, and of providing secretarial and technical support.
2. While the Secretariat assists Members in respect of dispute settlement at their request, there may also be a need to provide additional legal advice and assistance in respect of dispute settlement to developing country Members. To this end, the Secretariat shall make available a qualified legal expert from the WTO technical cooperation services to any developing country Member which so requests. This expert shall assist the developing country Member in a manner ensuring the continued impartiality of the Secretariat.
3. The Secretariat shall conduct special training courses for interested Members concerning these dispute settlement procedures and practices so as to enable Members' experts to be better informed in this regard.

APPENDIX 1: AGREEMENTS COVERED BY THE UNDERSTANDING

- (A) Agreement Establishing the World Trade Organization
- (B) Multilateral Trade Agreements
- Annex 1A: Multilateral Agreements on Trade in Goods
- Annex 1B: General Agreement on Trade in Services
- Annex 1C: Agreement on Trade-Related Aspects of Intellectual Property Rights
- Annex 2: Understanding on Rules and Procedures Governing the Settlement of Disputes
- (C) Plurilateral Trade Agreements
- Annex 4: Agreement on Trade in Civil Aircraft
 Agreement on Government Procurement
 International Dairy Agreement
 International Bovine Meat Agreement

The applicability of this Understanding to the Plurilateral Trade Agreements shall be subject to the adoption of a decision by the parties to each agreement setting out the terms for the application of the Understanding to the individual agreement, including any special or additional rules or procedures for inclusion in Appendix 2, as notified to the DSB.

APPENDIX 2: SPECIAL OR ADDITIONAL RULES AND PROCEDURES CONTAINED IN THE COVERED AGREEMENTS

<i>Agreement</i>	<i>Rules and Procedures</i>
Agreement on the Application of Sanitary and Phytosanitary Measures	11.2
Agreement on Textiles and Clothing	2.14, 2.21, 4.4, 5.2, 5.4, 5.6, 6.9, 6.10, 6.11, 8.1 through 8.12
Agreement on Technical Barriers to Trade	14.2 through 14.4, Annex 2
Agreement on Implementation of Article VI of GATT 1994	17.4 through 17.7
Agreement on Implementation of Article VII of GATT 1994	19.3 through 19.5, Annex II.2(f), 3, 9, 21
Agreement on Subsidies and Countervailing Measures	4.2 through 4.12, 6.6, 7.2 through 7.10, 8.5, footnote 35, 24.4, 27.7, Annex V
General Agreement on Trade in Services Annex on Financial Services	XXII:3, XXIII:3 4
Annex on Air Transport Services	4
Decision on Certain Dispute Settlement Procedures for the GATS	1 through 5

The list of rules and procedures in this Appendix includes provisions where only a part of the provision may be relevant in this context.

Any special or additional rules or procedures in the Plurilateral Trade Agreements as determined by the competent bodies of each agreement and as notified to the DSB.

APPENDIX 3: WORKING PROCEDURES

1. In its proceedings the panel shall follow the relevant provisions of this Understanding. In addition, the following working procedures shall apply.
2. The panel shall meet in closed session. The parties to the dispute, and interested parties, shall be present at the meetings only when invited by the panel to appear before it.
3. The deliberations of the panel and the documents submitted to it shall be kept confidential. Nothing in this Understanding shall preclude a party to a dispute from disclosing statements of its own positions to the public. Members shall treat as confidential information submitted by another Member to the panel which that Member has designated as confidential. Where a party to a dispute submits a confidential version of its written submissions to the panel, it shall also, upon request of a Member, provide a non-confidential summary of the information contained in its submissions that could be disclosed to the public.
4. Before the first substantive meeting of the panel with the parties, the parties to the dispute shall transmit to the panel written submissions in which they present the facts of the case and their arguments.
5. At its first substantive meeting with the parties, the panel shall ask the party which has brought the complaint to present its case. Subsequently, and still at the same meeting, the party against which the complaint has been brought shall be asked to present its point of view.
6. All third parties which have notified their interest in the dispute to the DSB shall be invited in writing to present their views during a session of the first substantive meeting of the panel set aside for that purpose. All such third parties may be present during the entirety of this session.
7. Formal rebuttals shall be made at a second substantive meeting of the panel. The party complained against shall have the right to take the floor first to be followed by the complaining party. The parties shall submit, prior to that meeting, written rebuttals to the panel.
8. The panel may at any time put questions to the parties and ask them for explanations either in the course of a meeting with the parties or in writing.
9. The parties to the dispute and any third party invited to present its views in accordance with Article 10 shall make available to the panel a written version of their oral statements.
10. In the interest of full transparency, the presentations, rebuttals and statements referred to in paragraphs 5 to 9 shall be made in the presence of the parties. Moreover, each party's written submissions, including any comments on the descriptive part of the report and responses to questions put by the panel, shall be made available to the other party or parties.
11. Any additional procedures specific to the panel.

12. Proposed timetable for panel work:

- | | | |
|-----|--|-----------|
| (a) | Receipt of first written submissions of the parties: | |
| | (1) complaining Party: | 3-6 weeks |
| | (2) Party complained against: | 2-3 weeks |
| (b) | Date, time and place of first substantive meeting with the parties; third party session: | 1-2 weeks |
| (c) | Receipt of written rebuttals of the parties: | 2-3 weeks |
| (d) | Date, time and place of second substantive meeting with the parties: | 1-2 weeks |
| (e) | Issuance of descriptive part of the report to the parties: | 2-4 weeks |
| (f) | Receipt of comments by the parties on the descriptive part of the report: | 2 weeks |
| (g) | Issuance of the interim report, including the findings and conclusions, to the parties: | 2-4 weeks |
| (h) | Deadline for party to request review of part(s) of report: | 1 week |
| (i) | Period of review by panel, including possible additional meeting with parties: | 2 weeks |
| (j) | Issuance of final report to parties to dispute: | 2 weeks |
| (k) | Circulation of the final report to the Members: | 3 weeks |

The above calendar may be changed in the light of unforeseen developments. Additional meetings with the parties shall be scheduled if required.

APPENDIX 4: EXPERT REVIEW GROUPS

The following rules and procedures shall apply to expert review groups established in accordance with the provisions of paragraph 2 of Article 13.

1. Expert review groups are under the panel's authority. Their terms of reference and detailed working procedures shall be decided by the panel, and they shall report to the panel.
2. Participation in expert review groups shall be restricted to persons of professional standing and experience in the field in question.
3. Citizens of parties to the dispute shall not serve on an expert review group without the joint agreement of the parties to the dispute, except in exceptional circumstances when the panel considers that the need for specialized scientific expertise cannot be fulfilled otherwise. Government officials of parties to the dispute shall not serve on an expert review group. Members of expert review groups shall serve in their individual capacities and not as government representatives, nor as representatives of any organization. Governments or organizations shall therefore not give them instructions with regard to matters before an expert review group.
4. Expert review groups may consult and seek information and technical advice from any source they deem appropriate. Before an expert review group seeks such information or advice from a source within the jurisdiction of a Member, it shall inform the government of that Member. Any Member shall respond promptly and fully to any request by an expert review group for such information as the expert review group considers necessary and appropriate.
5. The parties to a dispute shall have access to all relevant information provided to an expert review group, unless it is of a confidential nature. Confidential information provided to the expert review group shall not be released without formal authorization from the government, organization or person providing the information. Where such information is requested from the expert review group but release of such information by the expert review group is not authorized, a non-confidential summary of the information will be provided by the government, organization or person supplying the information.
6. The expert review group shall submit a draft report to the parties to the dispute with a view to obtaining their comments, and taking them into account, as appropriate, in the final report, which shall also be issued to the parties to the dispute when it is submitted to the panel. The final report of the expert review group shall be advisory only.

World Trade Organization

Japan – Taxes on Alcoholic Beverages

Report of the Appellate Body, 4 October 1996

WORLD TRADE ORGANIZATION
APPELLATE BODY

<i>Japan - Taxes on Alcoholic Beverages</i>	AB-1996-2
Japan, Appellant/Appellee United States, Appellant/Appellee	Present:
Canada, Appellee European Communities, Appellee	Lacarte-Muró, Presiding Member Bacchus, Member El-Naggar, Member

Japan - Taxes on Alcoholic Beverages

AB-1996-2

A. Introduction

Japan and the United States appeal from certain issues of law and legal interpretations in the Panel Report, *Japan - Taxes on Alcoholic Beverages*¹ (the "Panel Report"). That Panel (the "Panel") was established to consider complaints by the European Communities, Canada and the United States against Japan relating to the Japanese Liquor Tax Law (Shuzeiho), Law No. 6 of 1953 as amended (the "Liquor Tax Law").²

The Panel Report was circulated to the Members of the World Trade Organization (the "WTO") on 11 July 1996. It contains the following conclusions:

Report of the Appellate Body

(i) Shochu and vodka are like products and Japan, by taxing the latter in excess of the former, is in violation of its obligation under Article III:2, first sentence, of the General Agreement on Tariffs and Trade 1994.

(ii) Shochu, whisky, brandy, rum, gin, genever, and liqueurs are "directly competitive or substitutable products" and Japan, by not taxing them similarly, is in violation of its obligation under

¹WT/DS8/R, WT/DS10/R, WT/DS11/R.

²Norway originally reserved its right as a third party to the dispute but subsequently informed the Panel that it was withdrawing its request to participate as a third party.

Article III:2, second sentence, of the General Agreement on Tariffs and Trade 1994.³

The Panel made the following recommendations:

- 7.2 The Panel recommends that the Dispute Settlement Body request Japan to bring the Liquor Tax Law into conformity with its obligations under the General Agreement on Tariffs and Trade 1994.⁴
- On 8 August 1996, Japan notified the Dispute Settlement Body⁵ of the WTO of its decision to appeal certain issues of law covered in the Panel Report and legal interpretations developed by the Panel, pursuant to paragraph 4 of Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU") and filed a Notice of Appeal with the Appellate Body, pursuant to Rule 20 of the *Working Procedures for Appellate Review* (the "*Working Procedures*").⁶ On 19 August 1996, Japan filed an appellant's submission.⁷ On 23 August 1996, the United States filed an appellant's submission pursuant to Rule 23(1) of the *Working Procedures*. The European Communities, Canada and the United States submitted appellees' submissions pursuant to Rule 22 of the *Working Procedures*, on 2 September 1996. That same day, Japan submitted an appellee's submission pursuant to Rule 23(3) of the *Working Procedures*.

The oral hearing contemplated by Rule 27 of the *Working Procedures* was held on 9 September 1996. The participants presented their arguments and answered questions from the Division of the Appellate Body hearing the appeal (the "Division"). The participants answered most of these questions orally at the hearing. They answered some in writing.⁸ The Division gave each participant an opportunity to respond to the written post-hearing memoranda of the other participants.⁹

B. Arguments of Participants

1. Japan

³Panel Report, para. 7.1.

⁴Panel Report, para. 7.2.

⁵WT/DS8/9, WT/DS10/9, WT/DS11/6.

⁶WT/AB/WP/1.

⁷Pursuant to Rule 21(1) of the *Working Procedures*.

⁸Pursuant to Rule 28(1) of the *Working Procedures*.

⁹Pursuant to Rule 28(2) of the *Working Procedures*.

Japan appeals from the Panel's findings and conclusions, as well as from certain of the legal interpretations developed by the Panel. Japan argues that the Panel erred in its interpretation of Article III:2, first and second sentences of the General Agreement on Tariffs and Trade 1994 (the "GATT 1994"), which is an integral part of the *Marrakesh Agreement Establishing the World Trade Organization* (the "*WTO Agreement*").¹⁰ According to Japan, with respect to both the first and second sentences of Article III:2, the Panel erred in: (1) disregarding the need to determine whether the Liquor Tax Law has the aim of affording protection to domestic production; (2) ignoring whether there is "linkage" between the origin of products and the tax treatment they incur and, in this respect, not comparing the tax treatment of domestic products as a whole and foreign products as a whole; and (3) not giving proper weight to the tax/price ratio as a yardstick to compare the tax burdens.

With respect to the first sentence of Article III:2, Japan argues that the Panel erred by virtually ignoring Article III:1, particularly the phrase "so as to afford protection to domestic production", as part of the context of Article III:2. Japan maintains also that the title of Article III forms part of the context of Article III:2, and that the object and purpose of the GATT 1994 and the *WTO Agreement* as a whole must also be taken into account in interpreting Article III:2. Japan argues that the interpretation of Article III:2, first sentence, in the light of these considerations, requires an examination of both the aim and the effect of the measure in question. Japan also alleges that the Panel erred in placing excessive emphasis on tariff classification in finding that shochu and vodka are "like products" within the meaning of Article III:2, first sentence, arguing that the relevant tariff bindings indicate that these products are not "like".

With respect to the second sentence of Article III:2, Japan asserts that the Panel erred by failing to interpret correctly the principle of Article III:1, in particular, the language "so as to afford protection to domestic production", erroneously placing excessive emphasis on the phrase "not similarly taxed" in the Interpretative Note *Ad Article III:2*. Japan claims further that the Panel erred by failing to examine the issue of *de minimis* differences in the light of the principle of "so as to afford protection to domestic production"; the Panel examined the issue of *de minimis* differences only by comparing taxes in terms of taxation per kilolitre of product and taxation per degree of alcohol.

With respect to the points of appeal raised by the United States in its appellant's submission, Japan responds that the arguments advanced by the United States are not based on a correct understanding of the Japanese liquor tax system. Japan argues that the Liquor Tax Law has the legitimate policy purpose of ensuring neutrality and equity, particularly horizontal equity, and that it has neither the aim nor the effect of protecting domestic production. Japan asserts that it is not correct

¹⁰Done at Marrakesh, Morocco, 15 April 1994 and entered into effect on 1 January 1995.

to conclude that all distilled liquors are "like products" under Article III:2, first sentence, or to conclude that the Liquor Tax Law is inconsistent with Article III:2 because it imposes a tax on imported distilled liquors in excess of the tax on like domestic products.

2. United States

The United States supports the Panel's overall conclusions, but appeals nonetheless. The United States alleges several errors in the findings of the Panel and the legal interpretations developed by the Panel in reaching its conclusions in the Panel Report. The United States maintains that the Panel erred in its interpretation of Article III:2, first and second sentences, principally as a result of an erroneous understanding of the relationship between Article III:2 and Article III:1. The United States contends that the Panel disregarded Article III:1, which the United States sees as an integral part of the context that must be considered in interpreting Article III:2, and Article III generally. The United States asserts that Article III:1 sets out the object and purpose of Article III and must therefore be considered in any interpretation of the text of Article III:2. The United States argues that the Panel did not look beyond the text of Article III:2 in interpreting Article III:2 and thereby fell into error.

More specifically, with respect to the first sentence of Article III:2, the United States submits that the Panel erred in finding that "likeness" can be determined purely on the basis of physical characteristics, consumer uses and tariff classification without considering also the context and purpose of Article III, as set out in Article III:1, and without considering, in particular, whether regulatory distinctions are made, in the language of Article III:1, "so as to afford protection to domestic production". The United States concludes that the Panel erred in its interpretation of Article III:2, first sentence in: failing to interpret Article III:2, first sentence, in the light of Article III:1, consistently with the analysis in *United States - Measures Affecting Alcoholic and Malt Beverages* ("*Malt Beverages*");¹¹ not finding that all distilled spirits constitute "like products" under Article III:2, first sentence; and drawing a connection between national treatment obligations and tariff bindings.

With respect to the second sentence of Article III:2 and the *Ad Article* thereto, the United States argues that the Panel erred with respect to the *Ad Article* to the second sentence in its interpretation of the term "directly competitive or substitutable products" by not considering whether a tax distinction is applied "in a manner contrary to the principles set forth in paragraph 1 of [Article III]", that is, "so as to afford protection to domestic production". The United States also claims that the Panel erred by using cross-price elasticity as the "decisive criterion" for whether products are "directly competitive or substitutable".

¹¹Panel Report adopted on 19 June 1992, BISD 39S/206.

The United States contends as well that the Panel erred in not addressing the full scope of the products subject to the dispute and that there is inconsistency between the Panel's conclusions in paragraph 7.1(ii) of the Panel Report and in paragraphs 6.32-6.33 of the Panel Report. The United States further submits that the Panel erred in incorrectly assessing the relationship between Article III:2 and Article III:4 by stating that the product coverage of the two provisions is not identical.

Finally, the United States claims that the Panel erred in incorrectly characterizing adopted panel reports as "subsequent practice" within the meaning of Article 31(3)(b) of the *Vienna Convention on the Law of Treaties* (the "*Vienna Convention*").¹² According to the United States, adopted panel reports serve only to clarify, for the purposes of the particular dispute, the application of the rights and obligations of the parties to that dispute to the precise set of circumstances at that time. The *decision* to adopt a panel report constitutes a "decision" within the meaning of paragraph 1(b)(iv) of the language incorporating the GATT 1994 into the *WTO Agreement*, however, the adopted panel report as such does not constitute a "decision" in this sense.

With respect to the claims of error raised in Japan's appellant's submission, the United States responds that: the national treatment provisions in Article III of GATT 1994 can apply to origin-neutral measures; Japan's taxation under the Liquor Tax Law does have the aim and effect of affording protection to domestic production; and the tax/price ratios cited by Japan are not the appropriate basis for evaluating the consistency of taxation under the Liquor Tax Law with Article III:2.

3. European Communities

The European Communities support the Panel's conclusions, and largely agree with the legal interpretations of Article III:2, first and second sentences, employed by the Panel. With respect to Article III:2, first sentence, the European Communities submit that the Panel's reasons for adopting the interpretation in the Panel Report, and thus for rejecting a specific test of "aims and effects", are sound and "in accordance with customary rules of interpretation of public international law", as contemplated by Article 3.2 of the *DSU*.¹³ The European Communities contend that the Panel made it clear that the essential criterion for a "like product" determination is similarity of physical

¹²23 May 1969, 1155 U.N.T.S. 331; 8 *International Legal Materials* 679.

¹³Article 3.2 of the *DSU* states in pertinent part:

...The Members recognize that [the dispute settlement system] serves to preserve the rights and obligations of Members under the covered agreements, and to clarify the existing provisions of those agreements in accordance with customary rules of interpretation of public international law.

characteristics and that tariff nomenclatures may be relevant for a determination of "likeness" because they constitute an objective classification of products according to their physical characteristics. The European Communities maintain that the Panel's decision to identify only vodka and shochu as "like products" for purposes of Article III:2 cannot be regarded as arbitrary or insufficiently motivated. Although not entirely satisfied with the Panel's conclusions on the range of products found to be "like" under Article III:2, first sentence, the European Communities claim that those conclusions primarily involve the assessment of facts and, therefore, are not reviewable by the Appellate Body, which is limited to the consideration of issues of law under Article 17.6 of the DSU.¹⁴

With respect to Article III:2, second sentence, the European Communities argue that the Panel did not rule that cross-price elasticity is the decisive criterion for a determination that two products are directly competitive or substitutable, but rather ruled that such elasticity is only one of the criteria to be considered. The European Communities view the Panel's findings on the issue of the tax/price ratios as factual; however, if the Appellate Body nevertheless considers it necessary to rule on this issue, the European Communities argue that tax/price ratios are not the most appropriate yardstick for comparing tax burdens imposed by a system of specific taxes. The European Communities submit further that the Panel was correct in ignoring the linkage between differences in taxation and the origin of products. The European Communities assert that Japan's argument that the Liquor Tax Law is not applied "so as to afford protection to domestic production" of shochu because shochu is also produced in other countries and, therefore, is not an "inherently domestic product" rests on two wrong propositions: first, that "domestic production" of shochu is not "protected" if the same tax treatment is accorded to foreign shochu; and, second, that the mere fact that shochu is produced in third countries is sufficient to conclude that foreign shochu may benefit from the lower tax as much as domestic shochu and, consequently, that protection is not afforded only to domestic production. The European Communities further contend that the United States is incorrect to attribute to the Panel the statement that the product coverage of Article III:2 and Article III:4 is not equivalent.

With respect to the status of adopted panel reports, the European Communities conclude that the Panel's characterization of them as "subsequent practice in a specific case" is intrinsically contradictory, since the essence of subsequent practice is that it consists of a large number of legally relevant events and pronouncements. The European Communities' view is that one adopted panel report "would merely constitute part of a wall of the house that constitutes subsequent practice". The European Communities, therefore, ask the Appellate Body to modify the Panel's legal terminology on

¹⁴ Article 17.6 of the DSU states:

An appeal shall be limited to issues of law covered in the panel report and legal interpretations developed by the panel.

this issue. The European Communities further consider that the *decision* to adopt a panel report constitutes a "decision" within the meaning of paragraph 1(b)(iv) of the language of Annex 1A incorporating the GATT 1994 into the *WTO Agreement*, however an adopted panel report is not itself a "decision" in this sense.

4. Canada

Canada confined its submissions and arguments on appeal to Article III:2, second sentence. Canada supports the Panel's legal interpretations of Article III:2, second sentence, as well as the conclusion of the Panel that the Liquor Tax Law is inconsistent with Article III:2, second sentence. Canada claims that the Panel properly found that the phrase "so as to afford protection" in Article III:1 does not require a consideration of both the aim and effect of a measure to determine whether that measure affords protection to domestic production. Canada argues further that: first, the Panel Report did not create a *per se* test in Article III:2, second sentence, and did not equate the reference to "so as to afford protection to domestic production" with a determination that directly competitive or substitutable products are "not similarly taxed"; second, the Panel had sufficient evidence before it to conclude that differential tax treatment under the Liquor Tax Law favours domestic shochu production; third, the Panel Report considered in detail the issue of the tax/price ratios and assigned them their proper weight in assessing the tax burden on the products in dispute; and, finally, the Panel interpreted the phrase "directly competitive or substitutable" properly and did not identify "cross-price elasticity" as *the* decisive criterion for assessment of whether products are directly competitive or substitutable.

With regard to the status of adopted panel reports, Canada argues that decisions to adopt panel reports under GATT 1947 constitute "decisions" under Article 1(b)(iv) of the GATT 1994.

C. Issues Raised in the Appeal

The appellants, Japan and the United States, have raised the following issues in this appeal:

I. Japan

(a) whether the Panel erred in failing to interpret Article III:2, first and second sentences, in the light of Article III:1;

- (b) whether the Panel erred in rejecting an "aim-and-effect" test in establishing whether the Liquor Tax Law is applied "so as to afford protection to domestic production";
- (c) whether the Panel erred in failing to examine the effect of affording protection to domestic production from the perspective of the linkage between the origin of products and their treatment under the Liquor Tax Law;
- (d) whether the Panel failed to give proper weight to tax/price ratios as a yardstick for comparing tax burdens under Article III:2, first and second sentences;
- (e) whether the Panel erred in interpreting and applying Article III:2, second sentence, by equating the language "not similarly taxed" in *Ad Article III:2*, second sentence, with "so as to afford protection" in Article III:1; and
- (f) whether the Panel erred in placing excessive emphasis on tariff classification as a criterion for determining "like products".

2. United States

- (a) whether the Panel erred in failing to interpret Article III:2, first and second sentences, in the light of Article III:1;
- (b) whether the Panel erred in failing to find that all distilled spirits are "like products";
- (c) whether the Panel erred in drawing a connection between national treatment obligations and tariff bindings;
- (d) whether the Panel erred in interpreting and applying Article III:2, second sentence, by equating the language "not similarly taxed" in *Ad Article III:2*, second sentence, with "so as to afford protection" in Article III:1;
- (e) whether the Panel erred in its conclusions on "directly competitive or substitutable products" by examining cross-price elasticity as "the decisive criterion";

- (f) whether the Panel erred in failing to maintain consistency between the conclusions in paragraph 7.1(ii) of the Panel Report on "directly competitive or substitutable products" and the conclusions in paragraphs 6.32-6.33 of the Panel Report, and whether the Panel erred in failing to address the full scope of products subject of this dispute;
- (g) whether the Panel erred in finding that the coverage of Article III:2 and Article III:4 are not equivalent; and
- (h) whether the Panel erred in its characterization of panel reports adopted by the GATT CONTRACTING PARTIES and the WTO Dispute Settlement Body as "subsequent practice in a specific case by virtue of the decision to adopt them".

D. Treaty Interpretation

Article 3.2 of the *DSU* directs the Appellate Body to clarify the provisions of GATT 1994 and the other "covered agreements" of the *WTO Agreement* "in accordance with customary rules of interpretation of public international law". Following this mandate, in *United States - Standards for Reformulated and Conventional Gasoline*,¹⁵ we stressed the need to achieve such clarification by reference to the fundamental rule of treaty interpretation set out in Article 31(1) of the *Vienna Convention*. We stressed there that this general rule of interpretation "has attained the status of a rule of customary or general international law".¹⁶ There can be no doubt that Article 32 of the *Vienna Convention*, dealing with the role of supplementary means of interpretation, has also attained the same status.¹⁷

Article 31, as a whole, and Article 32 are each highly pertinent to the present appeal. They provide as follows:

¹⁵Adopted 20 May 1996, WT/DS2/9.

¹⁶*Ibid.*, at p. 17.

¹⁷See e.g.: Jiménez de Aréchaga, "International Law in the Past Third of a Century" (1978-1) 159 *Recueil des Cours* p.1 at 42; *Territorial Dispute (Libyan Arab Jamahiriya/Chad)*, Judgment, (1994), I.C.J. Reports, p. 6 at 20; *Maritime Delimitation and Territorial Questions between Qatar and Bahrain, Jurisdiction and Admissibility*, Judgment, (1995), I.C.J. Reports, p. 6 at 18; *Interpretation of the Convention of 1919 Concerning Employment of Women during the Night* (1932), P.C.I.J., Series A/B, No. 50, p. 365 at 380; cf. the *Serbian and Brazilian Loans Cases* (1929), P.C.I.J., Series A, Nos. 20-21, p. 5 at 30; *Constitution of the Maritime Safety Committee of the IMCO* (1960), I.C.J. Reports, p. 150 at 161; *Air Transport Services Agreement Arbitration (United States of America v. France)* (1963), *International Law Reports*, 38, p. 182 at 235-43.

ARTICLE 31

General rule of interpretation

1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.

2. The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes:

- (a) any agreement relating to the treaty which was made between all the parties in connexion with the conclusion of the treaty;
- (b) any instrument which was made by one or more parties in connexion with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.

3. There shall be taken into account together with the context:

- (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
- (b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
- (c) any relevant rules of international law applicable in the relations between the parties.

4. A special meaning shall be given to a term if it is established that the parties so intended.

ARTICLE 32

Supplementary means of interpretation

Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31:

- (a) leaves the meaning ambiguous or obscure; or
- (b) leads to a result which is manifestly absurd or unreasonable.

Article 31 of the *Vienna Convention* provides that the words of the treaty form the foundation for the interpretive process: "interpretation must be based above all upon the text of the treaty".¹⁸ The provisions of the treaty are to be given their ordinary meaning in their context.¹⁹ The object and purpose of the treaty are also to be taken into account in determining the meaning of its provisions.²⁰ A fundamental tenet of treaty interpretation flowing from the general rule of interpretation set out in Article 31 is the principle of effectiveness (*ut res magis valeat quam pereat*).²¹ In *United States - Standards for Reformulated and Conventional Gasoline*, we noted that "[o]ne of the corollaries of the 'general rule of interpretation' in the *Vienna Convention* is that interpretation must give meaning and effect to all the terms of the treaty. An interpreter is not free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility".²²

E. Status of Adopted Panel Reports

In this case, the Panel concluded that,

...panel reports adopted by the GATT CONTRACTING PARTIES and the WTO Dispute Settlement Body constitute subsequent practice in a specific case by virtue of the decision to adopt them. Article 1(b)(iv) of GATT 1994 provides institutional recognition that adopted panel reports constitute subsequent practice. Such reports are an integral part of GATT 1994, since they constitute "other decisions of the CONTRACTING PARTIES to GATT 1947".²³

¹⁸*Territorial Dispute (Libyan Arab Jamahiriya/Chad)*, Judgment, (1994) I.C.J. Reports, p. 6 at 20; *Maritime Delimitation and Territorial Questions between Qatar and Bahrain, Jurisdiction and Admissibility, Judgment*, (1995) I.C.J. Reports, p. 6 at 18.

¹⁹See, e.g., *Competence of the General Assembly for the Admission of a State to the United Nations (Second Admissions Case)* (1950), I.C.J. Reports, p. 4 at 8, in which the International Court of Justice stated: "The Court considers it necessary to say that the first duty of a tribunal which is called upon to interpret and apply the provisions of a treaty, is to endeavour to give effect to them in their natural and ordinary meaning and in the context in which they occur".

²⁰That is, the treaty's "object and purpose" is to be referred to in determining the meaning of the "terms of the treaty" and not as an independent basis for interpretation: Harris, *Cases and Materials on International Law* (4th ed., 1991) p. 770; Jiménez de Aréchaga, "International Law in the Past Third of a Century" (1978-1) 159 *Recueil des Cours* p. 1 at 44; Sinclair, *The Vienna Convention and the Law of Treaties* (2nd ed., 1984), p. 130. See e.g. Oppenheim's *International Law* (9th ed., Jennings and Watts, eds., 1992) Vol. 1, p.1273; *Competence of the ILO to Regulate the Personal Work of the Employer* (1926), P.C.I.J., Series B, No. 13, p. 6 at 18; *International Status of South West Africa* (1962), I.C.J. Reports, p. 128 at 336; *Re Competence of Conciliation Commission* (1955), 22 *International Law Reports*, p. 867 at 871.

²¹See also (1966) *Yearbook of the International Law Commission*, Vol. II, p. 219: "When a treaty is open to two interpretations one of which does and the other does not enable the treaty to have appropriate effects, good faith and the objects and purposes of the treaty demand that the former interpretation should be adopted."

²²*United States - Standards for Reformulated and Conventional Gasoline*, WT/DS2/9, adopted 20 May 1996, p. 23.

²³Panel Report, para. 6.10.

Article 31(3)(b) of the *Vienna Convention* states that "any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation" is to be "taken into account together with the context" in interpreting the terms of the treaty. Generally, in international law, the essence of subsequent practice in interpreting a treaty has been recognized as a "concordant, common and consistent" sequence of acts or pronouncements which is sufficient to establish a discernable pattern implying the agreement of the parties regarding its interpretation.²⁴ An isolated act is generally not sufficient to establish subsequent practice;²⁵ it is a sequence of acts establishing the agreement of the parties that is relevant.²⁶

Although GATT 1947²⁷ panel reports were adopted by decisions of the CONTRACTING PARTIES²⁸, a decision to adopt a panel report did not under GATT 1947 constitute agreement by the CONTRACTING PARTIES on the legal reasoning in that panel report. The generally-accepted view under GATT 1947 was that the conclusions and recommendations in an adopted panel report bound the parties to the dispute in that particular case, but subsequent panels did not feel legally bound by the details and reasoning of a previous panel report.²⁹

We do not believe that the CONTRACTING PARTIES, in deciding to adopt a panel report, intended that their decision would constitute a definitive interpretation of the relevant provisions of GATT 1947. Nor do we believe that this is contemplated under GATT 1994. There is specific cause for this conclusion in the *WTO Agreement*. Article IX:2 of the *WTO Agreement* provides: "The Ministerial Conference and the General Council shall have the exclusive authority to adopt interpretations of this Agreement and of the Multilateral Trade Agreements". Article IX:2 provides further that such decisions "shall be taken by a three-fourths majority of the Members". The fact that such an "exclusive authority" in interpreting the treaty has been established so specifically in the *WTO Agreement* is reason enough to conclude that such authority does not exist by implication or by inadvertence elsewhere.

²⁴Sinclair, *The Vienna Convention on the Law of Treaties* (2nd ed., 1984), p. 137; Yasseen, "L'interprétation des traités d'après la Convention de Vienne sur le Droit des Traités" (1976-II) 151 *Recueil des Cours* p. 1 at 48.

²⁵Sinclair, *supra*, footnote 24, p. 137.

²⁶(1966) Yearbook of the International Law Commission, Vol. II, p. 222; Sinclair, *supra*, footnote 24, p. 138.

²⁷By GATT 1947, we refer throughout to the General Agreement on Tariffs and Trade, dated 30 October 1947, annexed to the Final Act Adopted at the Conclusion of the Second Session of the Preparatory Committee of the United Nations Conference on Trade and Employment, as subsequently rectified, amended or modified.

²⁸By CONTRACTING PARTIES, we refer throughout to the CONTRACTING PARTIES of GATT 1947.

²⁹*European Economic Community - Restrictions on Imports of Dessert Apples*, BISD 36S/93, para. 12.1.

Historically, the decisions to adopt panel reports under Article XXIII of the GATT 1947 were different from joint action by the CONTRACTING PARTIES under Article XXV of the GATT 1947. Today, their nature continues to differ from interpretations of the GATT 1994 and the other Multilateral Trade Agreements under the *WTO Agreement* by the WTO Ministerial Conference or the General Council. This is clear from a reading of Article 3.9 of the *DSU*, which states:

The provisions of this Understanding are without prejudice to the rights of Members to seek authoritative interpretation of provisions of a covered agreement through decision-making under the *WTO Agreement* or a covered agreement which is a Plurilateral Trade Agreement.

Article XVI:1 of the *WTO Agreement* and paragraph 1(b)(iv) of the language of Annex 1A incorporating the GATT 1994 into the *WTO Agreement* bring the legal history and experience under the GATT 1947 into the new realm of the WTO in a way that ensures continuity and consistency in a smooth transition from the GATT 1947 system. This affirms the importance to the Members of the WTO of the experience acquired by the CONTRACTING PARTIES to the GATT 1947 -- and acknowledges the continuing relevance of that experience to the new trading system served by the WTO. Adopted panel reports are an important part of the GATT *acquis*. They are often considered by subsequent panels. They create legitimate expectations among WTO Members, and, therefore, should be taken into account where they are relevant to any dispute. However, they are not binding, except with respect to resolving the particular dispute between the parties to that dispute.³⁰ In short, their character and their legal status have not been changed by the coming into force of the *WTO Agreement*.

For these reasons, we do not agree with the Panel's conclusion in paragraph 6.10 of the Panel Report that "panel reports adopted by the GATT CONTRACTING PARTIES and the WTO Dispute Settlement Body constitute subsequent practice in a specific case" as the phrase "subsequent practice" is used in Article 31 of the *Vienna Convention*. Further, we do not agree with the Panel's conclusion in the same paragraph of the Panel Report that adopted panel reports in themselves constitute "other decisions of the CONTRACTING PARTIES to GATT 1947" for the purposes of paragraph 1(b)(iv) of the language of Annex 1A incorporating the GATT 1994 into the *WTO Agreement*.

³⁰It is worth noting that the Statute of the International Court of Justice has an explicit provision, Article 59, to the same effect. This has not inhibited the development by that Court (and its predecessor) of a body of case law in which considerable reliance on the value of previous decisions is readily discernible.

However, we agree with the Panel's conclusion in that same paragraph of the Panel Report that *unadopted* panel reports "have no legal status in the GATT or WTO system since they have not been endorsed through decisions by the CONTRACTING PARTIES to GATT or WTO Members".³¹ Likewise, we agree that "a panel could nevertheless find useful guidance in the reasoning of an unadopted panel report that it considered to be relevant".³²

F. Interpretation of Article III

The *WTO Agreement* is a treaty – the international equivalent of a contract. It is self-evident that in an exercise of their sovereignty, and in pursuit of their own respective national interests, the Members of the WTO have made a bargain. In exchange for the benefits they expect to derive as Members of the WTO, they have agreed to exercise their sovereignty according to the commitments they have made in the *WTO Agreement*.

One of those commitments is Article III of the GATT 1994, which is entitled "National Treatment on Internal Taxation and Regulation". For the purpose of this appeal, the relevant parts of Article III read as follows:

Article III

National Treatment on Internal Taxation and Regulation

1. The contracting parties recognize that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products, and internal quantitative regulations requiring the mixture, processing or use of products in specified amounts or proportions, should not be applied to imported or domestic products so as to afford protection to domestic production.*
2. The products of the territory of any contracting party imported into the territory of any other contracting party shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products. Moreover, no contracting party shall otherwise apply internal taxes or other internal charges to imported or domestic products in a manner contrary to the principles set forth in paragraph 1.*

³¹Panel Report, para. 6.10.

³²*Ibid.*

Ad Article III

Paragraph 2

A tax conforming to the requirements of the first sentence of paragraph 2 would be considered to be inconsistent with the provisions of the second sentence only in cases where competition was involved between, on the one hand, the taxed product and, on the other hand, a directly competitive or substitutable product which was not similarly taxed.

The broad and fundamental purpose of Article III is to avoid protectionism in the application of internal tax and regulatory measures. More specifically, the purpose of Article III "is to ensure that internal measures 'not be applied to imported or domestic products so as to afford protection to domestic production'".³³ Toward this end, Article III obliges Members of the WTO to provide equality of competitive conditions for imported products in relation to domestic products.³⁴ "[T]he intention of the drafters of the Agreement was clearly to treat the imported products in the same way as the like domestic products once they had been cleared through customs. Otherwise indirect protection could be given".³⁵ Moreover, it is irrelevant that "the trade effects" of the tax differential between imported and domestic products, as reflected in the volumes of imports, are insignificant or even non-existent; Article III protects expectations not of any particular trade volume but rather of the equal competitive relationship between imported and domestic products.³⁶ Members of the WTO are free to pursue their own domestic goals through internal taxation or regulation so long as they do not do so in a way that violates Article III or any of the other commitments they have made in the *WTO Agreement*.

The broad purpose of Article III of avoiding protectionism must be remembered when considering the relationship between Article III and other provisions of the *WTO Agreement*. Although the protection of negotiated tariff concessions is certainly one purpose of Article III,³⁷ the statement in Paragraph 6.13 of the Panel Report that "one of the main purposes of Article III is to guarantee that WTO Members will not undermine through internal measures their commitments under Article II" should not be overemphasized. The sheltering scope of Article III is not limited to products that are

³³*United States - Section 337 of the Tariff Act of 1930*, BISD 36S/345, para. 5.10.

³⁴*United States - Taxes on Petroleum and Certain Imported Substances*, BISD 34S/136, para. 5.1.9; *Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83, para. 5.5(b).

³⁵*Italian Discrimination Against Imported Agricultural Machinery*, BISD 7S/60, para. 11.

³⁶*United States - Taxes on Petroleum and Certain Imported Substances*, BISD 34S/136, para. 5.1.9.

³⁷*Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83, para. 5.5(b); *Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies*, BISD 39S/27, para. 5.30.

the subject of tariff concessions under Article II. The Article III national treatment obligation is a general prohibition on the use of internal taxes and other internal regulatory measures so as to afford protection to domestic production. This obligation clearly extends also to products not bound under Article II.³⁸ This is confirmed by the negotiating history of Article III.³⁹

G. Article III:1

The terms of Article III must be given their ordinary meaning -- in their context and in the light of the overall object and purpose of the *WTO Agreement*. Thus, the words actually used in the Article provide the basis for an interpretation that must give meaning and effect to all its terms. The proper interpretation of the Article is, first of all, a textual interpretation. Consequently, the Panel is correct in seeing a distinction between Article III:1, which "contains general principles", and Article III:2, which "provides for specific obligations regarding internal taxes and internal charges".⁴⁰

³⁸*Brazilian Internal Taxes*, BISD II/181, para. 4; *United States - Taxes on Petroleum and Certain Imported Substances*, BISD 34S/136, para. 5.1.9; *EEC - Regulation on Imports of Parts and Components*, BISD 37S/132, para. 5.4.

³⁹At the Second Session of the Preparatory Committee of the United Nations Conference on Trade and Employment, held in 1947, delegates in the Tariff Agreement Committee addressed the issue of whether to include the national treatment clause from the draft Charter for an International Trade Organization ("ITO Charter") in the GATT 1947. One delegate noted:

This Article in the Charter had two purposes, as I understand it. The first purpose was to protect the items in the Schedule or any other Schedule concluded as a result of any subsequent negotiations and agreements - that is, to ensure that a country offering a tariff concession could not nullify that tariff concession by imposing an internal tax on the commodity, which had an equivalent effect. If that were the sole purpose and content of this Article, there could really be no objection to its inclusion in the General Agreement. But the Article in the Charter had an additional purpose. That purpose was to prevent the use of internal taxes as a system of protection. It was part of a series of Articles designed to concentrate national protective measures into the forms permitted under the Charter, i.e. subsidies and tariffs, and since we have taken over this Article from the Charter, we are, by including the Article, doing two things: so far as the countries become parties to the Agreement, we are, first of all, ensuring that the tariff concessions they grant one another cannot be nullified by the imposition of corresponding internal taxes; but we are also ensuring that those countries which become parties to the Agreement undertake not to use internal taxes as a system of protection.

This view is reinforced by the following statement of another delegate:

... [Article III] is necessary to protect not only scheduled items in the Agreement, but, indeed, all items for all our exports and the exports of any country. If that is not done, then every item which does not appear in the Schedule would have to be reconsidered and possibly tariff negotiations re-opened if Article III were changed to permit any action on these non-scheduled items.

See EPCT/TAC/PV.10, pp. 3 and 33.

⁴⁰Panel Report, para. 6.12.

Article III:1 articulates a general principle that internal measures should not be applied so as to afford protection to domestic production. This general principle informs the rest of Article III. The purpose of Article III:1 is to establish this general principle as a guide to understanding and interpreting the specific obligations contained in Article III:2 and in the other paragraphs of Article III, while respecting, and not diminishing in any way, the meaning of the words actually used in the texts of those other paragraphs. In short, Article III:1 constitutes part of the context of Article III:2, in the same way that it constitutes part of the context of each of the other paragraphs in Article III. Any other reading of Article III would have the effect of rendering the words of Article III:1 meaningless, thereby violating the fundamental principle of effectiveness in treaty interpretation. Consistent with this principle of effectiveness, and with the textual differences in the two sentences, we believe that Article III:1 informs the first sentence and the second sentence of Article III:2 in different ways.

H. Article III:2

1. First Sentence

Article III:1 informs Article III:2, first sentence, by establishing that if imported products are taxed in excess of like domestic products, then that tax measure is inconsistent with Article III. Article III:2, first sentence does not refer specifically to Article III:1. There is no specific invocation in this first sentence of the general principle in Article III:1 that admonishes Members of the WTO not to apply measures "so as to afford protection". This omission must have some meaning. We believe the meaning is simply that the presence of a protective application need not be established separately from the specific requirements that are included in the first sentence in order to show that a tax measure is inconsistent with the general principle set out in the first sentence. However, this does not mean that the general principle of Article III:1 does not apply to this sentence. To the contrary, we believe the first sentence of Article III:2 is, in effect, an application of this general principle. The ordinary meaning of the words of Article III:2, first sentence leads inevitably to this conclusion. Read in their context and in the light of the overall object and purpose of the *WTO Agreement*, the words of the first sentence require an examination of the conformity of an internal tax measure with Article III by determining, first, whether the taxed imported and domestic products are "like" and, second, whether

the taxes applied to the imported products are "in excess of" those applied to the like domestic products. If the imported and domestic products are "like products", and if the taxes applied to the imported products are "in excess of" those applied to the like domestic products, then the measure is inconsistent with Article III:2, first sentence.⁴¹

This approach to an examination of Article III:2, first sentence, is consistent with past practice under the GATT 1947.⁴² Moreover, it is consistent with the object and purpose of Article III:2, which the panel in the predecessor to this case dealing with an earlier version of the Liquor Tax Law, *Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages ("1987 Japan - Alcohol")*, rightly stated as "promoting non-discriminatory competition among imported and like domestic products [which] could not be achieved if Article III:2 were construed in a manner allowing discriminatory and protective internal taxation of imported products in excess of like domestic products".⁴³

(a) "Like Products"

Because the second sentence of Article III:2 provides for a separate and distinctive consideration of the protective aspect of a measure in examining its application to a broader category of products that are not "like products" as contemplated by the first sentence, we agree with the Panel that the first sentence of Article III:2 must be construed narrowly so as not to condemn measures that its strict terms are not meant to condemn. Consequently, we agree with the Panel also that the definition of "like products" in Article III:2, first sentence, should be construed narrowly.⁴⁴

⁴²See *Brazilian Internal Taxes*, BISD IV/181, para. 14; *Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83, para. 5.5(d); *United States - Taxes on Petroleum and Certain Imported Substances*, BISD 34S/136, para. 5.1.1; *United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco*, DS44/R, adopted on 4 October 1994.

⁴³*Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83, para. 5.5(c).

⁴⁴We note the argument on appeal that the Panel suggested in paragraph 6.20 of the Panel Report that the product coverage of Article III:2 is not identical to the coverage of Article III:4. That is not what the Panel said. The Panel said the following:

⁴¹In accordance with Article 3.8 of the DSU, such a violation is *prima facie* presumed to nullify or impair benefits under Article XXIII of the GATT 1994. Article 3.8 reads as follows:

In cases where there is an infringement of the obligations assumed under a covered agreement, the action is considered *prima facie* to constitute a case of nullification or impairment. This means that there is normally a presumption that a breach of the rules has an adverse impact on other Members parties to that covered agreement, and in such cases, it shall be up to the Member against whom the complaint has been brought to rebut the charge.

How narrowly is a matter that should be determined separately for each tax measure in each case. We agree with the practice under the GATT 1947 of determining whether imported and domestic products are "like" on a case-by-case basis. The Report of the Working Party on *Border Tax Adjustments*, adopted by the CONTRACTING PARTIES in 1970, set out the basic approach for interpreting "like or similar products" generally in the various provisions of the GATT 1947:

... the interpretation of the term should be examined on a case-by-case basis. This would allow a fair assessment in each case of the different elements that constitute a "similar" product. Some criteria were suggested for determining, on a case-by-case basis, whether a product is "similar": the product's end-uses in a given market; consumers' tastes and habits, which change from country to country; the product's properties, nature and quality.⁴⁵

This approach was followed in almost all adopted panel reports after *Border Tax Adjustments*.⁴⁶ This approach should be helpful in identifying on a case-by-case basis the range of "like products" that fall within the narrow limits of Article III:2, first sentence in the GATT 1994. Yet this approach will be most helpful if decision makers keep ever in mind how narrow the range of "like products" in Article III:2, first sentence is meant to be as opposed to the range of "like" products contemplated in some other provisions of the GATT 1994 and other Multilateral Trade Agreements of the *WTO Agreement*. In applying the criteria cited in *Border Tax Adjustments* to the facts of any particular case, and in considering other criteria that may also be relevant in certain cases, panels can only apply their best judgement in determining whether in fact products are "like". This will always involve an unavoidable element of individual, discretionary judgement. We do not agree with the Panel's observation in paragraph 6.22 of the Panel Report that distinguishing between "like products" and "directly competitive or substitutable products" under Article III:2 is "an arbitrary decision". Rather, we think it is a discretionary decision that must be made in considering the various characteristics of products in individual cases.

No one approach to exercising judgement will be appropriate for all cases. The criteria in *Border Tax Adjustments* should be examined, but there can be no one precise and absolute definition of what is "like". The concept of "likeness" is a relative one that evokes the image of an accord. The accord of "likeness" stretches and squeezes in different places as different provisions of the *WTO*

If the coverage of Article III:2 is identical to that of Article III:4, a different interpretation of the term "like product" would be called for in the two paragraphs. Otherwise, if the term "like product" were to be interpreted in an identical way in both instances, the scope of the two paragraphs would be different. (emphasis added)

This was merely a hypothetical statement.

⁴⁵Report of the Working Party on *Border Tax Adjustments*, BISD 18S/97, para. 18.

⁴⁶*The Australian Subsidy on Ammonium Sulphate*, BISD IV/188; *EEC - Measures on Animal Feed Proteins*, BISD 25S/49; *Spain - Tariff Treatment of Unroasted Coffee*, BISD 28S/102; *Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83; *United States - Taxes on Petroleum and Certain Imported Substances*, BISD 34S/136. Also see *United States - Standards for Reformulated and Conventional Gasoline*, WT/DS2/9, adopted on 20 May 1996.

Agreement are applied. The width of the accordion in any one of those places must be determined by the particular provision in which the term "like" is encountered as well as by the context and the circumstances that prevail in any given case to which that provision may apply. We believe that, in Article III:2, first sentence of the GATT 1994, the accordion of "likeness" is meant to be narrowly squeezed.

The Panel determined in this case that shochu and vodka are "like products" for the purposes of Article III:2, first sentence. We note that the determination of whether vodka is a "like product" to shochu under Article III:2, first sentence, or a "directly competitive or substitutable product" to shochu under Article III:2, second sentence, does not materially affect the outcome of this case.

A uniform tariff classification of products can be relevant in determining what are "like products". If sufficiently detailed, tariff classification can be a helpful sign of product similarity. Tariff classification has been used as a criterion for determining "like products" in several previous adopted panel reports.⁴⁷ For example, in the 1987 *Japan - Alcohol* Panel Report, the panel examined certain wines and alcoholic

beverages on a "product-by-product basis" by applying the criteria listed in the Working Party Report on *Border Tax Adjustments*,

... as well as others recognized in previous GATT practice (see BISD 25S/49, 63), such as the Customs Cooperation Council Nomenclature (CCCN) for the classification of goods in customs tariffs which has been accepted by Japan.⁴⁸

Uniform classification in tariff nomenclatures based on the Harmonized System (the "HS") was recognized in GATT 1947 practice as providing a useful basis for confirming "likeness" in products. However, there is a major difference between tariff classification nomenclature and tariff bindings or concessions made by Members of the WTO under Article II of the GATT 1994. There are risks in using tariff bindings that are too broad as a measure of product "likeness". Many of the least-developed country Members of the WTO submitted schedules of concessions and commitments as annexes to the GATT 1994 for the first time as required by Article XI of the *WTO Agreement*. Many of these least-developed countries, as well as other developing countries, have bindings in their schedules which include broad ranges of products that cut across several different HS tariff headings. For example, many of these countries have very broad uniform bindings on non-agricultural products.⁴⁹ This does not necessarily indicate similarity of the products covered by a binding. Rather, it represents the results of trade concessions negotiated among Members of the WTO.

It is true that there are numerous tariff bindings which are in fact extremely precise with regard to product description and which, therefore, can provide significant guidance as to the identification of "like products". Clearly enough, these determinations need to be made on a case-by-case basis. However, tariff bindings that include a wide range of products are not a reliable criterion for determining or confirming product "likeness" under Article III:2.⁵⁰

With these modifications to the legal reasoning in the Panel Report, we affirm the legal conclusions and the findings of the Panel with respect to "like products" in all other respects.

⁴⁸*Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83, para. 5.6.

⁴⁹For example, Jamaica has bound tariffs on the majority of non-agricultural products at 50%. Trinidad and Tobago have bound tariffs on the majority of products falling within HS Chapters 25-97 at 50%. Peru has bound all non-agricultural products at 30%, and Costa Rica, El Salvador, Guatemala, Morocco, Paraguay, Uruguay and Venezuela have broad uniform bindings on non-agricultural products, with a few listed exceptions.

⁵⁰We believe, therefore, that statements relating to any relationship between tariff bindings and "likeness" must be made cautiously. For example, the Panel stated in paragraph 6.21 of the Panel Report that "... with respect to two products subject to the same tariff binding and therefore to the same maximum border tax, there is no justification, outside of those mentioned in GATT rules, to tax them in a differentiated way through internal taxation". This is incorrect.

⁴⁷*EEC - Measures on Animal Feed Proteins*, BISD 25S/49; *Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83; *United States - Standards for Reformulated and Conventional Gasoline*, WT/DS2/9, adopted on 20 May 1996.

(b) *"In Excess Of"*

The only remaining issue under Article III:2, first sentence, is whether the taxes on imported products are "in excess of" those on like domestic products. If so, then the Member that has imposed the tax is not in compliance with Article III. Even the smallest amount of "excess" is too much. "The prohibition of discriminatory taxes in Article III:2, first sentence, is not conditional on a 'trade effects test' nor is it qualified by a *de minimis* standard."⁵¹ We agree with the Panel's legal reasoning and with its conclusions on this aspect of the interpretation and application of Article III:2, first sentence.

2. Second Sentence

Article III:1 informs Article III:2, second sentence, through specific reference. Article III:2, second sentence, contains a general prohibition against "internal taxes or other internal charges" applied to "imported or domestic products in a manner contrary to the principles set forth in paragraph 1". As mentioned before, Article III:1 states that internal taxes and other internal charges "should not be applied to imported or domestic products so as to afford protection to domestic production". Again, *Ad Article III:2* states as follows:

A tax conforming to the requirements of the first sentence of paragraph 2 would be considered to be inconsistent with the provisions of the second sentence only in cases where competition was involved between, on the one hand, the taxed product and, on the other hand, a directly competitive or substitutable product which was not similarly taxed.

Article III:2, second sentence, and the accompanying *Ad Article* have equivalent legal status in that both are treaty language which was negotiated and agreed at the same time.⁵² The *Ad Article* does not replace or modify the language contained in Article III:2, second sentence, but, in fact, clarifies its meaning. Accordingly, the language of the second sentence and the *Ad Article* must be read together in order to give them their proper meaning.

Unlike that of Article III:2, first sentence, the language of Article III:2, second sentence, specifically invokes Article III:1. The significance of this distinction lies in the fact that whereas Article III:1 acts implicitly in addressing the two issues that must be considered in applying the first sentence, it acts explicitly as an entirely separate issue that must be addressed along with two other issues that are raised in applying the second sentence. Giving full meaning to the text and to its context, three separate issues must be addressed to determine whether an internal tax measure is inconsistent with Article III:2, second sentence. These three issues are whether:

- (1) the imported products and the domestic products are "*directly competitive or substitutable products*" which are in competition with each other;
- (2) the directly competitive or substitutable imported and domestic products are "*not similarly taxed*"; and
- (3) the dissimilar taxation of the directly competitive or substitutable imported domestic products is "*applied ... so as to afford protection to domestic production*".

Again, these are three separate issues. Each must be established separately by the complainant for a panel to find that a tax measure imposed by a Member of the WTO is inconsistent with Article III:2, second sentence.

⁵²The negotiating history of Article III:2 confirms that the second sentence and the *Ad Article* were added during the Havana Conference, along with other provisions and interpretative notes concerning Article 18 of the draft ITO Charter. When introducing these amendments to delegates, the relevant Sub-Committee reported that: "The new form of the Article makes clearer than did the Geneva text the intention that internal taxes on goods should not be used as a means of protection. The details have been relegated to interpretative notes so that it would be easier for Members to ascertain the precise scope of their obligations under the Article." E/CONF.2/C.3/59, page 8. Article 18 of the draft ITO Charter subsequently became Article III of the GATT pursuant to the Protocol Modifying Part II and Article XXVI, which entered into force on 14 December 1948.

⁵¹*United States - Measures Affecting Alcoholic and Malt Beverages*, BISD 39S/206, para 5.6; see also *Brazilian Internal Taxes*, BISD II/181, para. 16; *United States - Taxes on Petroleum and Certain Imported Substances*, BISD 34S/136, para. 5.1.9; *Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83, para. 5.8.

(a) "Directly Competitive or Substitutable Products"

If imported and domestic products are not "like products" for the narrow purposes of Article III:2, first sentence, then they are not subject to the strictures of that sentence and there is no inconsistency with the requirements of that sentence. However, depending on their nature, and depending on the competitive conditions in the relevant market, those same products may well be among the broader category of "directly competitive or substitutable products" that fall within the domain of Article III:2, second sentence. How much broader that category of "directly competitive or substitutable products" may be in any given case is a matter for the panel to determine based on all the relevant facts in that case. As with "like products" under the first sentence, the determination of the appropriate range of "directly competitive or substitutable products" under the second sentence must be made on a case-by-case basis.

In this case, the Panel emphasized the need to look not only at such matters as physical characteristics, common end-uses, and tariff classifications, but also at the "market place".⁵³ This seems appropriate. The GATT 1994 is a commercial agreement, and the WTO is concerned, after all, with markets. It does not seem inappropriate to look at competition in the relevant markets as one among a number of means of identifying the broader category of products that might be described as "directly competitive or substitutable".

Nor does it seem inappropriate to examine elasticity of substitution as one means of examining those relevant markets. The Panel did not say that cross-price elasticity of demand is "the decisive criterion"⁵⁴ for determining whether products are "directly competitive or substitutable". The Panel stated the following:

In the Panel's view, the decisive criterion in order to determine whether two products are directly competitive or substitutable is whether they have common end-uses, *inter alia*, as shown by elasticity of substitution.⁵⁵

We agree. And, we find the Panel's legal analysis of whether the products are "directly competitive or substitutable products" in paragraphs 6.28-6.32 of the Panel Report to be correct.

We note that the Panel's conclusions on "like products" and on "directly competitive or substitutable products" contained in paragraphs 7.1(i) and (ii), respectively, of the Panel Report fail to

⁵³Panel Report, para. 6.22.

⁵⁴United States Appellant's Submission, dated 23 August 1996, para. 98, p.63. (emphasis added)

⁵⁵Panel Report, para 6.22.

address the full range of alcoholic beverages included in the Panel's Terms of Reference.⁵⁶ More specifically, the Panel's conclusions in paragraph 7.1(ii) on "directly competitive or substitutable products" relate only to "shochu, whisky, brandy, rum, gin, genever, and liqueurs," which is narrower than the range of products referred to the Dispute Settlement Body by one of the complainants, the United States, which included in its request for the establishment of a panel "all other distilled spirits and liqueurs falling within HS heading 2208". We consider this failure to incorporate into its conclusions all the products referred to in the Terms of Reference, consistent with the matters referred to the DSB in WT/DS8/5, WT/DS10/5 and WT/DS11/2, to be an error of law by the Panel.

(b) "Not Similarly Taxed"

To give due meaning to the distinctions in the wording of Article III:2, first sentence, and Article III:2, second sentence, the phrase "not similarly taxed" in the *Ad Article* to the second sentence must not be construed so as to mean the same thing as the phrase "in excess of" in the first sentence. On its face, the phrase "in excess of" in the first sentence means *any* amount of tax on imported products "in excess of" the tax on domestic "like products". The phrase "not similarly taxed" in the *Ad Article* to the second sentence must therefore mean something else. It requires a different standard, just as "directly competitive or substitutable products" requires a different standard as compared to "like products" for these same interpretive purposes.

Reinforcing this conclusion is the need to give due meaning to the distinction between "like products" in the first sentence and "directly competitive or substitutable products" in the *Ad Article* to the second sentence. If "in excess of" in the first sentence and "not similarly taxed" in the *Ad Article* to the second sentence were construed to mean one and the same thing, then "like products" in the first sentence and "directly competitive or substitutable products" in the *Ad Article* to the second sentence would also mean one and the same thing. This would eviscerate the distinctive meaning that must be respected in the words of the text.

To interpret "in excess of" and "not similarly taxed" identically would deny any distinction between the first and second sentences of Article III:2. Thus, in any given case, there may be some amount of taxation on imported products that may well be "in excess of" the tax on domestic "like

⁵⁶The Panel's Terms of Reference cite the matters referred to the Dispute Settlement Body by the European Communities, Canada and the United States in WT/DS8/5, WT/DS10/5 and WT/DS11/2, respectively. In WT/DS8/5, the European Communities referred the Dispute Settlement Body to Japan's taxation of shochu, "spirits", "whisky/brandy", and "liqueurs". In WT/DS10/5, Canada referred the Dispute Settlement Body to Japan's taxation of shochu and products falling "within HS 2208.30 ('whiskies'), HS 2208.40 ('rum and tafia'), HS 2208.90 ('other' including fruit brandies, vodka, ouzo, korn, cream liqueurs and 'classic' liqueurs.)" In WT/DS11/2, the United States referred the Dispute Settlement Body to Japan's taxation of shochu and "all other distilled spirits and liqueurs falling within HS heading 2208".

products" but may not be so much as to compel a conclusion that "directly competitive or substitutable" imported and domestic products are "not similarly taxed" for the purposes of the *Ad* Article to Article III:2, second sentence. In other words, there may be an amount of excess taxation that may well be more of a burden on imported products than on domestic "directly competitive or substitutable products" but may nevertheless not be enough to justify a conclusion that such products are "not similarly taxed" for the purposes of Article III:2, second sentence. We agree with the Panel that this amount of differential taxation must be more than *de minimis* to be deemed "not similarly taxed" in any given case.⁵⁷ And, like the Panel, we believe that whether any particular differential amount of taxation is *de minimis* or is not *de minimis* must, here too, be determined on a case-by-case basis. Thus, to be "not similarly taxed", the tax burden on imported products must be heavier than on "directly competitive or substitutable" domestic products, and that burden must be more than *de minimis* in any given case.

In this case, the Panel applied the correct legal reasoning in determining whether "directly competitive or substitutable" imported and domestic products were "not similarly taxed". However, the Panel erred in blurring the distinction between that issue and the entirely separate issue of whether the tax measure in question was applied "so as to afford protection". Again, these are separate issues that must be addressed individually. If "directly competitive or substitutable products" are *not* "not similarly taxed", then there is neither need nor justification under Article III:2, second sentence, for inquiring further as to whether the tax has been applied "so as to afford protection". But if such products are "not similarly taxed", a further inquiry must necessarily be made.

(c) "*So As To Afford Protection*"

This third inquiry under Article III:2, second sentence, must determine whether "directly competitive or substitutable products" are "not similarly taxed" in a way that affords protection. This is not an issue of intent. It is not necessary for a panel to sort through the many reasons legislators and regulators often have for what they do and weigh the relative significance of those reasons to establish legislative or regulatory intent. If the measure is applied to imported or domestic products so as to afford protection to domestic production, then it does not matter that there may not have been any desire to engage in protectionism in the minds of the legislators or the regulators who imposed the measure. It is irrelevant that protectionism was not an intended objective if the particular tax measure in question is nevertheless, to echo Article III:1, "*applied* to imported or domestic products so as to afford protection to domestic production".⁵⁸ This is an issue of how the measure in question is *applied*.

⁵⁷Panel Report, para. 6.33.

⁵⁸Emphasis added.

In the 1987 *Japan- Alcohol* case, the panel subsumed its discussion of the issue of "not similarly taxed" within its examination of the separate issue of "so as to afford protection":

... whereas under the first sentence of Article III:2 the tax on the imported product and the tax on the like domestic product had to be equal in effect, Article III:1 and 2, second sentence, prohibited only the application of internal taxes to imported or domestic products in a manner "so as to afford protection to domestic production". The Panel was of the view that also small tax differences could influence the competitive relationship between directly competing distilled liquors, but the existence of protective taxation could be established only in the light of the particular circumstances of each case and there could be a *de minimis* level below which a tax difference ceased to have the protective effect prohibited by Article III:2, second sentence.⁵⁹

To detect whether the taxation was protective, the panel in the 1987 case examined a number of factors that it concluded were "sufficient evidence of fiscal distortions of the competitive relationship between imported distilled liquors and domestic shochu affording protection to the domestic production of shochu". These factors included the considerably lower specific tax rates on shochu than on imported directly competitive or substitutable products; the imposition of high *ad valorem* taxes on imported alcoholic beverages and the absence of *ad valorem* taxes on shochu; the fact that shochu was almost exclusively produced in Japan and that the lower taxation of shochu did "afford protection to domestic production"; and the mutual substitutability of these distilled liquors.⁶⁰ The panel in the 1987 case concluded that "the application of considerably lower internal taxes by Japan on shochu than on other directly competitive or substitutable distilled liquors had trade-distorting effects affording protection to domestic production of shochu contrary to Article III:1 and 2, second sentence".⁶¹

As in that case, we believe that an examination in any case of whether dissimilar taxation has been applied so as to afford protection requires a comprehensive and objective analysis of the structure and application of the measure in question on domestic as compared to imported products. We believe

⁵⁹*Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83, para. 5.11.

⁶⁰*Ibid.*

⁶¹*Ibid.*

it is possible to examine objectively the underlying criteria used in a particular tax measure, its structure, and its overall application to ascertain whether it is applied in a way that affords protection to domestic products.

Although it is true that the aim of a measure may not be easily ascertained, nevertheless its protective application can most often be discerned from the design, the architecture, and the revealing structure of a measure. The very magnitude of the dissimilar taxation in a particular case may be evidence of such a protective application, as the Panel rightly concluded in this case. Most often, there will be other factors to be considered as well. In conducting this inquiry, panels should give full consideration to all the relevant facts and all the relevant circumstances in any given case.

In this respect, we note and agree with the panel's acknowledgment in the 1987 *Japan - Alcohol* Report:

... that Article III:2 does not prescribe the use of any specific method or system of taxation. ... there could be objective reasons proper to the tax in question which could justify or necessitate differences in the system of taxation for imported and for domestic products. The Panel found that it could also be compatible with Article III:2 to allow two different methods of calculation of price for tax purposes. Since Article III:2 prohibited only discriminatory or protective tax burdens on imported products, what mattered was, in the view of the Panel, whether the application of the different taxation methods actually had a discriminatory or protective effect against imported products.⁶²

We have reviewed the Panel's reasoning in this case as well as its conclusions on the issue of "so as to afford protection" in paragraphs 6.33 - 6.35 of the Panel Report. We find cause for thorough examination. The Panel began in paragraph 6.33 by describing its approach as follows:

... if directly competitive or substitutable products are not "similarly taxed", and if it were found that the tax favours domestic products, then protection would be afforded to such products, and Article III:2, second sentence, is violated.

This statement of the reasoning required under Article III:2, second sentence is correct.

However, the Panel went on to note:

... for it to conclude that dissimilar taxation afforded protection, it would be sufficient for it to find that the dissimilarity in taxation is not *de minimis*. ... the Panel took the view that "similarly taxed" is the appropriate benchmark in order to determine whether a violation of Article III:2, second sentence, has occurred as opposed to "in excess of" that constitutes the appropriate benchmark to determine whether a violation of Article III:2, first sentence, has occurred.⁶³

In paragraph 6.34, the Panel added:

- (i) The benchmark in Article III:2, second sentence, is whether internal taxes operate "so as to afford protection to domestic production", a term which has been further interpreted in the Interpretative Note ad Article III:2, paragraph 2, to mean dissimilar taxation of domestic and foreign directly competitive or substitutable products.

And, furthermore, in its conclusions, in paragraph 7.1(ii), the Panel concluded that:

- (ii) Shochu, whisky, brandy, rum, gin, genever, and liqueurs are "directly competitive or substitutable products" and Japan, by not taxing them similarly, is in violation of its obligation under Article III:2, second sentence, of the General Agreement on Tariffs and Trade 1994.

Thus, having stated the correct legal approach to apply with respect to Article III:2, second sentence, the Panel then equated dissimilar taxation above a *de minimis* level with the separate and distinct requirement of demonstrating that the tax measure "affords protection to domestic production". As previously stated, a finding that "directly competitive or substitutable products" are "not similarly taxed" is necessary to find a violation of Article III:2, second sentence. Yet this is not enough. The dissimilar taxation must be more than *de minimis*. It may be so much more that it will be clear from that very differential that the dissimilar taxation was applied "so as to afford protection". In some cases, that may be enough to show a violation. In this case, the Panel concluded that it was enough. Yet in other cases, there may be other factors that will be just as relevant or more relevant to demonstrating that the dissimilar taxation at issue was applied "so as to afford protection". In any case, the three issues that must be addressed in determining whether there is such a violation must be addressed clearly and separately in each case and on a case-by-case basis. And, in every case, a careful, objective analysis, must be done of each and all relevant facts and all the relevant circumstances in order to determine "the existence of protective taxation".⁶⁴ Although the Panel blurred its legal reasoning in this respect, nevertheless we conclude that it reasoned correctly that in this case, the Liquor Tax Law is not in compliance with Article III:2. As the Panel did, we note that:

⁶² *Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83, para. 5.9(c).

⁶³ Panel Report, para 6.33.

⁶⁴ *Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83, para. 5.11.

...the combination of customs duties and internal taxation in Japan has the following impact: on the one hand, it makes it difficult for foreign-produced shochu to penetrate the Japanese market and, on the other, it does not guarantee equality of competitive conditions between shochu and the rest of 'white' and 'brown' spirits. Thus, through a combination of high import duties and differentiated internal taxes, Japan manages to "isolate" domestically produced shochu from foreign competition, be it foreign produced shochu or any other of the mentioned white and brown spirits.⁶⁵

Our interpretation of Article III is faithful to the "customary rules of interpretation of public international law".⁶⁶ WTO rules are reliable, comprehensible and enforceable. WTO rules are not so rigid or so inflexible as not to leave room for reasoned judgements in confronting the endless and ever-changing ebb and flow of real facts in the real world. They will serve the multilateral trading system best if they are interpreted with that in mind. In that way, we will achieve the "security and predictability" sought for the multilateral trading system by the Members of the WTO through the establishment of the dispute settlement system.⁶⁷

I. Conclusions and Recommendations

For the reasons set out in the preceding sections of this report, the Appellate Body has reached the following conclusions:

- (a) the Panel erred in law in its conclusion that "panel reports adopted by the GATT CONTRACTING PARTIES and the WTO Dispute Settlement Body constitute subsequent practice in a specific case by virtue of the decision to adopt them";
- (b) the Panel erred in law in failing to take into account Article III:1 in interpreting Article III:2, first and second sentences;
- (c) the Panel erred in law in limiting its conclusions in paragraph 7.1(ii) on "directly competitive or substitutable products" to "shochu, whisky, brandy, rum, gin, genever, and liqueurs", which is not consistent with the Panel's Terms of Reference; and
- (d) the Panel erred in law in failing to examine "so as to afford protection" in Article III:1 as a separate inquiry from "not similarly taxed" in the *Ad Article* to Article III:2, second sentence.

With the modifications to the Panel's legal findings and conclusions set out in this report, the Appellate Body affirms the Panel's conclusions that shochu and vodka are like products and that Japan, by taxing imported products in excess of like domestic products, is in violation of its obligations under Article III:2, first sentence, of the General Agreement on Tariffs and Trade 1994. Moreover, the Appellate Body concludes that shochu and other distilled spirits and liqueurs listed in HS 2208, except for vodka, are "directly competitive or substitutable products", and that Japan, in the application of the Liquor Tax Law, does not similarly tax imported and directly competitive or substitutable domestic products and affords protection to domestic production in violation of Article III:2, second sentence, of the General Agreement on Tariffs and Trade 1994.

The Appellate Body *recommends* that the Dispute Settlement Body request Japan to bring the Liquor Tax Law into conformity with its obligations under the General Agreement on Tariffs and Trade 1994.

⁶⁵ Panel Report, para. 6.35.

⁶⁶ Article 3.2 of the *DSU*.

⁶⁷ *Ibid.*

Signed in the original at Geneva this 25th day of September 1996 by:

Julio Lacarte-Muró
Presiding Member

James Bacchus
Member
Member

Said El-Naggar

World Trade Organization

**United States – Import Prohibition of Certain Shrimp and
Shrimp Products**

Report of the Appellate Body, 12 October 1998

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**UNITED STATES - IMPORT PROHIBITION OF
CERTAIN SHRIMP AND SHRIMP PRODUCTS**

AB-1998-4

Report of the Appellate Body

WORLD TRADE ORGANIZATION
APPELLATE BODY

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United States – Import Prohibition of Certain Shrimp and Shrimp Products

AB-1998-4

Present:

United States, *Appellant*
India, Malaysia, Pakistan, Thailand, *Appellees*

Feliciano, Presiding Member
Bacchus, Member
Lacarte-Muró, Member

Australia, Ecuador, the European Communities, Hong Kong, China, Mexico and Nigeria, *Third Participants*

I. Introduction : Statement of the Appeal

1. This is an appeal by the United States from certain issues of law and legal interpretations in the Panel Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*.¹ Following a joint request for consultations by India, Malaysia, Pakistan and Thailand on 8 October 1996², Malaysia and Thailand requested in a communication dated 9 January 1997³, and Pakistan asked in a communication dated 30 January 1997⁴, that the Dispute Settlement Body (the "DSB") establish a panel to examine their complaint regarding a prohibition imposed by the United States on the importation of certain shrimp and shrimp products by Section 609 of Public Law 101-162⁵ ("Section 609") and associated regulations and judicial rulings. On 25 February 1997, the DSB established two panels in accordance with these requests and agreed that these panels would be consolidated into a single Panel, pursuant to Article 9 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), with standard terms of reference.⁶ On

¹WT/DS58/R, 15 May 1998.

²WT/DS58/1, 14 October 1996.

³WT/DS58/6, 10 January 1997.

⁴WT/DS58/7, 7 February 1997.

⁵16 United States Code (U.S.C.) §1537.

⁶WT/DSB/M/29, 26 March 1997.

10 April 1997, the DSB established another panel with standard terms of reference in accordance with a request made by India in a communication dated 25 February 1997⁷, and agreed that this third panel, too, would be merged into the earlier Panel established on 25 February 1997.⁸ The Report rendered by the consolidated Panel was circulated to the Members of the World Trade Organization (the "WTO") on 15 May 1998.

2. The relevant factual and regulatory aspects of this dispute are set out in the Panel Report, in particular at paragraphs 2.1-2.16. Here, we outline the United States measure at stake before the Panel and in these appellate proceedings. The United States issued regulations in 1987 pursuant to the Endangered Species Act of 1973⁹ requiring all United States shrimp trawl vessels to use approved Turtle Excluder Devices ("TEDs") or tow-time restrictions in specified areas where there was a significant mortality of sea turtles in shrimp harvesting.¹⁰ These regulations, which became fully effective in 1990, were modified so as to require the use of approved TEDs at all times and in all areas where there is a likelihood that shrimp trawling will interact with sea turtles, with certain limited exceptions.

3. Section 609 was enacted on 21 November 1989. Section 609(a) calls upon the United States Secretary of State, in consultation with the Secretary of Commerce, *inter alia*, to "initiate negotiations as soon as possible for the development of bilateral or multilateral agreements with other nations for the protection and conservation of ... sea turtles" and to "initiate negotiations as soon as possible with all foreign governments which are engaged in, or which have persons or companies engaged in, commercial fishing operations which, as determined by the Secretary of Commerce, may affect adversely such species of sea turtles, for the purpose of entering into bilateral and multilateral treaties with such countries to protect such species of sea turtles; ...". Section 609(b)(1) imposed, not later than 1 May 1991, an import ban on shrimp harvested with commercial fishing technology which may adversely affect sea turtles. Section 609(b)(2) provides that the import ban on shrimp will not apply to harvesting nations that are certified. Two kinds of annual certifications are required for harvesting nations, details of which were further elaborated in regulatory guidelines in 1991, 1993

⁷WT/DS58/8, 4 March 1997.

⁸WT/DSB/M/31, 12 May 1997.

⁹Public Law 93-205, 16 U.S.C. 1531 *et. seq.*

¹⁰52 Fed. Reg. 24244, 29 June 1987 (the "1987 Regulations"). Five species of sea turtles fell under the regulations: loggerhead (*Caretta caretta*), Kemp's ridley (*Lepidochelys kempi*), green (*Chelonia mydas*), leatherback (*Dermochelys coriacea*) and hawksbill (*Eretmochelys imbricata*).

and 1996¹¹: First, certification shall be granted to countries with a fishing environment which does not pose a threat of the incidental taking of sea turtles in the course of shrimp harvesting.¹² According to the 1996 Guidelines, the Department of State "shall certify any harvesting nation meeting the following criteria without the need for action on the part of the government of the harvesting nation:

(a) Any harvesting nation without any of the relevant species of sea turtles occurring in waters subject to its jurisdiction; (b) Any harvesting nation that harvests shrimp exclusively by means that do not pose a threat to sea turtles, *e.g.*, any nation that harvests shrimp exclusively by artisanal means; or (c) Any nation whose commercial shrimp trawling operations take place exclusively in waters subject to its jurisdiction in which sea turtles do not occur."¹³

4. Second, certification shall be granted to harvesting nations that provide documentary evidence of the adoption of a regulatory program governing the incidental taking of sea turtles in the course of shrimp trawling that is comparable to the United States program *and* where the average rate of incidental taking of sea turtles by their vessels is comparable to that of United States vessels.¹⁴ According to the 1996 Guidelines, the Department of State assesses the regulatory program of the harvesting nation and certification shall be made if the program includes: (i) the required use of TEDs that are "comparable in effectiveness to those used in the United States. Any exceptions to this requirement must be comparable to those of the United States program ..."; and (ii) "a credible enforcement effort that includes monitoring for compliance and appropriate sanctions."¹⁵ The regulatory program may be in the form of regulations, or may, in certain circumstances, take the form of a voluntary arrangement between industry and government.¹⁶ Other measures that the harvesting nation undertakes for the protection of sea turtles will also be taken into account in making the comparability determination.¹⁷ The average incidental take rate "will be deemed comparable if the harvesting nation requires the use of TEDs in a manner comparable to that of the U.S. program ...".¹⁸

5. The 1996 Guidelines provide that all shrimp imported into the United States must be accompanied by a Shrimp Exporter's Declaration form attesting that the shrimp was harvested either

¹¹Hereinafter referred to as the "1991 Guidelines" (56 Federal Register 1051, 10 January 1991), the "1993 Guidelines" (58 Federal Register 9015, 18 February 1993) and the "1996 Guidelines" (61 Federal Register 17342, 19 April 1996), respectively.

¹²Section 609(b)(2)(C).

¹³1996 Guidelines, p. 17343.

¹⁴Section 609(b)(2)(A) and (B).

¹⁵1996 Guidelines, p. 17344.

¹⁶*Ibid.*

¹⁷*Ibid.*

¹⁸*Ibid.*

in the waters of a nation currently certified under Section 609 or "under conditions that do not adversely affect sea turtles", that is: (a) "Shrimp harvested in an aquaculture facility in which the shrimp spend at least 30 days in ponds prior to being harvested"; (b) "Shrimp harvested by commercial shrimp trawl vessels using TEDs comparable in effectiveness to those required in the United States"; (c) "Shrimp harvested exclusively by means that do not involve the retrieval of fishing nets by mechanical devices or by vessels using gear that, in accordance with the U.S. program ... , would not require TEDs"; and (d) "Species of shrimp, such as the pandalid species, harvested in areas where sea turtles do not occur."¹⁹ On 8 October 1996, the United States Court of International Trade ruled that the 1996 Guidelines were in violation of Section 609 in allowing the import of shrimp from non-certified countries if accompanied by a Shrimp Exporter's Declaration form attesting that they were caught with commercial fishing technology that did not adversely affect sea turtles.²⁰ A 25 November 1996 ruling of the United States Court of International Trade clarified that shrimp harvested by manual methods which did not harm sea turtles could still be imported from non-certified countries.²¹ On 4 June 1998, the United States Court of Appeals for the Federal Circuit vacated the decisions of the United States Court of International Trade of 8 October and 25 November 1996.²² In practice, however, exemption from the import ban for TED-caught shrimp from non-certified countries remained unavailable while this dispute was before the Panel and before us.²³

6. The 1991 Guidelines limited the geographical scope of the import ban imposed by Section 609 to countries in the wider Caribbean/western Atlantic region²⁴, and granted these countries a three-year phase-in period. The 1993 Guidelines maintained this geographical limitation. On 29 December 1995, the United States Court of International Trade held that the 1991 and 1993 Guidelines violated Section 609 by limiting its geographical scope to shrimp harvested in the wider Caribbean/western Atlantic region, and directed the Department of State to extend the ban worldwide not later than 1 May 1996.²⁵ On 10 April 1996, the United States Court of International Trade refused a subsequent request by the Department of State to postpone the 1 May 1996 deadline.²⁶ On

¹⁹1996 Guidelines, p. 17343.

²⁰*Earth Island Institute v. Warren Christopher*, 942 Fed. Supp. 597 (CIT 1996).

²¹*Earth Island Institute v. Warren Christopher*, 948 Fed. Supp. 1062 (CIT 1996).

²²1998 U.S. App. Lexis 11789.

²³Response by the United States to questioning at the oral hearing.

²⁴Specifically, Mexico, Belize, Guatemala, Honduras, Nicaragua, Costa Rica, Panama, Colombia, Venezuela, Trinidad and Tobago, Guyana, Suriname, French Guyana and Brazil.

²⁵*Earth Island Institute v. Warren Christopher*, 913 Fed. Supp. 559 (CIT 1995).

²⁶*Earth Island Institute v. Warren Christopher*, 922 Fed. Supp. 616 (CIT 1996).

19 April 1996, the United States issued the 1996 Guidelines, extending Section 609 to shrimp harvested in *all* foreign countries effective 1 May 1996.

7. In the Panel Report, the Panel reached the following conclusions:

In the light of the findings above, we conclude that the import ban on shrimp and shrimp products as applied by the United States on the basis of Section 609 of Public Law 101-162 is not consistent with Article XI:1 of GATT 1994, and cannot be justified under Article XX of GATT 1994.²⁷

and made this recommendation:

The Panel *recommends* that the Dispute Settlement Body request the United States to bring this measure into conformity with its obligations under the WTO Agreement.²⁸

8. On 13 July 1998, the United States notified the DSB of its decision to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, pursuant to paragraph 4 of Article 16 of the DSU, and filed a notice of appeal²⁹ with the Appellate Body pursuant to Rule 20 of the *Working Procedures for Appellate Review*. On 23 July 1998, the United States filed an appellant's submission.³⁰ On 7 August 1998, India, Pakistan and Thailand ("Joint Appellees") filed a joint appellees' submission and Malaysia filed a separate appellee's submission.³¹ On the same day, Australia, Ecuador, the European Communities, Hong Kong, China, and Nigeria each filed separate third participants' submissions.³² At the invitation of the Appellate Body, the United States, India, Pakistan, Thailand and Malaysia filed additional submissions on certain issues arising under Article XX(b) and Article XX(g) of the GATT 1994 on 17 August 1998. The oral hearing in the appeal was held on 19-20 August 1998. The participants and third participants presented oral arguments and responded to questions put to them by the Members of the Division hearing the appeal.

²⁷Panel Report, para. 8.1.

²⁸Panel Report, para. 8.2.

²⁹WT/DS58/11, 13 July 1998.

³⁰Pursuant to Rule 21(1) of the *Working Procedures for Appellate Review*.

³¹Pursuant to Rule 22(1) of the *Working Procedures for Appellate Review*.

³²Pursuant to Rule 24 of the *Working Procedures for Appellate Review*.

II. Arguments of the Participants and Third Participants

A. Claims of Error by the United States – Appellant

1. Non-requested Information from Non-governmental Organizations

9. The United States claims that the Panel erred in finding that it could not accept non-requested submissions from non-governmental organizations. According to the United States, there is nothing in the DSU that prohibits panels from considering information just because the information was unsolicited. The language of Article 13.2 of the DSU is broadly drafted to provide a panel with discretion in choosing its sources of information. When a non-governmental organization makes a submission to a panel, Article 13.2 of the DSU authorizes the panel to "seek" such information. To find otherwise would unnecessarily limit the discretion that the DSU affords panels in choosing the sources of information to consider.

2. Article XX of the GATT 1994

10. In the view of the United States, the Panel erred in finding that Section 609 was outside the scope of Article XX. The United States stresses that under the Panel's factual findings and undisputed facts on the record, Section 609 is within the scope of the Article XX chapeau and Article XX(g) and, in the alternative, Article XX(b), of the GATT 1994. The Panel was also incorrect in finding that Section 609 constitutes "unjustifiable discrimination between countries where the same conditions prevail". The Panel interprets the chapeau of Article XX as requiring panels to determine whether a measure constitutes a "threat to the multilateral trading system". This interpretation of Article XX has no basis in the text of the GATT 1994, has never been adopted by any previous panel or Appellate Body Report, and would impermissibly diminish the rights that WTO Members reserved under Article XX.

11. The United States contends that the Panel's findings are not based on the ordinary meaning and context of the term "unjustifiable discrimination". That term raises the issue of whether a particular discrimination is "justifiable". During the Panel proceeding, the United States presented the rationale of Section 609 for restricting imports of shrimp from some countries and not from others: sea turtles are threatened with extinction worldwide; most nations, including the appellees, recognize the importance of conserving sea turtles; and shrimp trawling without the use of TEDs contributes greatly to the endangerment of sea turtles. In these circumstances, it is reasonable and justifiable for Section 609 to differentiate between countries whose shrimp industries operate without TEDs, and

thereby endanger sea turtles, and those countries whose shrimp industries do employ TEDs in the course of harvesting shrimp.

12. The Panel, the United States believes, did not address the rationale of the United States for differentiating between shrimp harvesting countries. Rather, the Panel asked a different question: would the United States measure and similar measures taken by other countries "undermine the multilateral trading system"? The distinction between "unjustifiable discrimination" -- the actual term used in the GATT 1994 -- and the Panel's "threat to the multilateral trading system" test is crucial, in the view of the United States, and is posed sharply in paragraph 7.61 of the Panel Report, where the Panel states: "even though the situation of turtles is a serious one, we consider that the United States adopted measures which, irrespective of their environmental purpose, were clearly a threat to the multilateral trading system ...". An environmental purpose is fundamental to the application of Article XX, and such a purpose cannot be ignored, especially since the preamble to the *Marrakesh Agreement Establishing the World Trade Organization*³³ (the "*WTO Agreement*") acknowledges that the rules of trade should be "in accordance with the objective of sustainable development", and should seek to "protect and preserve the environment". Moreover, Article XX neither defines nor mentions the "multilateral trading system", nor conditions a Member's right to adopt a trade-restricting measure on the basis of hypothetical effects on that system.

13. In adopting its "threat to the multilateral trading system" analysis, the Panel fails to apply the ordinary meaning of the text: whether a justification can be presented for applying a measure in a manner which constitutes discrimination. Instead, the Panel expands the ordinary meaning of the text to encompass a much broader and more subjective inquiry. As a result, the Panel would add an entirely new obligation under Article XX of the GATT 1994: namely that Members may not adopt measures that would result in certain effects on the trading system. Under the ordinary meaning of the text, there is sufficient justification for an environmental conservation measure if a conservation purpose justifies a difference in treatment between Members. Further inquiry into effects on the trading system is uncalled for and incorrect.

14. In the view of the United States, the Panel also fails to take account of the context of the term "unjustifiable discrimination". The language of the Article XX chapeau indicates that the chapeau was intended to prevent the abusive application of the exceptions for protectionist or other discriminatory aims. This is consistent with the approach of the Appellate Body in *United States – Standards for Reformulated and Conventional Gasoline*³⁴ ("*United States – Gasoline*") and with the

³³Done at Marrakesh, 15 April 1994.

³⁴Adopted 20 May 1996, WT/DS2/AB/R.

preparatory work of the GATT 1947. In context, an alleged "discrimination between countries where the same conditions prevail" is not "unjustifiable" where the policy goal of the Article XX exception being applied provides a rationale for the justification.

15. In the context of the GATT/WTO dispute settlement system, measures within the scope of Article XX can be expected to result in reduced market access or discriminatory treatment. To interpret the prohibition of "unjustifiable discrimination" in the Article XX chapeau as excluding measures which result in "reduced market access" or "discriminatory treatment" would, in effect, erase Article XX from the GATT 1994. The Panel's "threat to the multilateral trading system" analysis erroneously confuses the question of whether a measure reduces market access with the further and separate question arising under the chapeau as to whether that measure is nevertheless "justifiable" under one of the general exceptions in Article XX. The proper inquiry under the Article XX chapeau is whether a non-protectionist rationale, such as a rationale based on the policy goal of the applicable Article XX exception, could justify any discrimination resulting from the measure. Here, any "discrimination" resulting from the measure is based on, and in support of, the goal of sea turtle conservation.

16. The United States also argues that the Panel incorrectly applies the object and purpose of the *WTO Agreement* in interpreting Article XX of the GATT 1994. It is legal error to jump from the observation that the GATT 1994 is a trade agreement to the conclusion that trade concerns must prevail over all other concerns in all situations arising under GATT rules. The very language of Article XX indicates that the state interests protected in that article are, in a sense, "pre-eminent" to the GATT's goals of promoting market access.

17. Furthermore, the Panel failed to recognize that most treaties have no single, undiluted object and purpose but rather a variety of different, and possibly conflicting, objects and purposes. This is certainly true of the *WTO Agreement*. Thus, while the first clause of the preamble to the *WTO Agreement* calls for the expansion of trade in goods and services, this same clause also recognizes that international trade and economic relations under the *WTO Agreement* should allow for "optimal use of the world's resources in accordance with the objective of sustainable development", and should seek "to protect and preserve the environment". The Panel in effect took a one-sided view of the object and purpose of the *WTO Agreement* when it fashioned a new test not found in the text of the Agreement.

18. The additional bases, the United States continues, invoked by the Panel to support its "threat to the multilateral trading system" analysis -- i.e. the protection of expectations of Members as to the competitive relationship between their products and the products of other Members; the application

of the international law principle according to which international agreements must be applied in good faith; and the *Belgian Family Allowances*³⁵ panel report -- are without merit.

19. The United States submits that Section 609 does not threaten the multilateral trading system. The Panel did not find Section 609 to be an *actual* threat to the multilateral trading system. Rather, the Panel found that if other countries in other circumstances were to adopt the same type of measure here adopted by the United States *potentially* a threat to the system might arise. The United States urges that in engaging in hypothetical speculations regarding the effects of other measures which might be adopted in differing situations, while ignoring the compelling circumstances of this case, the Panel violated the Appellate Body's prescription in *United States - Gasoline*³⁶ that Article XX must be applied on a "case-by-case basis", with careful scrutiny of the specific facts of the case at hand. The Panel's "threat to the multilateral trading system" analysis adds a new obligation under Article XX of the GATT 1994 and is inconsistent with the proper role of the Panel under the DSU, in particular Articles 3.2 and 19.2 thereof.

20. To the United States, Section 609 reasonably differentiates between countries on the basis of the risk posed to endangered sea turtles by their shrimp trawling industries. Considering the aim of the Article XX chapeau to prevent abuse of the Article XX exceptions, an evaluation of whether a measure constitutes "unjustifiable discrimination where the same conditions prevail" should take account of whether the differing treatment between countries relates to the policy goal of the applicable Article XX exception. If a measure differentiates between countries on a basis "legitimately connected" with the policy of an Article XX exception, rather than for protectionist reasons, that measure does not amount to an abuse of the applicable Article XX exception.

21. The contention of the United States is that its measure does not treat differently those countries whose shrimp trawling industries pose similar risks to sea turtles. Only nations with shrimp trawling industries that harvest shrimp in waters where there is a likelihood of intercepting sea turtles, and that employ mechanical equipment which harms sea turtles, are subject to the import restrictions. The Panel properly recognized that certain naturally-occurring conditions relating to sea turtle conservation (namely, whether sea turtles and shrimp occur concurrently in a Member's waters) and at least certain conditions relating to how shrimp are caught (namely, whether shrimp nets are retrieved mechanically or by hand) are relevant factors in applying the Article XX chapeau. However, the Panel found that another condition relating to how shrimp are caught -- namely, whether a country requires its shrimp fishermen to use TEDs -- did not provide a basis under the chapeau for

³⁵ Adopted 7 November 1952, BISD 1S/59.

³⁶ Adopted 20 May 1996, WT/DS2/AB/R.

treating countries differently. Differing treatment based on whether a country had adopted a TEDs requirement was, in the Panel's view, "unjustifiable".

22. The United States believes that the analysis employed by the Appellate Body in *United States - Gasoline*³⁷ leads to the conclusion that Section 609 does not constitute "unjustifiable discrimination". Section 609 is applied narrowly and fairly. The United States does not apply sea turtle conservation rules differently to United States and foreign shrimp fishermen. Moreover, the United States has taken steps to assist foreign shrimp fishermen in adopting conservation measures and has undertaken efforts to transfer TED technology to governments and industries in other countries, including the appellees. In addition, Section 609 is limited in coverage and focuses on sea turtle conservation.

23. During the Panel proceeding, the United States presented "compelling evidence", reaffirmed by five independent experts, that Section 609 was a *bona fide* conservation measure under Article XX, imbued with the purpose of conserving a species facing the threat of extinction. To uphold the findings of the Panel would impermissibly change the basic terms of the bargain agreed to by WTO Members in agreeing to the GATT 1994. Further, to condone the Panel's adoption of a vague and subjective "threat to the multilateral trading system" test would fundamentally alter the intended role of panels under the DSU, and could call into question the legitimacy of the WTO dispute settlement process.

24. The United States states that neither it nor the appellees have appealed the decisions of the Panel to address first the Article XX chapeau and not to reach the issues regarding Article XX(b) and Article XX(g). Because the Panel made no findings regarding the applicability of Article XX(b) and XX(g), there are no findings in respect thereof that could even be the subject of appeal. Accordingly, issues regarding the applicability of Article XX(b) and Article XX(g) are not initially presented to the Appellate Body. However, the United States concurs with Joint Appellees that the Appellate Body may address Article XX(b) or Article XX(g) if it finds that Section 609 meets the criteria of the Article XX chapeau. In that case, the United States asserts that Article XX(g) should be applied first as it is the "most pertinent" of the Article XX exceptions, and that issues relating to Article XX(b) need be reached only if Article XX(g) were found to be inapplicable. The United States incorporates by reference and briefly summarizes the submissions that it made to the Panel regarding Article XX(b) and Article XX(g).

³⁷Adopted 20 May 1996, WT/DS2/AB/R.

25. The essential claim of the United States is that Section 609 meets each element required under Article XX(g). Sea turtles are important natural resources. They are also an exhaustible natural resource since all species of sea turtles, including those found in the appellees' waters, face the danger of extinction. All species of sea turtles have been included in Appendix I of the Convention on International Trade in Endangered Species of Wild Flora and Fauna³⁸ (the "CITES") since 1975, and other international agreements also recognize the endangered status of sea turtles.³⁹ In paragraph 7.58 of the Panel Report, the Panel noted: "The endangered nature of the species of sea turtles mentioned in [CITES] Annex I as well as the need to protect them are consequently not contested by the parties to the dispute."

26. The United States maintains Section 609 "relates to" the conservation of sea turtles. A "substantial relationship" exists between Section 609 and the conservation of sea turtles. Shrimp trawl nets are a major cause of human-induced sea turtle deaths, and TEDs are highly effective in preventing such mortality. The Panel noted that "TEDs, when properly installed and used and adapted to the local area, would be an effective tool for the preservation of sea turtles."⁴⁰ By encouraging the use of TEDs, Section 609 promotes sea turtle conservation.

27. The United States contends that Section 609 is also "made effective in conjunction with restrictions on domestic production or consumption" within the meaning of Article XX(g). The United States requires its shrimp trawl vessels that operate in waters where there is a likelihood of intercepting sea turtles to use TEDs at all times, and Section 609 applies comparable standards to imported shrimp. Section 609 is also "even-handed": it allows any nation to be certified -- and thus avoid any restriction on shrimp exports to the United States -- if it meets criteria for sea turtle conservation in the course of shrimp harvesting that are comparable to criteria applicable in the United States. With respect to nations whose shrimp trawl vessels operate in waters where there is a likelihood of intercepting sea turtles, Section 609 provides for certification where those nations adopt TEDs-use requirements comparable to those in effect in the United States.

28. The United States submits, moreover, that Section 609 is a measure "necessary to protect human, animal or plant life or health" within the meaning of Article XX(b). Section 609 is intended

³⁸Done at Washington, 3 March 1973, 993 U.N.T.S. 243, 12 International Legal Materials 1085.

³⁹The United States states that all species of sea turtle except the flatback are listed in Appendices I and II of the Convention on the Conservation of Migratory Species of Wild Animals, done at Bonn, 23 June 1979, 19 International Legal Materials 15; and in Appendix II of the Protocol concerning Specially Protected Areas and Wildlife to the Convention for the Protection and Development of the Marine Environment of the Wider Caribbean Region, 29 March 1983, T.I.A.S. No. 11085.

⁴⁰The United States refers to Panel Report, para. 7.60, footnote 674.

to protect and conserve the life and health of sea turtles, by requiring that shrimp imported into the United States shall not have been harvested in a manner harmful to sea turtles. Section 609 is "necessary" in two different senses. First, efforts to reduce sea turtle mortality are "necessary" because all species of sea turtles are threatened with extinction. Second, Section 609 relating to the use of TEDs is "necessary" because other measures to protect sea turtles are not sufficient to allow sea turtles to move back from the brink of extinction.

B. *India, Pakistan and Thailand – Joint Appellees*

I. Non-requested Information from Non-governmental Organizations

29. Joint Appellees submit that the Panel's ruling rejecting non-requested information is correct and should be upheld. According to Joint Appellees, the United States misinterprets Article 13 of the DSU in arguing that nothing in the DSU prohibits panels from considering information merely because the information was unsolicited. The Panel correctly noted that, "pursuant to Article 13 of the DSU, the initiative to seek information and to select the source of information rests with the Panel."⁴¹ It is evident from Article 13 that Members have chosen to establish a formalized system for the collection of information, which gives a panel discretion to determine the information it needs to resolve a dispute. Panels have no obligation to consider unsolicited information, and the United States is wrong to argue that they do.

30. According to Joint Appellees, when a panel does seek information from an individual or body within a Member's jurisdiction, that panel has an obligation to inform the authorities of that Member. This demonstrates that a panel retains control over the information sought, and also that the panel is required to keep the Members informed of its activities. The process accepted by the Members necessarily implies three steps: a panel's decision to seek technical advice; the notification to a Member that such advice is being sought within its jurisdiction; and the consideration of the requested advice. In the view of Joint Appellees, the interpretation offered by the United States would eliminate the first two of these three steps, thereby depriving a panel of its right to decide whether it needs supplemental information, and what type of information it should seek; as well as depriving Members of their right to know that information is being sought from within their jurisdiction.

31. Joint Appellees point to Appendix 3 of the DSU, which sets out Working Procedures for panels, and especially paragraphs 4 and 6 thereof, which limit the right to present panels with written submissions to parties and third parties. Thus, Joint Appellees argue, Members that are not parties or third parties cannot avail themselves of the right to present written submissions. It would be unreasonable, in the view of Joint Appellees, to interpret the DSU as granting the right to submit an unsolicited written submission to a non-Member, when many Members do not enjoy a similar right.

32. Joint Appellees maintain that, if carried to its logical conclusion, the appellant's argument could result in panels being deluged with unsolicited information from around the world. Such information might be strongly biased, if nationals from Members involved in a dispute could provide unsolicited information. They argue that this would not improve the dispute settlement mechanism, and would only increase the administrative tasks of the already overburdened Secretariat.

33. Joint Appellees argue as well that parties to a panel proceeding might feel obliged to respond to all unsolicited submissions -- just in case one of the unsolicited submissions catches the attention of a panel member. Due process requires that a party know what submissions a panel intends to consider, and that all parties be given an opportunity to respond to all submissions. Finally, because Article 12.6 of the DSU requires that second written submissions of the parties be submitted simultaneously, if a party is permitted to append *amicus curiae* briefs to its second submission, other parties can be deprived of their right to respond and be heard.

2. Article XX of the GATT 1994

34. Joint Appellees maintain that the Panel's ruling on the chapeau of Article XX is correct and should be upheld by the Appellate Body. They underline that the appellant does not appeal either the Panel's conclusion that Section 609 violated Article XI:1 of the GATT 1994, or the Panel's decision to address the chapeau of Article XX before addressing sub-paragraph (b) or (g) of that Article. Nor does the United States dispute that it bears the burden of proving that its measure is within Article XX. The United States takes issue with the Panel's alleged application of the chapeau to protect against a "threat to the multilateral trading system", submitting that the Panel developed a new chapeau "interpretation", "analysis" or "test" to invalidate Section 609, thus impermissibly diminishing the rights of WTO Members. According to Joint Appellees, the appellant's argument is baseless and results from a mischaracterization of the Panel's decision. The Panel did not invent a new "interpretation", "analysis" or "test", nor did it simply interpret "unjustifiable" to mean "a threat to the multilateral trading system". Instead, the Panel rendered a well-reasoned decision fully

⁴¹Joint Appellees refer to Panel Report, para. 7.8.

supported by the *WTO Agreement*, past GATT/WTO practice, and the accepted rules of interpretation set forth in the Vienna Convention on the Law of Treaties⁴² (the "Vienna Convention").

35. Joint Appellees argue that the flaw in Section 609, and in the appellant's argument, is the appellant's failure to accept that conditioning access to markets for a given product upon the adoption of certain policies by exporting Members, can violate the *WTO Agreement*. A Member must seek multilateral solutions to trade-related environmental problems. The threat to the multilateral trade system cited by the Panel is unrelated to the appellant's support for TEDs or turtle conservation. The threat is much simpler: the United States has abused Article XX by unilaterally developing a trade policy, and unilaterally imposing this policy through a trade embargo, as opposed to proceeding down the multilateral path. The multilateral trade system is based on multilateral cooperation. If every WTO Member were free to pursue its own trade policy solutions to what it perceives to be environmental concerns, the multilateral trade system would cease to exist. By preventing the abuse of Article XX, the chapeau protects against threats to the multilateral trading system. The prevention of abuse and the prevention of threats to the multilateral trading system are therefore inextricably linked to the object, purpose and goals of Article XX of the GATT 1994.

36. Joint Appellees submit that on the basis of its interpretation of the term "unjustifiable" in the chapeau and in light of the object and purpose of Article XX of the GATT 1994 and the object and purpose of the *WTO Agreement*, the Panel concluded that the chapeau of Article XX permits Members to derogate from GATT provisions, but prohibits derogations which would constitute abuse of the exceptions contained in Article XX, thereby undermining the WTO multilateral trading system. According to Joint Appellees, what the appellant claims to be a new "test" for justifiability is nothing more than a restatement of the principle that the chapeau's object and purpose is to prevent the abuse of the Article XX exceptions, specifying more clearly what may result from such abuse. In the light of recent and past GATT/WTO practice, in particular the panel report in *United States – Restrictions on Imports of Tuna*⁴³, the Panel correctly interpreted the chapeau, identifying its object and purpose as the prevention of abuse of the Article XX exceptions, and associating the prevention of such abuse with the preservation of the multilateral trading system.

⁴²Done at Vienna, 23 May 1969, 1155 U.N.T.S. 33; 8 International Legal Materials 679.

⁴³Unadopted, DS29/R, 16 June 1994, para 5.26.

37. In the view of Joint Appellees, the Panel's decision mirrors the Appellate Body's reasoning in *United States – Gasoline*⁴⁴ and is therefore correct. The Appellate Body made three pronouncements in *United States – Gasoline* that influenced the Panel's ruling: first, that the chapeau, by its express terms, addresses, not so much the questioned measure or its specific contents as such, but rather the manner in which the measure is applied⁴⁵; second, that it is, accordingly, important to underscore that the purpose and object of the introductory clauses of Article XX is generally the prevention of abuse of the exceptions of Article XX⁴⁶; and, third, that the Appellate Body cautioned against the application of Article XX exceptions so as to "frustrate or defeat" legal obligations of the holder of rights under the GATT 1994.⁴⁷

38. Joint Appellees state that, in examining Section 609, the Panel paid particular attention to the manner in which the embargo is applied, and the Panel noted that the appellant conditioned market access on the adoption by exporting Members of conservation policies comparable to its own. The Panel also found that the United States did not enter into negotiations before it imposed its import ban. The Panel concluded that Section 609 abused Article XX and posed a threat to the multilateral trading system. The Panel equated the prevention of the abuse of Article XX with the avoidance of measures that would "frustrate or defeat the purposes and objects of the General Agreement and the WTO Agreement or its legal obligations under the substantive rules of GATT by abusing the exception contained in Article XX."⁴⁸ The Panel buttressed its conclusion by referring to the related principles of good faith and *pacta sunt servanda*, and by citing the *Belgian Family Allowances*⁴⁹ panel report.

39. Should the Appellate Body decide to reverse the Panel's findings with respect to the chapeau of Article XX, Joint Appellees request that the Appellate Body rule that Section 609 is "applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade" in violation of the chapeau of Article XX. Consistently with its decision in *United States – Gasoline*⁵⁰, the Appellate Body should examine the manner in which Section 609 has been applied, and decide whether an

⁴⁴Adopted 20 May 1996, WT/DS2/AB/R.

⁴⁵*United States – Gasoline*, adopted 20 May 1996, WT/DS2/AB/R, page 22.

⁴⁶*Ibid.*

⁴⁷*Ibid.*

⁴⁸Joint Appellees refer to Panel Report, para 7.40.

⁴⁹Adopted 7 November 1952, BISD 1S/59.

⁵⁰Adopted 20 May 1996, WT/DS2/AB/R.

Article XX exception is being abused so as to frustrate or defeat the substantive rights of the appellees under the GATT 1994.

40. Joint Appellees submit that, even leaving aside the "threat to the multilateral trading system" language of the Panel, there is "compelling evidence" in the record that the appellant abused Article XX and its exceptions. Joint Appellees maintain that this abuse takes several forms, each instance "grave", and, by itself, adequate to support a finding that Section 609 has been applied in an abusive manner so as to frustrate the substantive rights of the appellees under the *WTO Agreement*.

41. First, Section 609 was applied without a serious attempt to reach a cooperative multilateral solution with Joint Appellees. The importance of multilateralism should be clear to the United States because it is an integral provision of Section 609, has been emphasised at numerous GATT and WTO meetings, is reflected in Article 23.1 of the DSU and in Principle 12 of the Rio Declaration on Environment and Development⁵¹, and was underscored by the Appellate Body in *United States - Gasoline*.⁵² The chapeau violation that the United States committed in *United States - Gasoline* is, Joint Appellees believe, the same violation committed by the United States in this dispute.

42. Second, the United States discriminated impermissibly among exporting countries, and between exporting countries and the United States in, *inter alia*, the following ways: (a) "[t]he Panel found that the Appellant negotiated an agreement to protect and conserve sea turtles with some WTO Members, but did not propose the negotiation of such an agreement with the ... Appellees until after having concluded its negotiations with the other Members. The Panel also found that Section 609 was already in effect against the Appellees by the time such negotiations were proposed"; (b) "[p]hase-in periods for the use of TEDs differed depending on the countries involved. 'Initially affected countries' had a three year phase-in period, while 'newly affected nations' were given four months or less to change shrimp harvesting practices"; and (c) Section 609 "discriminates between products based on non-product-related processes and production methods."

43. Third, Joint Appellees contend that the appellant's argument misconstrues key portions of the chapeau and of the Panel Report. The appellant's starting-point is that the Panel's findings are not based on the ordinary meaning of the phrase "unjustifiable discrimination" in the context in which it appears. The appellant also suggests that the only object and purpose of the chapeau is the prevention of "indirect protection". This interpretation is contradicted by recent WTO practice. The Appellate

Body Report in *United States - Gasoline*⁵³ stands for the proposition that "unjustifiable discrimination" has a meaning larger than "indirect protection". The appellant, in effect, suggests that justifiability should be determined by reference to the specific Article XX exception invoked. If discrimination were to be justified merely on the basis of the policy goals of the particular exception invoked, all trade measures that meet the requirements of an Article XX exception would, *ipso facto*, satisfy the requirements of the chapeau. The chapeau would be rendered meaningless -- in violation of the commonly accepted rule of treaty interpretation which requires that meaning and effect be given to all treaty terms. The principles enunciated in the Appellate Body Report in *United States - Gasoline* would also become null.

44. Joint Appellees argue that both the Appellate Body in *United States - Gasoline*⁵⁴ and the Panel in the present case, recognized that the Article XX chapeau must be interpreted in light of the object and purpose of the *WTO Agreement*. This does not mean re-incorporating substantive GATT provisions into the analysis through the chapeau; it means instead examining a proposed Article XX derogation from the perspective of the broader policy goals of the *WTO Agreement*. The Panel identified two such goals: endeavouring to find cooperative solutions to trade problems; and preventing the risk that a multiplicity of conflicting trade requirements, each justified by reference to Article XX, could emerge. Section 609 jeopardizes both goals and poses a threat to the multilateral trading system.

45. Should the Appellate Body decide to reverse the Panel's legal findings with respect to the chapeau of Article XX and rule that Section 609 meets the requirements of the chapeau, Joint Appellees request that the Appellate Body make legal findings on Article XX(b) and Article XX(g) of the GATT 1994. They incorporate by reference their submissions to the Panel with respect to the interpretation of Article XX(b) and Article XX(g), while noting at the same time that there are persuasive reasons for following the interpretative approach adopted by the Panel in examining the chapeau first. Not only does the concept of judicial economy favour such an analysis, but also none of the participants has questioned the Panel's interpretative approach in their submissions (although, Joint Appellees note, one third participant, Australia, did comment with disapproval on this approach).

⁵¹UN Doc. A/CONF. 151/5/Rev.1, 13 June 1992, 31 International Legal Materials 874.

⁵²Adopted 20 May 1996, WT/DS2/AB/R, pp. 27-28.

⁵³Adopted 20 May 1996, WT/DS2/AB/R.

⁵⁴*Ibid.*

C. *Malaysia - Appellee*

1. Non-requested Information from Non-governmental Organizations

46. Malaysia submits that the Panel ruled correctly on this issue and that its ruling should be upheld as there is nothing in the DSU that *permits* the admission of unsolicited briefs from non-governmental organizations. Malaysia does not agree with the United States that there is nothing in the DSU *prohibiting* panels from considering information just because the information was offered unsolicited. Under Article 13 of the DSU, the prerequisite for invocation of that provision is that a panel must "seek" information. In the view of Malaysia, the Panel correctly noted that the initiative to seek information and to select the source of information rests with the Panel. The Panel could not consider unsolicited information. In the alternative, should the Appellate Body accept the United States argument that panels may accept *amicus curia* briefs, it must be left to the complete discretion of panel members whether or not to read them. A panel's decision not to read the briefs cannot constitute a procedural mistake and cannot influence the outcome of a panel report.

2. Article XX of the GATT 1994

47. Malaysia maintains that the Panel's decision concerning Article XX of the GATT 1994 represents a balanced view of the requirements of the provisions of the *WTO Agreement*, rules of treaty interpretation and GATT practice. The appellant misconceives the Panel's findings: the Panel did not in any way allude to the supremacy of trade concerns over non-trade concerns, and did not fail to recognize that most treaties have no single, undiluted object and purpose but a variety of different objects and purposes. The Panel in fact alluded to the first, second and third paragraphs of the preamble to the *WTO Agreement*, which make reference to different objects and purposes. Moreover, in Malaysia's view, the appellant misapplies the principle in *India - Patent Protection for Pharmaceutical and Agricultural Chemical Products*⁵⁵ to the facts of this case, and misconstrues the Panel's application of the *Belgian Family Allowances*⁵⁶ panel report.

48. To Malaysia, the Panel's "threat to the multilateral trading system" analysis does not constitute a new test, but is in fact a restatement of the approach taken by the Panel that Members are not allowed to resort to measures that would undermine the multilateral trading system and thus abuse the exceptions contained in Article XX. The Panel itself states that its findings are the result of the

application of the interpretative methods required by Article 3.2 of the DSU and that its process of interpretation does not add to Members' obligations in contravention of Article 3.2 of the DSU.

49. It was also noted by Malaysia that the Panel found on the facts that the import ban is applied even on TED-caught shrimp, as long as the country has not been certified; certification is only granted if comprehensive requirements regarding the use of TEDs by fishing vessels are applied by the exporting country concerned or if shrimp trawling operations of the exporting country take place exclusively in waters in which sea turtles do not occur. On the basis of these findings, the Panel concluded that the United States measure constitutes unjustifiable discrimination between countries where the same conditions prevail.

50. Malaysia believes that the Panel relied in large measure on the Appellate Body Report in *United States - Gasoline*.⁵⁷ Although the requirement of use of TEDs is applied to both United States and foreign shrimp trawlers, Malaysia contends that Section 609 violates the chapeau prohibition of "unjustifiable discrimination between countries where the same conditions prevail": not all species of sea turtles covered by Section 609 and found in Malaysia and the United States are alike -- Kemp's ridley and loggerhead turtles, which occur in the United States, are absent or occur only in negligible numbers in Malaysian waters; the habitats of these turtles do not coincide with areas of shrimp trawling operations in Malaysia; certain countries which have been exempted from TED requirements are harvesting sea turtles commercially and exploiting the eggs; and the time given to countries to comply with the requirements of Section 609 varied.

51. In response to the appellant's statement that it has taken steps to assist foreign shrimp fishermen in adopting turtle conservation measures, Malaysia states that there has been no transfer of TEDs technology to the government and industries in Malaysia, apart from participation by Malaysia in one regional workshop.

52. Malaysia's submissions on legal issues arising under Article XX(b) and Article XX(g) have been addressed by the Panel, at paragraphs 3.213, 3.218-3.221, 3.231, 3.233, 3.236, 3.240, 3.247, 3.257, 3.266, 3.271-3.275, 3.286-3.288 and 3.293 of the Panel Report.

⁵⁵ Adopted 16 January 1998, WT/DS50/AB/R.

⁵⁶ Adopted 7 November 1952, BISD 1S/59.

⁵⁷ Adopted 20 May 1996, WT/DS2/AB/R.

D. *Arguments of Third Participants*

I. Australia

53. Australia states that with respect to unsolicited submissions to the Panel by non-governmental organizations, the United States appears to suggest that the Panel's legal interpretation of the provisions of the DSU would limit the discretion the DSU affords to panels in choosing the sources of information they should consider. However, in the view of Australia, nothing in the Panel Report suggests that the Panel saw any legal obstacles to its requesting information from the non-governmental sources, if it had so wished. The decision of the Panel not to seek such information would appear to reflect the exercise of its discretion as provided by the DSU, and was not the result of any perceived legal obstacles. Australia notes that the United States has not claimed that the Panel's exercise of its discretion in this matter was inappropriate or involved an error in law.

54. Australia believes that the Panel correctly found that Section 609 constitutes "unjustifiable discrimination between countries where the same conditions prevail". However, Australia supports the appeal by the United States of the Panel's finding that Section 609 "is not within the scope of measures permitted under the chapeau of Article XX." Australia submits that the Appellate Body should complete the analysis under Article XX and find that the United States has not demonstrated that its measure is in conformity with Article XX, including the provisions of the chapeau. Australia's concerns are that the United States has sought to impose a unilaterally determined conservation measure through restrictions on trade, and has not explored the scope for working cooperatively with other countries to identify internationally shared concerns about sea turtle conservation issues and consider ways to address these concerns. Therefore, the United States has imposed Section 609 in a manner that constitutes unjustifiable discrimination between countries where the same conditions prevail and also a disguised restriction on international trade.

55. Australia agrees with the United States that the Panel failed to interpret the terms of the chapeau of Article XX requiring that measures not be applied in a manner which would constitute "a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail" in accordance with customary rules of interpretation of public international law, in particular, with its ordinary meaning and in context.

56. In Australia's view, the Panel's decision to examine first whether Section 609 met the requirements of the chapeau before considering whether it met the requirements of any of the paragraphs of Article XX may not necessarily have been an error in law, but contributed to the Panel's errors in its examination of Section 609 under Article XX. Australia argues that it is preferable to

begin examination of the legal issues raised by Article XX by considering the policy objective of the measure, and the connection between the policy objective and the measure, before turning to the chapeau. This approach would enable the examination of all aspects of the case that may be relevant in determining whether a particular measure meets the requirements of the chapeau. There is nothing in the wording of Article XX, read in its context and in the light of the object and purposes of the GATT 1994 and the *WTO Agreement*, to suggest that it is intended to exclude particular classes or types of measures from its coverage. The Panel erred in law in conducting this generalized inquiry. By its terms, Article XX would seem capable of application only on a case-by-case basis.

57. Article XX contains a series of tests designed to ensure that its provisions cannot be abused. There must be a presumption that a measure which meets the requirements of Article XX will not "undermine the WTO multilateral trading system." According to Australia, there is no textual basis for interpreting "unjustifiable discrimination" in such a broad manner that it becomes an independent test of this issue. Under the Panel's interpretation, the chapeau of Article XX could serve to nullify the effects of the paragraphs of that Article, rather than acting as a safeguard against their abuse.

58. Australia agrees with the United States that the Panel's interpretation of "unjustifiable discrimination" is based on an incorrect interpretation and application of the object and purpose of the *WTO Agreement* in construing the GATT 1994. The Panel has projected a view of the relationship between the objectives of the WTO multilateral trading system and environmental considerations which is at odds with the Ministerial Decision on Trade and Environment.⁵⁸

59. At the same time, to Australia, the alternative interpretation of "unjustifiable discrimination" put forward by the United States -- i.e. that discrimination is not "unjustifiable" where the policy goal of the Article XX exemption being applied provides a rationale for the justification -- is in error. This interpretation would weaken the important safeguard represented by the chapeau of Article XX of avoiding the abuse or illegitimate use of the Article XX exceptions. This interpretation confuses the tests applied under the two tiers of Article XX, fails to give effect to all the terms of the treaty and is not based on the ordinary meaning of "unjustifiable discrimination" in its context and in the light of the object and purpose of the *WTO Agreement* and the GATT 1994.

60. Australia maintains that Section 609 is applied by the United States in a manner constituting an unjustifiable discrimination and a disguised restriction on international trade. Australia observes that the only justification the United States appears to offer for Section 609 is that it is required to

⁵⁸ Adopted by Ministers at the Meeting of the Trade Negotiations Committee at Marrakesh, 14 April 1994.

enforce a unilaterally determined conservation measure. However, Australia argues that the United States has not demonstrated that it has adequately explored means of addressing its concerns about shrimp harvesting practices and turtle conservation in other countries through cooperation with the governments concerned.

61. It is the view of Australia that Section 609 does not reasonably and properly differentiate between countries based on the risks posed to sea turtles in the exporting country's shrimp fishery. The Panel focused on exports of wild shrimp, and it is misleading to suggest that the Panel drew conclusions about whether the same conditions prevailed in certain other circumstances with respect to shrimp not subject to the import prohibition. Furthermore, the United States has provided no evidence that it took into account the views of other countries about sea turtle conservation issues within their jurisdictions, or their respective national programs, in making its determination of "countries where the same conditions prevail". In particular, the United States has provided no evidence that it considered the possibility that other Members may have had sea turtle conservation programs in place which differed from that of the United States but which were comparable and appropriate for their circumstances. Australia argues that the United States refused to certify Australia under Section 609 even though Australia's sea turtle conservation regime "extends well beyond protecting turtles from shrimping nets and ... includes cooperative programs with the shrimp industry to limit turtle bycatch."

62. In Australia's view, the legal obligations of the United States under the chapeau of Article XX required the United States to explore adequately means of mitigating the discriminatory and trade restrictive application of its measure. In particular, given the transboundary and global character of the environmental concern involved in this dispute, the United States should have consulted with affected Members to see whether the discrimination imposed by the measure in dispute could have been avoided, whether the restrictions on trade were required, whether alternative approaches were available, and whether the incidence of any trade measures could have been reduced.

2. Ecuador

63. Ecuador endorses the Panel's finding that Section 609 is inconsistent with Article XI:1 of the GATT 1994 and cannot be justified under Article XX of the GATT 1994. Ecuador is participating as a third party in this case in order to defend basic principles, such as the principle reaffirming that relations among states should be established on the basis of international law -- since it is unacceptable that one state impose its domestic policy objectives upon other states -- as well as the observance of more specific principles and aspects set forth in the agreements governing the

multilateral trading system. These include non-discrimination in national treatment, the protection of the environment and the implementation of environmental policy.

64. According to Ecuador, this dispute does not concern the desirability of implementing some kind of conservation policy, to which Ecuador attaches the utmost importance, but rather the manner in which such a policy should be implemented. It is unacceptable that internal legislation is applied in an arbitrary manner, creating a high degree of uncertainty, and consequently prejudice, in a sector that is central to Ecuador's national economy. Ecuador endorses the Panels' view that Members are free to establish their own environmental policies in a manner consistent with their WTO obligations.

3. European Communities

65. With respect to unsolicited submissions to a panel by non-governmental organizations, the European Communities asserts that Article 13 of the DSU clearly gives a panel the "pro-active discretion" to "seek" certain information that the panel believes may be relevant to the case at hand. In addition, non-governmental organizations are free to publish their views so that their opinion is heard by the general public, which could include the parties to a dispute, the WTO Secretariat or the members of a panel. However, the European Communities "wonders whether the text of the DSU could be interpreted so widely" as to give non-governmental organizations the right to file submissions directly to a panel.

66. The European Communities contends that Article 13 of the DSU "does not oblige panels to 'accept' non-requested information which was not 'sought' for the purposes of a dispute settlement procedure." Panels should therefore reject submissions from non-governmental organizations when the panel itself had not requested such submissions. However, in the view of the European Communities, if a panel were interested in the information contained in an *amicus curiae* brief from a non-governmental organization, it would have the right to request and receive (to "seek") exactly the same information as had first been sent to it in an unsolicited manner. The European Communities agrees with the Panel that a Member, party to a dispute, is free to put forward as part of its own submission, a submission of a non-governmental organization that it considers relevant. The European Communities notes that its comments are based on the current language of Article 13 of the DSU.

67. The European Communities states further that the issues at stake in this dispute concern principles to which it attaches great importance, such as respect for the environment and the functioning of the multilateral trading system. The European Communities is bound by the text of the

Treaty Establishing the European Community⁵⁹ to ensure a harmonious and balanced development of economic activities with respect for the environment. The principle of sustainable development, also laid down in the first paragraph of the preamble to the *WTO Agreement*, as well as the precautionary principle, play an important role in the implementation of all EC policies. The EC position is mirrored in public international law by statements of the International Court of Justice, stressing the significance of respect for the environment.⁶⁰

68. The European Communities is convinced that international cooperation is the most effective means to address global and transboundary environmental problems, rather than unilateral measures which may be less environmentally effective and more trade disruptive. Economic performance and environmental performance are not necessarily incompatible. The European Communities asserts that "[w]hile countries have the sovereign right to design and implement their own environmental policies through the measures they consider appropriate to protect their domestic environment -- including the life and health of humans, animals and plants -- all countries have a responsibility to contribute to the solution of international environmental problems." Thus, the European Communities considers that "in general, the most effective means to attain the shared objectives relating to the conservation of global resources is by proceeding through the process of international co-operation."

69. To the European Communities, the approach to Article XX developed by previous panels and followed by the Appellate Body in *United States - Gasoline*⁶¹ -- that is, first examining whether a measure falls under one of the exceptions set out in paragraphs (a) to (j) of Article XX and, then, making an inquiry under the chapeau -- makes logical sense and could reasonably have been applied by the Panel in this case.

70. The European Communities agrees with the United States that it would be wrong for trade concerns to prevail over all other concerns in all situations under WTO rules. Article XX should not be construed so that trade concerns always prevail over the non-trade concerns reflected in that Article, including environmental concerns and those related to health and other legitimate policy objectives. It is up to panels and the Appellate Body to judge each case on its own merits, taking into account Members' rights and obligations.

⁵⁹Done at Rome, 25 March 1957, as amended.

⁶⁰The European Communities refers to: *Legality of the Threat or Use of Nuclear Weapons*, Advisory Opinion, (1996) I.C.J.Rep. pp. 241-242, para. 29; *Case Concerning the Gabčíkovo-Nagymoros Project*, (1998) 37 International Legal Materials 162, para. 140.

⁶¹Adopted 20 May 1996, WT/DS2/AB/R.

71. The European Communities also agrees with the United States that the adoption of the Panels' "test" -- namely, whether a measure is of a type that would threaten the security and predictability of the multilateral trading system -- would make trade concerns paramount to all other concerns and is thus inconsistent with the object and purpose of the *WTO Agreement*.

72. In the view of the European Communities, certain species, in particular migratory species, may require application of protective measures beyond usual territorial boundaries. Sea turtles should be considered a globally shared environmental resource because they are included in Annex I of CITES and are a species protected under the Convention on the Conservation of Migratory Species of Wild Animals.⁶² The appropriate way for Members concerned with the preservation of globally shared environmental resources to ensure such preservation is through internationally agreed solutions. Measures taken pursuant to such multilateral agreements would in general be allowed under the chapeau of Article XX.

73. However, the European Communities would not want to exclude the possibility, as a last resort, for a WTO Member, on its own, to take a "reasonable" measure with the aim of protecting and preserving a particular global environmental resource. However, such a measure would only be justified under exceptional circumstances and if consistent with general principles of public international law on "prescriptive jurisdiction". The Member would have to demonstrate that its environmentally protective measure was "reasonable", that is, no more trade restrictive than required to protect the globally shared environmental resource. Such a measure should be directly connected to the environmental objective and not go beyond what was required to limit the environmental damage. Finally, in such a case, the Member should have made genuine efforts to enter into cooperative environmental agreements with other Members. This is consistent with Principle 12 of the Rio Declaration on Environment and Development.

74. Given the Panel's factual finding that the United States did not enter into negotiations with the appellees before it imposed the import ban, the European Communities concludes that the United States has not demonstrated that a negotiated solution in respect of measures to protect sea turtles could not be found.

4. Hong Kong, China

75. Hong Kong, China states that it would be a "serious misunderstanding of the role of the WTO" if the multilateral trading system were viewed as impervious to environmental concerns. The

⁶²Done at Bonn, 23 June 1979, 19 International Legal Materials 15.

WTO system does not, and should not, impede the adoption of non-arbitrary and justifiable measures to protect the environment. Hong Kong, China fully shares the Panels' concern that the chapeau of Article XX should not be interpreted in a way that will threaten the security and predictability of trade relations under the *WTO Agreement*. With reference to the Appellate Body Report in *United States – Gasoline*⁶³, Hong Kong, China contends that an examination under the chapeau should focus on the manner in which the measure is applied, and answer the key question of whether the manner of application constitutes an abuse of the exceptions. Questions pertaining to the policy objective of the measure concerned should be set aside in examining the consistency of a measure with the chapeau.

76. Hong Kong, China argues that in line with the views of the Appellate Body in *United States – Gasoline*⁶⁴, Article XX should not be read to establish an unqualified deviation from the GATT principle of non-discrimination. Taken together, the three elements of the chapeau of Article XX impose an obligation not to discriminate based on the origin of the product. With respect to "non-discrimination", the standard of obligation imposed by the chapeau is different from that imposed by Articles I and III of the GATT 1994, which is based on a strict interpretation of the concept of "like products". The chapeau of Article XX requires governments that intervene in order to achieve one of the objectives laid down in the sub-paragraphs of Article XX to ensure that the competitive conditions resulting from their intervention do not *de jure* or *de facto* favour their domestic products, nor the products of a certain specific origin. There should be no ambiguity about the exact content of the level of protection and the competitive conditions established as a result of government intervention. In the view of Hong Kong, China, a legal finding of inconsistency of a measure with the chapeau of Article XX is predicated on a factual finding that a particular measure does not respect the principle of non-discrimination. If this requirement is satisfied, a panel then can proceed to examine whether the requirements laid down in a sub-paragraph of Article XX have been satisfied as well.

77. Hong Kong, China contends that Section 609 violates the chapeau of Article XX to the extent that, after the October 1996 ruling of the United States Court of International Trade, shrimp caught by fishermen in uncertified countries are subject to the import ban even if they were caught with nets that are equipped with TEDs. The resulting competitive conditions show that Section 609 does not meet the requirement of no arbitrary or unjustifiable discrimination between countries where the same conditions prevail. In addition, the 1993 Guidelines removed the possibility available to foreign producers to use any form of fishing other than TEDs in shrimp harvesting to avoid the incidental taking of sea turtles. This would be consistent with the Article XX chapeau only if the use of TEDs is

⁶³ Adopted 20 May 1996, WT/DS2/AB/R, page 22.

⁶⁴ *Ibid.*

proven to be the sole means by which the stated objective can be achieved. Otherwise, it must be acknowledged that other means may exist whose effectiveness can be demonstrated to be comparable to TEDs, and the United States must give the same treatment to shrimp harvested with measures that exporters could demonstrate are comparable in effectiveness to TEDs. Failure to do so renders Section 609 a means of arbitrary and unjustifiable discrimination between countries where the same conditions prevail. If the Appellate Body finds it necessary to examine the measure in question under sub-paragraphs (b) and (g) of Article XX, Hong Kong, China invites the Appellate Body to consider its arguments submitted to the Panel and reflected in the Panel Report, in particular, at paragraphs 4.44 and 4.45.

5. Nigeria

78. Nigeria confirms its views expressed in paragraph 4.53 of the Panel Report and requests the Appellate Body to uphold the Panel's decision. Nigeria shares the concern about the conservation and protection of sea turtles but, however, objects to the methods and measures for doing so. Nigeria's position is defined by paragraphs 169 and 171 of the Report (1996) of the Committee on Trade and Environment.⁶⁵

⁶⁵ Nigeria refers to WT/CTE/1, 12 November 1996. Paragraph 169 of the Report states: "WTO Member governments are committed not to introduce WTO-inconsistent or protectionist trade restrictions or countervailing measures in an attempt to offset any real or perceived adverse domestic economic or competitiveness effects of applying environmental policies; not only would this undermine the open, equitable and non-discriminatory nature of the multilateral trading system, it would also prove counterproductive to meeting environmental objectives and promoting sustainable development. Equally, and bearing in mind the fact that governments have the right to establish their national environmental standards in accordance with their respective environmental and developmental conditions, needs and priorities, WTO Members note that it would be inappropriate for them to relax their existing national environmental standards or their enforcement in order to promote their trade. The CTE notes the statement in the 1995 Report on Trade and Environment to the OECD Council at Ministerial Level that there has been no evidence of a systematic relationship between existing environmental policies and competitiveness impacts, nor of countries deliberately resorting to low environmental standards to gain competitive advantages. The CTE welcomes similar policy statements made in other inter-governmental fora."

Paragraph 171 of the Report states: "The CTE notes that governments have endorsed in the results of the 1992 U.N. Conference on Environment and Development their commitment to Principle 12 of the *Rio Declaration* that "Unilateral actions to deal with environmental challenges outside the jurisdiction of the importing country should be avoided. Environmental measures addressing transboundary or global problems should, as far as possible, be based on an international consensus." There is a clear complementarity between this approach and the work of the WTO in seeking cooperative multilateral solutions to trade concerns. The CTE endorses and supports multilateral solutions based on international cooperation and consensus as the best and most effective way for governments to tackle environmental problems of a transboundary or global nature. WTO Agreements and multilateral environmental agreements (MEAs) are representative of efforts of the international community to pursue shared goals, and in the development of a mutually supportive relationship between them due respect must be afforded to both."

III. Procedural Matters and Rulings

A. *Admissibility of the Briefs by Non-governmental Organizations Appended to the United States Appellant's Submission*

79. The United States attached to its appellant's submission, filed on 23 July 1998, three Exhibits, containing comments by, or "amicus curiae" briefs" submitted by, the following three groups of non-governmental organizations⁶⁶: 1. the Earth Island Institute; the Humane Society of the United States; and the Sierra Club; 2. the Center for International Environmental Law ("CIEL"); the Centre for Marine Conservation; the Environmental Foundation Ltd.; the Mangrove Action Project; the Philippine Ecological Network; Red Nacional de Accion Ecologica; and Sobrevivencia; and 3. the Worldwide Fund for Nature and the Foundation for International Environmental Law and Development. On 3 August 1998, CIEL *et al.* submitted a slightly revised version of their brief.

80. In their joint appellees' submission, filed on 7 August 1998, Joint Appellees object to these briefs appended to the appellant's submission, and request that the Appellate Body not consider these briefs. Joint Appellees argue that the appellant's submission, including its three Exhibits, is not in conformity with the stipulation in Article 17.6 of the DSU that an appeal "shall be limited to issues of law covered in the panel report and legal interpretations developed by the panel", nor with Rule 21(2) of the *Working Procedures for Appellate Review*. They ask the Appellate Body to reject as irrelevant the factual assertions made in certain paragraphs of the appellant's submission, as well as the factual information presented in the Exhibits. In their view, because of the incorporation of unauthorized material through the attachment of the Exhibits, the appellant's submission could no longer be considered a "precise statement" as required by Rule 21(2) of the *Working Procedures for Appellate Review*. Rather, a number of the factual and legal assertions contained in the Exhibits go beyond the position taken by the appellant, resulting in confusion concerning the exact nature and linkage between the appeal and the three Exhibits.

81. Joint Appellees state further that the submission of Exhibits that present the views of non-governmental organizations, as opposed to the views of the appellant Member, is not contemplated in, or authorized by, the DSU or the *Working Procedures for Appellate Review*. Such submissions were

not in conformity with Article 17.4 of the DSU, nor with Rule 28(1) of the *Working Procedures for Appellate Review*, which vests the discretion to request additional submissions with the Appellate Body. According to Joint Appellees, the decision of the appellant to attach the Exhibits to its submission gives rise both to contradictions and internal inconsistencies, and raises serious procedural and systemic problems. Joint Appellees maintain that by virtue of their incorporation into the appellant's submission, these pleadings are no longer "amicus curiae" briefs", but instead have become a portion of the appellant's submission, and thus have also become what would appear to be the official United States position.

82. In its appellee's submission, also filed on 7 August 1998, Malaysia similarly urges the Appellate Body to rule that the three Exhibits appended to the United States appellant's submission are inadmissible in this appeal. Malaysia refers to its argument before the Panel that briefs from non-governmental organizations do not fall within Article 13 of the DSU. In addition, according to Malaysia, admission of the Exhibits would not be consonant with Article 17.6 of the DSU, or with Rule 21(2) of the *Working Procedures for Appellate Review*, as the United States appellant's submission and Exhibit 2 contain statements of facts. Moreover, Article 17.4 of the DSU only grants the right to make written and oral submissions to third parties. Articles 11 and 17.12 of the DSU are significant and serve to safeguard the admissibility of evidence before the Appellate Body. In the alternative, in the event the Appellate Body ruled that Exhibits 1-3 of the appellant's submission should be admitted, Malaysia submits rebuttals to each of the Exhibits.

83. On 11 August 1998, we issued a ruling on this preliminary procedural matter addressed to the participants and third participants, as follows:

We have decided to accept for consideration, insofar as they may be pertinent, the legal arguments made by the various non-governmental organizations in the three briefs attached as exhibits to the appellant's submission of the United States, as well as the revised version of the brief by the Center for International Environmental Law *et al.*, which was submitted to us on 3 August 1998. The reasons for our ruling will be given in the Appellate Body Report.

84. In the same ruling, we addressed the following questions to the appellant, the United States:

to what extent do you agree with or adopt any one or more of the legal arguments set out in the three briefs prepared by the non-governmental organizations and appended as exhibits to your appellant's submission? In particular, do you adopt the legal arguments stated therein relating to paragraphs (b) and (g) and the chapeau of Article XX of the GATT 1994?

⁶⁶In respect of these Exhibits, the United States stated the following: "Encouraging the use of TEDs in order to promote sea turtle conservation is a matter of great importance to a number of nongovernmental environmental organizations. Three groups of these organizations – each with specialized expertise in conservation of sea turtles and other endangered species – have prepared submissions reflecting their respective independent views with respect to the use of TEDs and other issues. The United States is submitting these materials to the Appellate Body for its information attached hereto as U.S. Appellant Exhibits 1-3." United States appellant's submission, para. 2, footnote 1.

85. We asked the United States to respond in writing to these questions by 13 August 1998, and offered an opportunity to the appellees and the third participants to respond, by 17 August 1998, to the answer filed by the United States concerning which aspects of these briefs it accepted and endorsed as part of its appeal as well as to the legal arguments made in the briefs by the non-governmental organizations. We noted at the time that Malaysia had already done the latter in Exhibits 1 through 3 attached to its appellee's submission.

86. On 13 August 1998, the United States replied as follows:

The main U.S. submission reflects the views of the United States on the legal issues in this appeal. As explained in our appellant's submission, the three submissions prepared by non-governmental organizations reflect the independent views of those organizations. . . . These non-governmental organizations have a great interest, and specialized expertise, in sea turtle conservation and related matters. It is appropriate therefore that the Appellate Body be informed of those organizations' views. The United States is not adopting these views as separate matters to which the Appellate Body must respond.

The United States agrees with the legal arguments in the submissions of the non-governmental organizations to the extent those arguments concur with the U.S. arguments set out in our main submission

87. On 17 August 1998, Joint Appellees filed a joint response, and Malaysia filed a separate one, to the matters raised in the reply of the United States, as well as in the Exhibits. Without prejudice to their view that the receipt and consideration by the Appellate Body of the briefs of non-governmental organizations attached to the appellant's submission is not authorized by the DSU or the *Working Procedures for Appellate Review*, Joint Appellees responded to certain legal arguments made in the briefs. Malaysia incorporated by reference its rebuttals to the briefs contained in its appellee's submission of 7 August 1998, and made certain additional comments in respect of each of the briefs. Also, on 17 August 1998, Hong Kong, China and Mexico filed statements in respect of the same matters. Hong Kong, China stated that the reply by the United States was unclear and that it was not possible, at that stage, to comment further on the legal arguments. For its part, Mexico stated that if the Appellate Body were to make use of arguments which are outside the terms of Article 17.6 of the DSU and which are not clearly and explicitly attributable to a Member that is a party to the dispute, the Appellate Body would exceed its powers under the DSU.

88. The admissibility of the briefs by certain non-governmental organizations which have been appended to the appellant's submission of the United States is a legal question raised by the appellees. This is a legal issue which does not relate to a finding of law made, or a legal interpretation developed, by the Panel in the Panel Report. For this reason, it has seemed appropriate to us to deal

with this issue separately from the issues raised by the appellant and addressed in the succeeding portions of this Appellate Body Report.

89. We consider that the attaching of a brief or other material to the submission of either appellant or appellee, no matter how or where such material may have originated, renders that material at least *prima facie* an integral part of that participant's submission. On the one hand, it is of course for a participant in an appeal to determine for itself what to include in its submission. On the other hand, a participant filing a submission is properly regarded as assuming responsibility for the contents of that submission, including any annexes or other attachments.

90. In the present appeal, the United States has made it clear that its views "on the legal issues in this appeal" are found in "the main U.S. submission." The United States has confirmed its agreement with the legal arguments in the attached submissions of the non-governmental organizations, to the extent that those arguments "concur with the U.S. arguments set out in [its] main submission."

91. We admit, therefore, the briefs attached to the appellant's submission of the United States as part of that appellant's submission. At the same time, considering that the United States has itself accepted the briefs in a tentative and qualified manner only, we focus in the succeeding sections below on the legal arguments in the main U.S. appellant's submission.

B. *Sufficiency of the Notice of Appeal*

92. In their joint appellee's submission, filed on 7 August 1998, Joint Appellees contend that the notice of appeal by the United States is defective in form and that the action is, therefore, not properly before the Appellate Body. They contend that the appellant's notice of appeal is both vague and cursory, and is, accordingly, not in compliance with the procedural requirements set forth in Rule 20(2)(d) of the *Working Procedures for Appellate Review*. It is also not a proper "submission" filed "within the required time periods" pursuant to Rule 29 of the *Working Procedures for Appellate Review*. As a result, it is argued, the United States' appeal should be dismissed by the Appellate Body on this ground alone. The appellant's notice of appeal does not identify any legal errors in a manner sufficient for the appellees to develop a defence, and this, in the appellees' view, made it impossible for them to discern the issues that were going to be the subject of the appeal until the appellant filed its written submission 10 days later. This reduced the time available for all appellees to draft their responsive submissions from 25 days to 15 days.

93. According to Joint Appellees, vague notices of appeal should not be tolerated for at least two reasons. First, considerations of fundamental fairness and good faith mandate that the appellant should not be permitted to gain a tactical advantage through its failure to fulfill the requirements of the *Working Procedures for Appellate Review*. Second, carefully considered and well-drafted submissions benefit the decision-making process of the Appellate Body.

94. The United States in turn submits that the notice of appeal provided just the type of "brief statement of the nature of the appeal, including the allegations of error in the issues of law covered in the panel report and legal interpretations developed by the panel" (emphasis in the original) called for in Rule 20(2)(d) of the *Working Procedures for Appellate Review*. First, the notice of appeal explained that the United States was appealing from the findings on issues of law and related legal interpretations leading to the panel's conclusion that the United States measure was outside the scope of the Article XX chapeau. Second, the notice of appeal stated that the United States was appealing from the Panel's procedural finding that the Panel lacked discretion to accept materials received from non-governmental sources. The appellees did not explain what additional information they believed should have been included in the notice of appeal. Furthermore, according to the United States, the appellees' allegation of prejudice was unfounded. The appellees well knew the basic argument that the United States would present to support its claim of legal error. Indeed, the appellees themselves had pointed out that the United States appeal rests solely on one leg, that is, that the Panel created a "threat to the multilateral trading system" test, and that the United States already raised this same issue at the interim review stage. In short, the appeal did not result in any unfair surprise to the appellees.

95. Rule 20(2) of the *Working Procedures for Appellate Review* provides, in relevant part:

(2) A Notice of Appeal shall include the following information:

-
- (d) a *brief statement of the nature of the appeal, including the allegations of errors* in the issues of law covered in the panel report and legal interpretations developed by the panel.(emphasis added)

The *Working Procedures for Appellate Review* enjoin the appellant to be *brief* in its notice of appeal in setting out "the nature of the appeal, including the allegations of errors". We believe that, in principle, the "nature of the appeal" and "the allegations of errors" are sufficiently set out where the notice of appeal adequately identifies the findings or legal interpretations of the Panel which are being

appealed as erroneous. The notice of appeal is not expected to contain the reasons why the appellant regards those findings or interpretations as erroneous. The notice of appeal is not designed to be a summary or outline of the arguments to be made by the appellant. The legal arguments in support of the allegations of error are, of course, to be set out and developed in the appellant's submission.

96. In this instance, the notice of appeal does communicate the decision by the United States to appeal certain legal issues covered and certain legal interpretations developed in the Panel Report. The notice then refers to the two allegedly erroneous findings of the Panel being appealed from -- the finding that the United States measure at issue is not within the scope of measures permitted under the chapeau of Article XX; and the finding that accepting non-requested information from non-governmental sources is incompatible with the DSU. The notice did not cite the numbered paragraphs of the Panel Report containing the above findings, but Joint Appellees do not assert that that is necessary. The references in the notice of appeal to these two findings of the Panel are terse⁶⁷, but there is no mistaking which findings or interpretations of the Panel the Appellate Body is asked to review. We accordingly hold that the notice of appeal by the United States meets the requirements of Rule 20(2)(d) of the *Working Procedures for Appellate Review*, and deny the request of Joint Appellees to dismiss the entire appeal summarily on the sole ground of insufficiency of the notice of appeal.

97. It remains only to recall that the right of a party to appeal from legal findings and legal interpretations reached by a panel in a dispute settlement proceeding is an important new right established in the DSU resulting from the Uruguay Round. We believe that the provisions of Rule 20(2) and other Rules of the *Working Procedures for Appellate Review* are most appropriately read so as to give full meaning and effect to the right of appeal and to give a party which regards itself aggrieved by some legal finding or interpretation in a panel report a real and effective opportunity to demonstrate the error in such finding or interpretation. It is scarcely necessary to add that an appellee is, of course, always entitled to its full measure of due process. In the present appeal, perhaps the best indication that that full measure of due process was not in any degree impaired by the notice of appeal filed by the United States, is the developed and substantial nature of the appellees' submissions.

⁶⁷The interpretation of the Panel concerning non-requested information, and its finding on the inconsistency of Section 609 with Article XX of the GATT 1994, are themselves cast in fairly terse language; Panel Report, paras. 7.8, fourth sentence, 7.49 and 7.62.

IV. Issues Raised in This Appeal

98. The issues raised in this appeal by the appellant, the United States, are the following:
- (a) whether the Panel erred in finding that accepting non-requested information from non-governmental sources would be incompatible with the provisions of the DSU as currently applied; and
 - (b) whether the Panel erred in finding that the measure at issue constitutes unjustifiable discrimination between countries where the same conditions prevail and thus is not within the scope of measures permitted under Article XX of the GATT 1994.

V. Panel Proceedings and Non-requested Information

99. In the course of the proceedings before the Panel, on 28 July 1997, the Panel received a brief from the Center for Marine Conservation ("CMC") and the Center for International Environmental Law ("CIEL"). Both are non-governmental organizations. On 16 September 1997, the Panel received another brief, this time from the World Wide Fund for Nature. The Panel acknowledged receipt of the two briefs, which the non-governmental organizations also sent directly to the parties to this dispute. The complaining parties -- India, Malaysia, Pakistan and Thailand -- requested the Panel not to consider the contents of the briefs in dealing with the dispute. In contrast, the United States urged the Panel to avail itself of any relevant information in the two briefs, as well as in any other similar communications.⁶⁸ The Panel disposed of this matter in the following manner:

We had not requested such information as was contained in the above-mentioned documents. We note that, pursuant to Article 13 of the DSU, the initiative to seek information and to select the source of information rests with the Panel. In any other situations, only parties and third parties are allowed to submit information directly to the Panel. Accepting non-requested information from non-governmental sources would be, in our opinion, incompatible with the provisions of the DSU as currently applied. We therefore informed the parties that we did not intend to take these documents into consideration. We observed, moreover, that it was usual practice for parties to put forward whatever documents they considered relevant to support their case and that, if any party in the present dispute wanted to put forward these documents, or parts of them, as part of their own submissions to the Panel, they were free to do so. If this were the case, the other parties would have two weeks to respond to the additional material.

We noted that the United States availed themselves of this opportunity by designating Section III of the document submitted by the Center for Marine Conservation and the Center for International Environmental Law as an annex to its second submission to the Panel.⁶⁹ (emphasis added)

100. We note that the Panel did two things. First, the Panel declared a legal interpretation of certain provisions of the DSU: i.e., that accepting non-requested information from non-governmental sources would be "incompatible with the provisions of the DSU as currently applied." Evidently as a result of this legal interpretation, the Panel announced that it would not take the briefs submitted by non-governmental organizations into consideration. Second, the Panel nevertheless allowed any party to the dispute to put forward the briefs, or any part thereof, as part of its own submissions to the Panel, giving the other party or parties, in such case, two additional weeks to respond to the additional material. The United States appeals from this legal interpretation of the Panel.

101. It may be well to stress at the outset that access to the dispute settlement process of the WTO is limited to Members of the WTO. This access is not available, under the *WTO Agreement* and the covered agreements as they currently exist, to individuals or international organizations, whether governmental or non-governmental. Only Members may become parties to a dispute of which a panel may be seized, and only Members "having a substantial interest in a matter before a panel" may become third parties in the proceedings before that panel.⁷⁰ Thus, under the DSU, only Members who are parties to a dispute, or who have notified their interest in becoming third parties in such a dispute to the DSB, have a *legal right* to make submissions to, and have a *legal right* to have those

⁶⁹Panel Report, para. 7.8.

⁷⁰See Articles 4, 6, 9 and 10 of the DSU.

⁶⁸Panel Report, para. 3.129

submissions considered by, a panel.⁷¹ Correlatively, a panel is *obliged* in law to accept and give due consideration only to submissions made by the parties and the third parties in a panel proceeding. These are basic legal propositions; they do not, however, dispose of the issue here presented by the appellant's first claim of error. We believe this interpretative issue is most appropriately addressed by examining what a panel is *authorized* to do under the DSU.

102. Article 13 of the DSU reads as follows:

Article 13
Right to Seek Information

1. *Each panel shall have the right to seek information and technical advice from any individual or body which it deems appropriate.* However, before a panel seeks such information or advice from any individual or body within the jurisdiction of a Member it shall inform the authorities of that Member. *A Member should respond promptly and fully to any request by a panel for such information as the panel considers necessary and appropriate.* Confidential information which is provided shall not be revealed without formal authorization from the individual, body, or authorities of the Member providing the information.
2. *Panels may seek information from any relevant source and may consult experts to obtain their opinion on certain aspects of the matter.* With respect to a factual issue concerning a scientific or other technical matter raised by a party to a dispute, a panel may request an advisory report in writing from an expert review group. Rules for the establishment of such a group and its procedures are set forth in Appendix 4. (emphasis added)

103. In *EC Measures Affecting Meat and Meat Products (Hormones)*, we observed that Article 13 of the DSU⁷² "enable[s] panels to seek information and advice as they deem appropriate in a particular case."⁷³ Also, in *Argentina – Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items*, we ruled that:

⁷¹Articles 10 and 12, and Appendix 3 of the DSU. We note that Article 17.4 of the DSU limits the right to appeal a panel report to parties to a dispute, and permits third parties which have notified the DSB of their substantial interest in the matter to make written submissions to, and be given an opportunity to be heard by, the Appellate Body.

⁷²As well as Article 11.2 of the *Agreement on the Application of Sanitary and Phytosanitary Measures*.

⁷³Adopted 13 February 1998, WT/DS26/AB/R, WT/DS48/AB/R, para. 147.

Pursuant to Article 13.2 of the DSU, a panel may seek information from any relevant source and may consult experts to obtain their opinions on certain aspects of the matter at issue. *This is a grant of discretionary authority: a panel is not duty-bound to seek information in each and every case or to consult particular experts under this provision.* We recall our statement in *EC Measures Concerning Meat and Meat Products (Hormones)* that Article 13 of the DSU enables a panel to seek information and technical advice as it deems appropriate in a particular case, and that the DSU leaves "to the sound discretion of a panel the determination of whether the establishment of an expert review group is necessary or appropriate." *Just as a panel has the discretion to determine how to seek expert advice, so also does a panel have the discretion to determine whether to seek information or expert advice at all.*

...

In this case, we find that the Panel acted within the bounds of its discretionary authority under Articles 11 and 13 of the DSU in deciding not to seek information from, nor to consult with, the IMF.⁷⁴ (emphasis added)

104. The comprehensive nature of the authority of a panel to "seek" information and technical advice from "any individual or body" it may consider appropriate, or from "any relevant source", should be underscored. This authority embraces more than merely the choice and evaluation of the source of the information or advice which it may seek. A panel's authority includes the authority to decide *not to seek* such information or advice at all. We consider that a panel also has the authority to *accept or reject* any information or advice which it may have sought and received, or to *make some other appropriate disposition* thereof. It is particularly within the province and the authority of a panel to determine *the need for information and advice* in a specific case, to ascertain the *acceptability and relevancy* of information or advice received, and to decide *what weight to ascribe to that information or advice* or to conclude that no weight at all should be given to what has been received.

105. It is also pertinent to note that Article 12.1 of the DSU authorizes panels to depart from, or to add to, the Working Procedures set forth in Appendix 3 of the DSU, and in effect to develop their own Working Procedures, after consultation with the parties to the dispute. Article 12.2 goes on to direct that "[p]anel procedures should provide *sufficient flexibility* so as to *ensure high-quality panel reports* while *not unduly delaying the panel process*." (emphasis added)

⁷⁴Adopted 22 April 1998, WT/DS56/AB/R, paras. 84-86.

106. The thrust of Articles 12 and 13, taken together, is that the DSU accords to a panel established by the DSB, and engaged in a dispute settlement proceeding, ample and extensive authority to undertake and to control the process by which it informs itself both of the relevant facts of the dispute and of the legal norms and principles applicable to such facts. That authority, and the breadth thereof, is indispensably necessary to enable a panel to discharge its duty imposed by Article 11 of the DSU to "make an objective assessment of the matter before it, including an *objective assessment of the facts of the case* and the *applicability of and conformity with the relevant covered agreements*" (emphasis added)

107. Against this context of broad authority vested in panels by the DSU, and given the object and purpose of the Panel's mandate as revealed in Article 11, we do not believe that the word "seek" must necessarily be read, as apparently the Panel read it, in too literal a manner. That the Panel's reading of the word "seek" is unnecessarily formal and technical in nature becomes clear should an "individual or body" first ask a panel for permission to file a statement or a brief. In such an event, a panel may decline to grant the leave requested. If, in the exercise of its sound discretion in a particular case, a panel concludes *inter alia* that it could do so without "unduly delaying the panel process", it could grant permission to file a statement or a brief, subject to such conditions as it deems appropriate. The exercise of the panel's discretion could, of course, and perhaps should, include consultation with the parties to the dispute. In this kind of situation, for all practical and pertinent purposes, the distinction between "requested" and "non-requested" information vanishes.

108. In the present context, authority to *seek* information is not properly equated with a *prohibition* on accepting information which has been submitted without having been requested by a panel. A panel has the discretionary authority either to accept and consider or to reject information and advice submitted to it, *whether requested by a panel or not*. The fact that a panel may *motu proprio* have initiated the request for information does not, by itself, bind the panel to accept and consider the information which is actually submitted. The amplitude of the authority vested in panels to shape the processes of fact-finding and legal interpretation makes clear that a panel will *not* be deluged, as it were, with non-requested material, *unless that panel allows itself to be so deluged*.

109. Moreover, acceptance and rejection of the information and advice of the kind here submitted to the Panel need not exhaust the universe of possible appropriate dispositions thereof. In the present case, the Panel did not reject the information outright. The Panel suggested instead, that, if any of the parties wanted "to put forward these documents, or parts of them, as part of their own submissions to

the Panel, they were free to do so."⁷⁵ In response, the United States then designated Section III of the document submitted by CIEL/CMC as an annex to its second submission to the Panel, and the Panel gave the appellees two weeks to respond. We believe that this practical disposition of the matter by the Panel in this dispute may be detached, as it were, from the legal interpretation adopted by the Panel of the word "seek" in Article 13.1 of the DSU. When so viewed, we conclude that the actual disposition of these briefs by the Panel does not constitute either legal error or abuse of its discretionary authority in respect of this matter. The Panel was, accordingly, entitled to treat and take into consideration the section of the brief that the United States appended to its second submission to the Panel, just like any other part of the United States pleading.

110. We find, and so hold, that the Panel erred in its legal interpretation that accepting non-requested information from non-governmental sources is incompatible with the provisions of the DSU. At the same time, we consider that the Panel acted within the scope of its authority under Articles 12 and 13 of the DSU in allowing any party to the dispute to attach the briefs by non-governmental organizations, or any portion thereof, to its own submissions.

VI. Appraising Section 609 Under Article XX of the GATT 1994

111. We turn to the second issue raised by the appellant, the United States, which is whether the Panel erred in finding that the measure at issue⁷⁶ constitutes unjustifiable discrimination between countries where the same conditions prevail and, thus, is not within the scope of measures permitted under Article XX of the GATT 1994.

A. *The Panel's Findings and Interpretative Analysis*

112. The Panel's findings, from which the United States appeals, and the gist of its supporting reasoning, are set forth below *in extenso*:

⁷⁵Panel Report, para. 7.8.

⁷⁶The United States measure at issue is referred to in this Report as "Section 609" or "the measure". By these terms, we mean Section 609 and the 1996 Guidelines.

... [W]e are of the opinion that the *chapeau* [of Article XX, interpreted within its context and in the light of the object and purpose of GATT and of the WTO Agreement, only allows Members to derogate from GATT provisions so long as, in doing so, they do not undermine the WTO multilateral trading system, thus also abusing the exceptions contained in Article XX. Such undermining and abuse would occur when a Member jeopardizes the operation of the WTO Agreement in such a way that guaranteed market access and nondiscriminatory treatment within a multilateral framework would no longer be possible. ... We are of the view that a *type of measure adopted by a Member* which, on its own, may appear to have a relatively minor impact on the multilateral trading system, may nonetheless raise a serious threat to that system if similar measures are adopted by the same or other Members. Thus, by allowing such type of measures even though their individual impact may not appear to be such as to threaten the multilateral trading system, one would affect the security and predictability of the multilateral trading system. We consequently find that when considering a measure under Article XX, we must determine not only whether the measure on its own undermines the WTO multilateral trading system, but also whether such type of measure, if it were to be adopted by other Members, would threaten the security and predictability of the multilateral trading system.⁷⁷

In our view, if an interpretation of the *chapeau* of Article XX were to be followed which would allow a Member to adopt measures conditioning access to its market for a given product upon the adoption by the exporting Members of certain policies, including conservation policies, GATT 1994 and the WTO Agreement could no longer serve as a multilateral framework for trade among Members as security and predictability of trade relations under those agreements would be threatened. This follows because, if one WTO Member were allowed to adopt such measures, then other Members would also have the right to adopt similar measures on the same subject but with differing, or even conflicting, requirements. ... Market access for goods could become subject to an increasing number of conflicting policy requirements for the same product and this would rapidly lead to the end of the WTO multilateral trading system.⁷⁸

⁷⁷Panel Report, para. 7.44.

⁷⁸Panel Report, para. 7.45.

... Section 609, as applied, is a measure conditioning access to the US market for a given product on the adoption by exporting Members of conservation policies that the United States considers to be comparable to its own in terms of regulatory programmes and incidental taking.⁷⁹

... it appears to us that, in light of the context of the term "unjustifiable" and the object and purpose of the WTO Agreement, the US measure at issue constitutes unjustifiable discrimination between countries where the same conditions prevail and thus is not within the scope of measures permitted under Article XX.⁸⁰

...

We therefore find that the US measure at issue is not within the scope of measures permitted under the *chapeau* of Article XX.⁸¹ (emphasis added)

113. Article XX of the GATT 1994 reads, in its relevant parts:

Article XX
General Exceptions

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Member of measures:

- ...
 - (b) necessary to protect human, animal or plant life or health;
 - ...
 - (g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption;

114. The Panel did not follow all of the steps of applying the "customary rules of interpretation of public international law" as required by Article 3.2 of the DSU. As we have emphasized numerous

⁷⁹Panel Report, para. 7.48.

⁸⁰Panel Report, para. 7.49.

⁸¹Panel Report, para. 7.62.

times⁸², these rules call for an examination of the ordinary meaning of the words of a treaty, read in their context, and in the light of the object and purpose of the treaty involved. A treaty interpreter must begin with, and focus upon, the text of the particular provision to be interpreted. It is in the words constituting that provision, read in their context, that the object and purpose of the states parties to the treaty must first be sought. Where the meaning imparted by the text itself is equivocal or inconclusive, or where confirmation of the correctness of the reading of the text itself is desired, light from the object and purpose of the treaty as a whole may usefully be sought.⁸³

115. In the present case, the Panel did not expressly examine the ordinary meaning of the words of Article XX. The Panel disregarded the fact that the introductory clauses of Article XX speak of the "manner" in which measures sought to be justified are "applied". In *United States - Gasoline*, we pointed out that the chapeau of Article XX "by its express terms addresses, not so much the questioned measure or its specific contents as such, but rather the manner in which that measure is applied."⁸⁴ (emphasis added) The Panel did not inquire specifically into how the application of Section 609 constitutes "a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade." What the Panel did, in purporting to examine the consistency of the measure with the chapeau of Article XX, was to focus repeatedly on the *design of the measure itself*. For instance, the Panel stressed that it was addressing "a particular situation where a Member has taken unilateral measures which, by their nature, could put the multilateral trading system at risk."⁸⁵ (emphasis added)

116. The general design of a measure, as distinguished from its application, is, however, to be examined in the course of determining whether that measure falls within one or another of the paragraphs of Article XX following the chapeau. The Panel failed to scrutinize the *immediate*

⁸² See, for example, the Appellate Body Reports in: *United States - Gasoline*, adopted 20 May 1996, WT/DS2/AB/R, p. 17; *Japan - Taxes on Alcoholic Beverages*, adopted 1 November 1996, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, pp. 10-12; *India - Patent Protection for Pharmaceutical and Agricultural Chemical Products*, adopted 16 January 1998, WT/DS50/AB/R, paras. 45-46; *Argentina - Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items*, adopted 13 February 1998, WT/DS56/AB/R, para. 47; and *European Communities - Customs Classification of Certain Computer Equipment*, adopted 22 June 1998, WT/DS62/AB/R, WT/DS67/AB/R, WT/DS68/AB/R, para. 85.

⁸³ J. Sinclair, *The Vienna Convention on the Law of Treaties*, 2nd ed. (Manchester University Press, 1984), pp. 130-131.

⁸⁴ Adopted 20 May 1996, WT/DS2/AB/R, p. 22.

⁸⁵ Panel Report, para. 7.60. The Panel also stated, in paras. 7.33-7.34 of the Panel Report: "... Pursuant to the chapeau of Article XX, a measure may discriminate, but not in an 'arbitrary' or 'unjustifiable' manner.

We therefore move to consider whether the US measure conditioning market access on the adoption of certain conservation policies by the exporting Member could be considered as 'unjustifiable discrimination' ... (emphasis added)

context of the chapeau: i.e., paragraphs (a) to (j) of Article XX. Moreover, the Panel did not look into the object and purpose of the *chapeau of Article XX*. Rather, the Panel looked into the object and purpose of the *whole of the GATT 1994 and the WTO Agreement*, which object and purpose it described in an overly broad manner. Thus, the Panel arrived at the very broad formulation that measures which "undermine the WTO multilateral trading system"⁸⁶ must be regarded as "not within the scope of measures permitted under the chapeau of Article XX."⁸⁷ Maintaining, rather than undermining, the multilateral trading system is necessarily a fundamental and pervasive premise underlying the *WTO Agreement*; but it is not a right or an obligation, nor is it an interpretative rule which can be employed in the appraisal of a given measure under the chapeau of Article XX. In *United States - Gasoline*, we stated that it is "important to underscore that the purpose and object of the introductory clauses of Article XX is generally the prevention of 'abuse of the exceptions of [Article XX]'"⁸⁸ (emphasis added) The Panel did not attempt to inquire into how the measure at stake was being *applied in such a manner* as to constitute *abuse or misuse of a given kind of exception*.

117. The above flaws in the Panel's analysis and findings flow almost naturally from the fact that the Panel disregarded the sequence of steps essential for carrying out such an analysis. The Panel defined its approach as first "determin[ing] whether the measure at issue satisfies the conditions contained in the chapeau."⁸⁹ If the Panel found that to be the case, it said that it "shall then examine whether the US measure is covered by the terms of Article XX(b) or (g)."⁹⁰ The Panel attempted to justify its interpretative approach in the following manner:

As mentioned by the Appellate Body in its report in the *Gasoline* case, in order for the justification of Article XX to be extended to a given measure, it must not only come under one or another of the particular exceptions - paragraphs (a) to (j) - listed under Article XX; it must also satisfy the requirements imposed by the opening clause of Article XX. We note that panels have in the past considered the specific paragraphs of Article XX before reviewing the applicability of the conditions contained in the chapeau. However, as the conditions contained in the introductory provision apply to any of the paragraphs of Article XX, it seems equally appropriate to analyse first the introductory provision of Article XX.⁹¹ (emphasis added)

⁸⁶ See, for example, Panel Report, para. 7.44.

⁸⁷ Panel Report, para. 7.62.

⁸⁸ Adopted 20 May 1996, WT/DS2/AB/R, p. 22.

⁸⁹ Panel Report, para. 7.29.

⁹⁰ *Ibid.*

⁹¹ Panel Report, para. 7.28.

118. In *United States - Gasoline*, we enunciated the appropriate method for applying Article XX of the GATT 1994:

In order that the justifying protection of Article XX may be extended to it, the measure at issue must not only come under one or another of the particular exceptions -- paragraphs (a) to (j) -- listed under Article XX; it must also satisfy the requirements imposed by the opening clauses of Article XX. *The analysis is, in other words, two-tiered: first, provisional justification by reason of characterization of the measure under XX(g); second, further appraisal of the same measure under the introductory clauses of Article XX.*⁹² (emphasis added)

119. The sequence of steps indicated above in the analysis of a claim of justification under Article XX reflects, not inadvertence or random choice, but rather the fundamental structure and logic of Article XX. The Panel appears to suggest, albeit indirectly, that following the indicated sequence of steps, or the inverse thereof, does not make any difference. To the Panel, reversing the sequence set out in *United States - Gasoline* "seems equally appropriate."⁹³ We do not agree.

120. The task of interpreting the chapeau so as to prevent the abuse or misuse of the specific exemptions provided for in Article XX is rendered very difficult, if indeed it remains possible at all, where the interpreter (like the Panel in this case) has not first identified and examined the specific exception threatened with abuse. The standards established in the chapeau are, moreover, necessarily broad in scope and reach: the prohibition of the *application* of a measure "in a manner which would constitute a means of *arbitrary or unjustifiable discrimination* between countries where the same conditions prevail" or "a *disguised restriction* on international trade." (emphasis added) When applied in a particular case, the actual contours and contents of these standards will vary as the kind of measure under examination varies. What is appropriately characterizable as "arbitrary discrimination" or "unjustifiable discrimination", or as a "disguised restriction on international trade" in respect of one category of measures, need not be so with respect to another group or type of measures. The standard of "arbitrary discrimination", for example, under the chapeau may be different for a measure that purports to be necessary to protect public morals than for one relating to the products of prison labour.

121. The consequences of the interpretative approach adopted by the Panel are apparent in its findings. The Panel formulated a broad standard and a test for appraising measures sought to be justified under the chapeau; it is a standard or a test that finds no basis either in the text of the chapeau or in that of either of the two specific exceptions claimed by the United States. The Panel, in effect, constructed an *a priori* test that purports to define a category of measures which, *ratione*

⁹²Adopted 20 May 1996, WT/DS2/AB/R, p. 22.

⁹³Panel Report, para 7.28.

materiae, fall outside the justifying protection of Article XX's chapeau.⁹⁴ In the present case, the Panel found that the United States measure at stake fell within that class of excluded measures because Section 609 conditions access to the domestic shrimp market of the United States on the adoption by exporting countries of certain conservation policies prescribed by the United States. It appears to us, however, that conditioning access to a Member's domestic market on whether exporting Members comply with, or adopt, a policy or policies unilaterally prescribed by the importing Member may, to some degree, be a common aspect of measures falling within the scope of one or another of the exceptions (a) to (j) of Article XX. Paragraphs (a) to (j) comprise measures that are recognized as *exceptions to substantive obligations* established in the GATT 1994, because the domestic policies embodied in such measures have been recognized as important and legitimate in character. It is not necessary to assume that requiring from exporting countries compliance with, or adoption of, certain policies (although covered in principle by one or another of the exceptions) prescribed by the importing country, renders a measure *a priori* incapable of justification under Article XX. Such an interpretation renders most, if not all, of the specific exceptions of Article XX inutile, a result abhorrent to the principles of interpretation we are bound to apply.

122. We hold that the findings of the Panel quoted in paragraph 112 above, and the interpretative analysis embodied therein, constitute error in legal interpretation and accordingly reverse them.

123. Having reversed the Panel's legal conclusion that the United States measure at issue "is not within the scope of measures permitted under the chapeau of Article XX"⁹⁵, we believe that it is our duty and our responsibility to complete the legal analysis in this case in order to determine whether Section 609 qualifies for justification under Article XX. In doing this, we are fully aware of our jurisdiction and mandate under Article 17 of the DSU. We have found ourselves in similar situations on a number of occasions. Most recently, in *European Communities - Measures Affecting the Importation of Certain Poultry Products*, we stated:

In certain appeals, ... the reversal of a panel's finding on a legal issue may require us to make a finding on a legal issue which was not addressed by the panel.⁹⁶

In that case, having reversed the panel's finding on Article 5.1(b) of the *Agreement on Agriculture*, we completed the legal analysis by making a finding on the consistency of the measure at issue with Article 5.5 of the *Agreement on Agriculture*. Similarly, in *Canada - Certain Measures Concerning*

⁹⁴See, for example, Panel Report, para. 7.50.

⁹⁵Panel Report, para. 7.62.

⁹⁶Adopted 23 July 1998, WT/DS69/AB/R, para. 156.

*Periodicals*⁹⁷, having reversed the panel's findings on the issue of "like products" under the first sentence of Article III:2 of the GATT 1994, we examined the consistency of the measure with the second sentence of Article III:2. And, in *United States – Gasoline*⁹⁸, having reversed the panel's findings on the first part of Article XX(g) of the GATT 1994, we completed the analysis of the terms of Article XX(g), and then examined the application of the measure at issue in that case under the chapeau of Article XX.

124. As in those previous cases, we believe it is our responsibility here to examine the claim by the United States for justification of Section 609 under Article XX in order properly to resolve this dispute between the parties. We do this, in part, recognizing that Article 3.7 of the DSU emphasizes that: "The aim of the dispute settlement mechanism is to secure a positive solution to a dispute." Fortunately, in the present case, as in the mentioned previous cases, we believe that the facts on the record of the panel proceedings permit us to undertake the completion of the analysis required to resolve this dispute.

B. *Article XX(g): Provisional Justification of Section 609*

125. In claiming justification for its measure, the United States primarily invokes Article XX(g). Justification under Article XX(b) is claimed only in the alternative; that is, the United States suggests that we should look at Article XX(b) only if we find that Section 609 does not fall within the ambit of Article XX(g).⁹⁹ We proceed, therefore, to the first tier of the analysis of Section 609 and to our consideration of whether it may be characterized as provisionally justified under the terms of Article XX(g).

126. Paragraph (g) of Article XX covers measures:

relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption;

I. "Exhaustible Natural Resources"

127. We begin with the threshold question of whether Section 609 is a measure concerned with the conservation of "exhaustible natural resources" within the meaning of Article XX(g). The Panel, of

⁹⁷Adopted 30 July 1997, WT/DS31/AB/R, pp. 23 and 24.

⁹⁸Adopted 20 May 1996, WT/DS2/AB/R, pp. 19 ff.

⁹⁹Additional submission of the United States, dated 17 August, 1998, para. 5.

course, with its "chapeau-down" approach, did not make a finding on whether the sea turtles that Section 609 is designed to conserve constitute "exhaustible natural resources" for purposes of Article XX(g). In the proceedings before the Panel, however, the parties to the dispute argued this issue vigorously and extensively. India, Pakistan and Thailand contended that a "reasonable interpretation" of the term "exhaustible" is that the term refers to "finite resources such as minerals, rather than biological or renewable resources."¹⁰⁰ In their view, such finite resources were exhaustible "because there was a limited supply which could and would be depleted unit for unit as the resources were consumed."¹⁰¹ Moreover, they argued, if "all" natural resources were considered to be exhaustible, the term "exhaustible" would become superfluous.¹⁰² They also referred to the drafting history of Article XX(g), and, in particular, to the mention of minerals, such as manganese, in the context of arguments made by some delegations that "export restrictions" should be permitted for the preservation of scarce natural resources.¹⁰³ For its part, Malaysia added that sea turtles, being living creatures, could only be considered under Article XX(b), since Article XX(g) was meant for "nonliving exhaustible natural resources".¹⁰⁴ It followed, according to Malaysia, that the United States cannot invoke both the Article XX(b) and the Article XX(g) exceptions simultaneously.¹⁰⁵

128. We are not convinced by these arguments. Textually, Article XX(g) is *not* limited to the conservation of "mineral" or "non-living" natural resources. The complainants' principal argument is rooted in the notion that "living" natural resources are "renewable" and therefore cannot be "exhaustible" natural resources. We do not believe that "exhaustible" natural resources and "renewable" natural resources are mutually exclusive. One lesson that modern biological sciences teach us is that living species, though in principle, capable of reproduction and, in that sense, "renewable", are in certain circumstances indeed susceptible of depletion, exhaustion and extinction, frequently because of human activities. Living resources are just as "finite" as petroleum, iron ore and other non-living resources.¹⁰⁶

¹⁰⁰Panel Report, para. 3.237.

¹⁰¹*Ibid.*

¹⁰²*Ibid.*

¹⁰³Panel Report, para 3.238. India, Pakistan and Thailand referred, *inter alia*, to E/PC/T/C.II/QR/PV/5, 18 November 1946, p. 79.

¹⁰⁴Panel Report, para. 3.240.

¹⁰⁵*Ibid.*

¹⁰⁶We note, for example, that the World Commission on Environment and Development stated: "The planet's species are under stress. There is growing scientific consensus that species are disappearing at rates never before witnessed on the planet" World Commission on Environment and Development, *Our Common Future* (Oxford University Press, 1987), p. 13.

129. The words of Article XX(g), "exhaustible natural resources", were actually crafted more than 50 years ago. They must be read by a treaty interpreter in the light of contemporary concerns of the community of nations about the protection and conservation of the environment. While Article XX was not modified in the Uruguay Round, the preamble attached to the *WTO Agreement* shows that the signatories to that Agreement were, in 1994, fully aware of the importance and legitimacy of environmental protection as a goal of national and international policy. The preamble of the *WTO Agreement* -- which informs not only the GATT 1994, but also the other covered agreements -- explicitly acknowledges "the objective of *sustainable development*"¹⁰⁷n:

The *Parties* to this Agreement,

Recognizing that their relations in the field of trade and economic endeavour should be conducted *with a view to raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, and expanding the production of and trade in goods and services, while allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development, ...*¹⁰⁸ (emphasis added)

130. From the perspective embodied in the preamble of the *WTO Agreement*, we note that the generic term "natural resources" in Article XX(g) is not "static" in its content or reference but is rather "by definition, evolutionary".¹⁰⁹ It is, therefore, pertinent to note that modern international conventions and declarations make frequent references to natural resources as embracing both living and non-living resources. For instance, the 1982 United Nations Convention on the Law of the

¹⁰⁷This concept has been generally accepted as integrating economic and social development and environmental protection. See e.g., G. Handl, "Sustainable Development: General Rules versus Specific Obligations", in *Sustainable Development and International Law* (ed. W. Lang, 1995), p. 35; World Commission on Environment and Development, *Our Common Future* (Oxford University Press, 1987), p. 43.

¹⁰⁸Preamble of the *WTO Agreement*.

¹⁰⁹See *Namibia (Legal Consequences) Advisory Opinion* (1971) I.C.J. Rep., p. 31. The International Court of Justice stated that where concepts embodied in a treaty are "by definition, evolutionary", their interpretation cannot remain unaffected by the subsequent development of law ... Moreover, an international instrument has to be interpreted and applied within the framework of the entire legal system prevailing at the time of the interpretation." See also *Ageean Sea Continental Shelf Case*, (1978) I.C.J. Rep., p. 3; Jennings and Watts (eds.), *Oppenheim's International Law*, 9th ed., Vol. I (Longman's, 1992), p. 1282 and E. Jimenez de Arechaga, "International Law in the Past Third of a Century", (1978-1) 159 *Recueil des Cours* I, p. 49.

Sea¹¹⁰ ("UNCLOS"), in defining the jurisdictional rights of coastal states in their exclusive economic zones, provides:

Article 56

Rights, jurisdiction and duties of the coastal State in the exclusive economic zone

1. In the exclusive economic zone, the coastal State has:
 - (a) sovereign rights for the purpose of exploring and exploiting, conserving and managing the *natural resources, whether living or non-living, of the waters superjacent to the sea-bed and of the sea-bed and its subsoil, ...* (emphasis added)

The UNCLOS also repeatedly refers in Articles 61 and 62 to "living resources" in specifying rights and duties of states in their exclusive economic zones. The Convention on Biological Diversity¹¹¹ uses the concept of "biological resources". Agenda 21¹¹² speaks most broadly of "natural resources" and goes into detailed statements about "marine living resources". In addition, the Resolution on Assistance to Developing Countries, adopted in conjunction with the Convention on the Conservation of Migratory Species of Wild Animals, recites:

Conscious that an important element of development lies in the conservation and management of *living natural resources* and that migratory species constitute a significant part of these resources;
...¹¹³ (emphasis added)

¹¹⁰Done at Montego Bay, 10 December 1982, UN Doc. A/CONF.62/122; 21 International Legal Materials 1261. We note that India, Malaysia and Pakistan have ratified the UNCLOS. Thailand has signed, but not ratified the Convention, and the United States has not signed the Convention. In the oral hearing, the United States stated: "... we have not ratified this Convention although, with respect to fisheries law, for the most part we do believe that UNCLOS reflects international customary law." Also see, for example, W. Burke, *The New International Law of Fisheries* (Clarendon Press, 1994), p. 40.

[the] coastal state sovereign rights over fisheries in a 200-mile zone are now considered part of customary international law. The evidence of state practice supporting this derives not only from the large number of coastal states claiming an EEZ [exclusive economic zone] in which such rights are advanced, but also from the fact that many of those states not claiming an EEZ assert rights not appreciably different than those in an EEZ. The provision for sovereign rights of the coastal state in [Article 56.1(a) of] the 1982 Convention is also a part of this evidence, but has particular weight because of the uniformity of state practice outside the Convention.

¹¹¹Done at Rio de Janeiro, 5 June 1992, UNEP/Bio.Div./N7-INC/5/4; 31 International Legal Materials 818. We note that India, Malaysia and Pakistan have ratified the Convention on Biological Diversity, and that Thailand and the United States have signed but not ratified the Convention.

¹¹²Adopted by the United Nations Conference on Environment and Development, 14 June 1992, UN Doc. A/CONF.151/26/Rev.1. See, for example, para. 17.70, ff.

¹¹³Final Act of the Conference to Conclude a Convention on the Conservation of Migratory Species of Wild Animals, done at Bonn, 23 June 1979, 19 International Legal Materials 11, p. 15. We note that India and Pakistan have ratified the Convention on the Conservation of Migratory Species of Wild Animals, but that Malaysia, Thailand and the United States are not parties to the Convention.

131. Given the recent acknowledgement by the international community of the importance of concerted bilateral or multilateral action to protect living natural resources, and recalling the explicit recognition by WTO Members of the objective of sustainable development in the preamble of the *WTO Agreement*, we believe it is too late in the day to suppose that Article XX(g) of the GATT 1994 may be read as referring only to the conservation of exhaustible mineral or other non-living natural resources.¹¹⁴ Moreover, two adopted GATT 1947 panel reports previously found fish to be an "exhaustible natural resource" within the meaning of Article XX(g).¹¹⁵ We hold that, in line with the principle of effectiveness in treaty interpretation¹¹⁶, measures to conserve exhaustible natural resources, whether *living* or *non-living*, may fall within Article XX(g).

132. We turn next to the issue of whether the living natural resources sought to be conserved by the measure are "exhaustible" under Article XX(g). That this element is present in respect of the five species of sea turtles here involved appears to be conceded by all the participants and third participants in this case. The exhaustibility of sea turtles would in fact have been very difficult to controvert since all of the seven recognized species of sea turtles are today listed in Appendix 1 of the Convention on International Trade in Endangered Species of Wild Fauna and Flora ("CITES"). The list in Appendix 1 includes "all species *threatened with extinction* which are or may be affected by trade."¹¹⁷(emphasis added)

133. Finally, we observe that sea turtles are highly migratory animals, passing in and out of waters subject to the rights of jurisdiction of various coastal states and the high seas. In the Panel Report, the Panel said:

¹¹⁴Furthermore, the drafting history does not demonstrate an intent on the part of the framers of the GATT 1947 to exclude "living" natural resources from the scope of application of Article XX(g).

¹¹⁵*United States – Prohibition of Imports of Tuna and Tuna Products from Canada*, adopted 22 February 1982, BISD 29S/91, para. 4.9; *Canada – Measures Affecting Exports of Unprocessed Herring and Salmon*, adopted 22 March 1988, BISD 35S/98, para. 4.4.

¹¹⁶See the following Appellate Body Reports: *United States – Gasoline*, adopted 20 May 1996, WT/DS2/AB/R, p. 23; *Japan – Taxes on Alcoholic Beverages*, adopted 1 November 1996, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, p. 12; and *United States – Restrictions on Imports of Cotton and Man-made Fibre Underwear*, adopted 25 February 1997, WT/DS24/AB/R, p. 16. See also Jennings and Watts (eds.), *Oppenheim's International Law*, 9th ed., Vol. 1 (Longman's, 1992), pp. 1280-1281; M.S. McDougal, H.D. Lasswell and J. Miller, *The Interpretation of International Agreements and World Public Order: Principles of Content and Procedure* (New Haven/Martinus Nijhoff, 1994), p. 184; I. Sinclair, *The Vienna Convention on the Law of Treaties*, 2nd ed. (Manchester University Press, 1984), p. 118; D. Carreau, *Droit International* (Editions A. Pedone, 1994), para. 369; P. Daillier and A. Pellet, *Droit International Public*, 5th ed. (L.G.D.J., 1994), para. 172; L.A. Podesta Costa and J.M. Ruda, *Derecho Internacional Público* (Tipografica Editora Argentina, 1985), pp. 109-110 and M. Diez de Velasco, *Instituciones de Derecho Internacional Público*, 11th ed. (Tecnos, 1997), p. 169.

¹¹⁷CITES, Article II.1.

... Information brought to the attention of the Panel, including documented statements from the experts, tends to confirm the fact that sea turtles, in certain circumstances of their lives, migrate through the waters of several countries and the high sea. ...¹¹⁸ (emphasis added)

The sea turtle species here at stake, i.e., covered by Section 609, are all known to occur in waters over which the United States exercises jurisdiction.¹¹⁹ Of course, it is not claimed that all populations of these species migrate to, or traverse, at one time or another, waters subject to United States jurisdiction. Neither the appellant nor any of the appellees claims any rights of exclusive ownership over the sea turtles, at least not while they are swimming freely in their natural habitat -- the oceans. We do not pass upon the question of whether there is an implied jurisdictional limitation in Article XX(g), and if so, the nature or extent of that limitation. We note only that in the specific circumstances of the case before us, there is a sufficient nexus between the migratory and endangered marine populations involved and the United States for purposes of Article XX(g).

134. For all the foregoing reasons, we find that the sea turtles here involved constitute "exhaustible natural resources" for purposes of Article XX(g) of the GATT 1994.

2. "Relating to the Conservation of Exhaustible Natural Resources"

135. Article XX(g) requires that the measure sought to be justified be one which "relat[es] to" the conservation of exhaustible natural resources. In making this determination, the treaty interpreter essentially looks into the relationship between the measure at stake and the legitimate policy of conserving exhaustible natural resources. It is well to bear in mind that the policy of protecting and conserving the endangered sea turtles here involved is shared by all participants and third participants in this appeal, indeed, by the vast majority of the nations of the world.¹²⁰ None of the parties to this dispute question the genuineness of the commitment of the others to that policy.¹²¹

136. In *United States – Gasoline*, we inquired into the relationship between the baseline establishment rules of the United States Environmental Protection Agency (the "EPA") and the

¹¹⁸Panel Report, para. 7.53.

¹¹⁹See Panel Report, para. 2.6. The 1987 Regulations, 52 Fed. Reg. 24244, 29 June 1987, identified five species of sea turtles as occurring within the areas concerned and thus falling under the regulations: loggerhead (*Caretta caretta*), Kemp's ridley (*Lepidochelys kempi*), green (*Chelonia mydas*), leatherback (*Dermochelys coriacea*) and hawksbill (*Ereimochelys imbricata*). Section 609 refers to "those species of sea turtles the conservation of which is the subject of regulations promulgated by the Secretary of Commerce on 29 June, 1987."

¹²⁰There are currently 144 states parties to CITES.

¹²¹We note that all of the participants in this appeal are parties to CITES.

conservation of natural resources for the purposes of Article XX(g). There, we answered in the affirmative the question posed before the panel of whether the baseline establishment rules were "primarily aimed at" the conservation of clean air.¹²² We held that:

... The baseline establishment rules whether individual or statutory, were designed to permit scrutiny and monitoring of the level of compliance of refiners, importers and blenders with the "non-degradation" requirements. Without baselines of some kind, such scrutiny would not be possible and the Gasoline Rule's objective of stabilizing and preventing further deterioration of the level of air pollution prevailing in 1990, would be substantially frustrated. ... We consider that, given that substantial relationship, the baseline establishment rules cannot be regarded as merely incidentally or inadvertently aimed at the conservation of clean air in the United States for the purposes of Article XX(g).¹²³

The substantial relationship we found there between the EPA baseline establishment rules and the conservation of clean air in the United States was a close and genuine relationship of ends and means.

137. In the present case, we must examine the relationship between the general structure and design of the measure here at stake, Section 609, and the policy goal it purports to serve, that is, the conservation of sea turtles.

138. Section 609(b)(1) imposes an import ban on shrimp that have been harvested with commercial fishing technology which may adversely affect sea turtles. This provision is designed to influence countries to adopt national regulatory programs requiring the use of TEDs by their shrimp fishermen. In this connection, it is important to note that the general structure and design of Section 609 *cum* implementing guidelines is fairly narrowly focused. There are two basic exemptions from the import ban, both of which relate clearly and directly to the policy goal of conserving sea turtles. First, Section 609, as elaborated in the 1996 Guidelines, excludes from the import ban shrimp harvested "under conditions that do not adversely affect sea turtles". Thus, the measure, by its terms, excludes from the import ban: aquaculture shrimp; shrimp species (such as *pandalid* shrimp) harvested in water areas where sea turtles do not normally occur; and shrimp harvested exclusively by artisanal methods, even from non-certified countries.¹²⁴ The harvesting of such shrimp clearly does not affect sea turtles. Second, under Section 609(b)(2), the measure exempts from the import ban shrimp caught in waters subject to the jurisdiction of certified countries.

¹²² Adopted 20 May 1996, WT/DS2/AB/R, p. 19.

¹²³ *Ibid.*

¹²⁴ See the 1996 Guidelines, p. 17343.

139. There are two types of certification for countries under Section 609(b)(2). First, under Section 609(b)(2)(C), a country may be certified as having a fishing environment that does not pose a threat of incidental taking of sea turtles in the course of commercial shrimp trawl harvesting. There is no risk, or only a negligible risk, that sea turtles will be harmed by shrimp trawling in such an environment.

140. The second type of certification is provided by Section 609(b)(2)(A) and (B). Under these provisions, as further elaborated in the 1996 Guidelines, a country wishing to export shrimp to the United States is required to adopt a regulatory program that is comparable to that of the United States program and to have a rate of incidental take of sea turtles that is comparable to the average rate of United States' vessels. This is, essentially, a requirement that a country adopt a regulatory program requiring the use of TEDs by commercial shrimp trawling vessels in areas where there is a likelihood of intercepting sea turtles.¹²⁵ This requirement is, in our view, directly connected with the policy of conservation of sea turtles. It is undisputed among the participants, and recognized by the experts consulted by the Panel¹²⁶, that the harvesting of shrimp by commercial shrimp trawling vessels with mechanical retrieval devices in waters where shrimp and sea turtles coincide is a significant cause of sea turtle mortality. Moreover, the Panel did "not question ... the fact generally acknowledged by the experts that TEDs, when properly installed and adapted to the local area, would be an effective tool for the preservation of sea turtles."¹²⁷

141. In its general design and structure, therefore, Section 609 is not a simple, blanket prohibition of the importation of shrimp imposed without regard to the consequences (or lack thereof) of the mode of harvesting employed upon the incidental capture and mortality of sea turtles. Focusing on the design of the measure here at stake¹²⁸, it appears to us that Section 609, *cum* implementing guidelines, is not disproportionately wide in its scope and reach in relation to the policy objective of protection and conservation of sea turtle species. The means are, in principle, reasonably related to the ends. The means and ends relationship between Section 609 and the legitimate policy of conserving an exhaustible, and, in fact, endangered species, is observably a close and real one, a relationship that is every bit as substantial as that which we found in *United States - Gasoline* between the EPA baseline establishment rules and the conservation of clean air in the United States.

¹²⁵ See the 1996 Guidelines, p. 17343.

¹²⁶ For example, Panel Report, paras. 5.91-5.118.

¹²⁷ Panel Report, para. 7.60, footnote 674.

¹²⁸ We focus on the *application* of the measure below, in Section VI.C of this Report.

142. In our view, therefore, Section 609 is a measure "relating to" the conservation of an exhaustible natural resource within the meaning of Article XX(g) of the GATT 1994.

3. "If Such Measures are Made Effective in conjunction with Restrictions on Domestic Production or Consumption"

143. In *United States – Gasoline*, we held that the above-captioned clause of Article XX(g),

... is appropriately read as a requirement that the measures concerned impose restrictions, not just in respect of imported gasoline but also with respect to domestic gasoline. The clause is a requirement of *even-handedness* in the imposition of restrictions, in the name of conservation, upon the production or consumption of exhaustible natural resources.¹²⁹

In this case, we need to examine whether the restrictions imposed by Section 609 with respect to imported shrimp are also imposed in respect of shrimp caught by United States shrimp trawl vessels.

144. We earlier noted that Section 609, enacted in 1989, addresses the mode of harvesting of imported shrimp only. However, two years earlier, in 1987, the United States issued regulations pursuant to the Endangered Species Act requiring all United States shrimp trawl vessels to use approved TEDs, or to restrict the duration of tow-times, in specified areas where there was significant incidental mortality of sea turtles in shrimp trawls.¹³⁰ These regulations became fully effective in 1990 and were later modified. They now require United States shrimp trawlers to use approved TEDs "in areas and at times when there is a likelihood of intercepting sea turtles"¹³¹, with certain limited exceptions.¹³² Penalties for violation of the Endangered Species Act, or the regulations issued thereunder, include civil and criminal sanctions.¹³³ The United States government currently relies on monetary sanctions and civil penalties for enforcement.¹³⁴ The government has the ability to seize

¹²⁹ Adopted 20 May 1996, WT/DS2/AB/R, pp. 20-21.

¹³⁰ 52 Fed. Reg. 24244, 29 June 1987.

¹³¹ See the 1996 Guidelines, p. 17343.

¹³² According to the 1996 Guidelines, p. 17343, the exceptions are: vessels equipped exclusively with certain special types of gear; vessels whose nets are retrieved exclusively by manual rather than mechanical means; and, in exceptional circumstances, where the National Marine Fisheries Service determines that the use of TEDs would be impracticable because of special environmental conditions, vessels are permitted to restrict tow-times instead of using TEDs.

¹³³ Endangered Species Act, Section 11.

¹³⁴ Statement by the United States at the oral hearing.

shrimp catch from trawl vessels fishing in United States waters and has done so in cases of egregious violations.¹³⁵ We believe that, in principle, Section 609 is an even-handed measure.

145. Accordingly, we hold that Section 609 is a measure made effective in conjunction with the restrictions on domestic harvesting of shrimp, as required by Article XX(g).

C. *The Introductory Clauses of Article XX: Characterizing Section 609 under the Chapeau's Standards*

146. As noted earlier, the United States invokes Article XX(b) only if and to the extent that we hold that Section 609 falls outside the scope of Article XX(g). Having found that Section 609 does come within the terms of Article XX(g), it is not, therefore, necessary to analyze the measure in terms of Article XX(b).

147. Although provisionally justified under Article XX(g), Section 609, if it is ultimately to be justified as an exception under Article XX, must also satisfy the requirements of the introductory clauses -- the "chapeau" -- of Article XX, that is,

Article XX

General Exceptions

Subject to the requirement that such measures are *not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade,* nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Member of measures: (emphasis added)

We turn, hence, to the task of appraising Section 609, and specifically the manner in which it is applied under the chapeau of Article XX; that is, to the second part of the two-tier analysis required under Article XX.

I. General Considerations

148. We begin by noting one of the principal arguments made by the United States in its appellant's submission. The United States argues:

¹³⁵ Statement by the United States at the oral hearing.

In context, an alleged "discrimination between countries where the same conditions prevail" is not "unjustifiable" where the policy goal of the Article XX exception being applied provides a rationale for the justification. If, for example, a measure is adopted for the purpose of conserving an exhaustible natural resource under Article XX(g), it is relevant whether the conservation goal justifies the discrimination. In this way, the Article XX chapeau guards against the misuse of the Article XX exceptions for the purpose of achieving indirect protection.¹³⁶

...

[A]n evaluation of whether a measure constitutes "unjustifiable discrimination [between countries] where the same conditions prevail" should take account of whether differing treatment between countries relates to the policy goal of the applicable Article XX exception. If a measure differentiates between countries based on a rationale legitimately connected with the policy of an Article XX exception, rather than for protectionist reasons, the measure does not amount to an abuse of the applicable Article XX exception.¹³⁷ (emphasis added)

149. We believe this argument must be rejected. The policy goal of a measure at issue cannot provide its rationale or justification under the standards of the chapeau of Article XX. The legitimacy of the declared policy objective of the measure, and the relationship of that objective with the measure itself and its general design and structure, are examined under Article XX(g), and the treaty interpreter may then and there declare the measure inconsistent with Article XX(g). If the measure is not held provisionally justified under Article XX(g), it cannot be ultimately justified under the chapeau of Article XX. On the other hand, it does not follow from the fact that a measure falls within the terms of Article XX(g) that that measure also will necessarily comply with the requirements of the chapeau. To accept the argument of the United States would be to disregard the standards established by the chapeau.

150. We commence the second tier of our analysis with an examination of the ordinary meaning of the words of the chapeau. The precise language of the chapeau requires that a measure not be applied in a manner which would constitute a means of "arbitrary or unjustifiable discrimination between countries where the same conditions prevail" or a "disguised restriction on international trade." There are three standards contained in the chapeau: first, arbitrary discrimination between countries where the same conditions prevail; second, unjustifiable discrimination between countries where the same conditions prevail; and third, a disguised restriction on international trade. In order for a measure to

¹³⁶United States appellant's submission, para. 28.

¹³⁷United States appellant's submission, para. 53.

be applied in a manner which would constitute "arbitrary or unjustifiable discrimination between countries where the same conditions prevail", three elements must exist. First, the application of the measure must result in discrimination. As we stated in *United States – Gasoline*, the nature and quality of this discrimination is different from the discrimination in the treatment of products which was already found to be inconsistent with one of the substantive obligations of the GATT 1994, such as Articles I, III or XI.¹³⁸ Second, the discrimination must be *arbitrary or unjustifiable* in character. We will examine this element of *arbitrariness or unjustifiability* in detail below. Third, this discrimination must occur *between countries where the same conditions prevail*. In *United States – Gasoline*, we accepted the assumption of the participants in that appeal that such discrimination could occur not only between different exporting Members, but also between exporting Members and the importing Member concerned.¹³⁹ Thus, the standards embodied in the language of the chapeau are not only different from the requirements of Article XX(g); they are also different from the standard used in determining that Section 609 is violative of the substantive rules of Article XI:1 of the GATT 1994.

151. In *United States – Gasoline*, we stated that "the purpose and object of the introductory clauses of Article XX is generally the prevention of 'abuse of the exceptions of [Article XX]'"¹⁴⁰ We went on to say that:

... The chapeau is animated by the principle that while the exceptions of Article XX may be invoked as a matter of legal right, they should not be so applied as to frustrate or defeat the legal obligations of the holder of the right under the substantive rules of the *General Agreement*. If those exceptions are not to be abused or misused, in other words, the measures falling within the particular exceptions must be applied reasonably, with due regard both to the legal duties of the party claiming the exception and the legal rights of the other parties concerned.¹⁴¹

152. At the end of the Uruguay Round, negotiators fashioned an appropriate preamble for the new *WTO Agreement*, which strengthened the multilateral trading system by establishing an international organization, *inter alia*, to facilitate the implementation, administration and operation, and to further the objectives, of that Agreement and the other agreements resulting from that Round.¹⁴² In

¹³⁸In *United States – Gasoline*, adopted 20 May 1996, WT/DS2/AB/R, p. 23, we stated: "The provisions of the chapeau cannot logically refer to the same standard(s) by which a violation of a substantive rule has been determined to have occurred."

¹³⁹*Ibid.*, pp. 23-24.

¹⁴⁰*Ibid.*, p. 22.

¹⁴¹*Ibid.*

¹⁴²*WTO Agreement*, Article III:1.

recognition of the importance of continuity with the previous GATT system, negotiators used the preamble of the GATT 1947 as the template for the preamble of the new *WTO Agreement*. Those negotiators evidently believed, however, that the objective of "full use of the resources of the world" set forth in the preamble of the GATT 1947 was no longer appropriate to the world trading system of the 1990's. As a result, they decided to qualify the original objectives of the GATT 1947 with the following words:

... while allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development, ...¹⁴³

153. We note once more¹⁴⁴ that this language demonstrates a recognition by WTO negotiators that optimal use of the world's resources should be made in accordance with the objective of sustainable development. As this preamble language reflects the intentions of negotiators of the *WTO Agreement*, we believe it must add colour, texture and shading to our interpretation of the agreements annexed to the *WTO Agreement*, in this case, the GATT 1994. We have already observed that Article XX(g) of the GATT 1994 is appropriately read with the perspective embodied in the above preamble.¹⁴⁵

154. We also note that since this preamble language was negotiated, certain other developments have occurred which help to elucidate the objectives of WTO Members with respect to the relationship between trade and the environment. The most significant, in our view, was the Decision of Ministers at Marrakesh to establish a permanent Committee on Trade and Environment (the "CTE"). In their Decision on Trade and Environment, Ministers expressed their intentions, in part, as follows:

... *Considering* that there should not be, nor need be, any policy contradiction between upholding and safeguarding an open, non-discriminatory and equitable multilateral trading system on the one hand, and acting for the protection of the environment, and the promotion of sustainable development on the other, ...¹⁴⁶

¹⁴³Preamble of the *WTO Agreement*, first paragraph.

¹⁴⁴*Supra*, para. 129.

¹⁴⁵*Supra*, para. 131.

¹⁴⁶Preamble of the Decision on Trade and Environment.

In this Decision, Ministers took "note" of the Rio Declaration on Environment and Development¹⁴⁷, Agenda 21¹⁴⁸, and "its follow-up in the GATT, as reflected in the statement of the Council of Representatives to the CONTRACTING PARTIES at their 48th Session in 1992 ..."¹⁴⁹ We further note that this Decision also set out the following terms of reference for the CTE:

- (a) to identify the relationship between trade measures and environmental measures, in order to promote sustainable development;
- (b) to make appropriate recommendations on whether any modifications of the provisions of the multilateral trading system are required, compatible with the open, equitable and non-discriminatory nature of the system, as regards, in particular:
 - the need for rules to enhance positive interaction between trade and environmental measures, for the promotion of sustainable development, with special consideration to the needs of developing countries, in particular those of the least developed among them; and
 - the avoidance of protectionist trade measures, and the adherence to effective multilateral disciplines to ensure responsiveness of the multilateral trading system to environmental objectives set forth in Agenda 21 and the Rio Declaration, in particular Principle 12; and
 - surveillance of trade measures used for environmental purposes, of trade-related aspects of environmental measures which have significant trade affects, and of effective implementation of the multilateral disciplines governing those measures.¹⁵⁰

155. With these instructions, the General Council of the WTO established the CTE in 1995, and the CTE began its important work. Pending any specific recommendations by the CTE to WTO Members on the issues raised in its terms of reference, and in the absence up to now of any agreed amendments or modifications to the substantive provisions of the GATT 1994 and the *WTO Agreement* generally, we must fulfill our responsibility in this specific case, which is to interpret

¹⁴⁷We note that Principle 3 of the Rio Declaration on Environment and Development states: "The right to development must be fulfilled so as to equitably meet developmental and environmental needs of present and future generations." Principle 4 of the Rio Declaration on Environment and Development states that: "In order to achieve sustainable development, environmental protection shall constitute an integral part of the development process and cannot be considered in isolation from it."

¹⁴⁸Agenda 21 is replete with references to the shared view that economic development and the preservation and protection should be mutually supportive. For example, paragraph 2.3(b) of Agenda 21 states: "The international economy should provide a supportive international climate for achieving environment and development goals by ... [m]aking trade and environment mutually supportive ...". Similarly, paragraph 2.9(d) states that an "objective" of governments should be: "To promote and support policies, domestic and international, that make economic growth and environmental protection mutually supportive."

¹⁴⁹Preamble of the Decision on Trade and Environment.

¹⁵⁰Decision on Trade and Environment.

the existing language of the chapeau of Article XX by examining its ordinary meaning, in light of its context and object and purpose in order to determine whether the United States measure at issue qualifies for justification under Article XX. It is proper for us to take into account, as part of the context of the chapeau, the specific language of the preamble to the *WTO Agreement*, which, we have said, gives colour, texture and shading to the rights and obligations of Members under the *WTO Agreement*, generally, and under the GATT 1994, in particular.

156. Turning then to the chapeau of Article XX, we consider that it embodies the recognition on the part of WTO Members of the need to maintain a balance of rights and obligations between the right of a Member to invoke one or another of the exceptions of Article XX, specified in paragraphs (a) to (j), on the one hand, and the substantive rights of the other Members under the GATT 1994, on the other hand. Exercise by one Member of its right to invoke an exception, such as Article XX(g), if abused or misused, will, to that extent, erode or render naught the substantive treaty rights in, for example, Article XI:1, of other Members. Similarly, because the GATT 1994 itself makes available the exceptions of Article XX, in recognition of the legitimate nature of the policies and interests there embodied, the right to invoke one of those exceptions is not to be rendered illusory. The same concept may be expressed from a slightly different angle of vision, thus, a balance must be struck between the *right* of a Member to invoke an exception under Article XX and the *duty* of that same Member to respect the treaty rights of the other Members. To permit one Member to abuse or misuse its right to invoke an exception would be effectively to allow that Member to degrade its own treaty obligations as well as to devalue the treaty rights of other Members. If the abuse or misuse is sufficiently grave or extensive, the Member, in effect, reduces its treaty obligation to a merely facultative one and dissolves its juridical character, and, in so doing, negates altogether the treaty rights of other Members. The chapeau was installed at the head of the list of "General Exceptions" in Article XX to prevent such far-reaching consequences.

157. In our view, the language of the chapeau makes clear that each of the exceptions in paragraphs (a) to (j) of Article XX is a *limited and conditional* exception from the substantive obligations contained in the other provisions of the GATT 1994, that is to say, the ultimate availability of the exception is subject to the compliance by the invoking Member with the requirements of the chapeau.¹⁵¹ This interpretation of the chapeau is confirmed by its negotiating

¹⁵¹This view is consistent with the approach taken by the panel in *United States – Section 337 of the United States Tariff Act of 1930*, which stated:

Article XX is entitled "General Exceptions" and ... the central phrase in the introductory clause reads: "nothing in this Agreement shall be construed to prevent the adoption or enforcement ... of measures...". Article XX(d) thus provides a *limited and conditional exception from obligations under other provisions*.¹⁵¹ (emphasis added) Adopted 7 November 1989, BISD 36/5/345, para. 5.9.

history.¹⁵² The language initially proposed by the United States in 1946 for the chapeau of what would later become Article XX was unqualified and unconditional.¹⁵³ Several proposals were made during the First Session of the Preparatory Committee of the United Nations Conference on Trade and Employment in 1946 suggesting modifications.¹⁵⁴ In November 1946, the United Kingdom proposed that "in order to prevent abuse of the exceptions of Article 32 [which would subsequently become Article XX]", the chapeau of this provision should be qualified.¹⁵⁵ This proposal was generally accepted, subject to later review of its precise wording. Thus, the negotiating history of Article XX confirms that the paragraphs of Article XX set forth *limited and conditional* exceptions from the obligations of the substantive provisions of the GATT. Any measure, to qualify finally for exception, must also satisfy the requirements of the chapeau. This is a fundamental part of the balance of rights and obligations struck by the original framers of the GATT 1947.

158. The chapeau of Article XX is, in fact, but one expression of the principle of good faith. This principle, at once a general principle of law and a general principle of international law, controls the exercise of rights by states. One application of this general principle, the application widely known as the doctrine of *abus de droit*, prohibits the abusive exercise of a state's rights and enjoins that whenever the assertion of a right "impinges on the field covered by [a] treaty obligation, it must be

¹⁵²Article 32 of the Vienna Convention permits recourse to "supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when interpretation according to article 31: (a) leaves the meaning ambiguous or obscure; or (b) leads to a result which is manifestly absurd or unreasonable." Here, we refer to the negotiating history of Article XX to confirm the interpretation of the chapeau we have reached from applying Article 31 of the Vienna Convention.

¹⁵³The chapeau of Article 32 of the United States Draft Charter for an International Trade Organization, which formed the basis for discussions at the First Session of the Preparatory Committee of the United Nations Conference on Trade and Employment in late 1946, read, in relevant part:

Nothing in Chapter IV of this Charter shall be construed to prevent the adoption or enforcement by any member of measures: ...

¹⁵⁴For example, the Netherlands, Belgium and Luxembourg stated that the exceptions should be qualified in some way:

Indirect protection is an undesirable and dangerous phenomenon. ... Many times, the stipulations to 'protect animal or plant life or health' are misused for indirect protection. It is recommended to insert a clause which prohibits expressly to direct such measures that they constitute an indirect protection or, in general, to use these measures to attain results, which are irreconcilable [*sic*] with the aim of chapters IV, V and VI. E/PC/T/C.II/32, 30 October 1946

¹⁵⁵The United Kingdom's proposed text for the chapeau read:

The undertaking in Chapter IV of this Charter relating to import and export restrictions shall not be construed to prevent the adoption or enforcement by any member of measures for the following purposes, provided that they are not applied in such a manner as to constitute a means of arbitrary discrimination between countries where the same conditions prevail, or a disguised restriction on international trade. E/PC/T/C.II/50, pp. 7 and 9; E/PC/T/C.II/54/Rev.1, 28 November 1946, p. 36.

exercised bona fide, that is to say, reasonably."¹⁵⁶ An abusive exercise by a Member of its own treaty right thus results in a breach of the treaty rights of the other Members and, as well, a violation of the treaty obligation of the Member so acting. Having said this, our task here is to interpret the language of the chapeau, seeking additional interpretative guidance, as appropriate, from the general principles of international law.¹⁵⁷

159. The task of interpreting and applying the chapeau is, hence, essentially the delicate one of locating and marking out a line of equilibrium between the right of a Member to invoke an exception under Article XX and the rights of the other Members under varying substantive provisions (e.g., Article XI) of the GATT 1994, so that neither of the competing rights will cancel out the other and thereby distort and nullify or impair the balance of rights and obligations constructed by the Members themselves in that Agreement. The location of the line of equilibrium, as expressed in the chapeau, is not fixed and unchanging; the line moves as the kind and the shape of the measures at stake vary and as the facts making up specific cases differ.

160. With these general considerations in mind, we address now the issue of whether the application of the United States measure, although the measure itself falls within the terms of Article XX(g), nevertheless constitutes "a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail" or "a disguised restriction on international trade". We address, in other words, whether the application of this measure constitutes an abuse or misuse of the provisional justification made available by Article XX(g). We note, preliminarily, that the application of a measure may be characterized as amounting to an abuse or misuse of an exception of Article XX not only when the detailed operating provisions of the measure prescribe the arbitrary or unjustifiable activity, but also where a measure, otherwise fair and just on its face, is actually applied in an

¹⁵⁶B. Cheng, *General Principles of Law as applied by International Courts and Tribunals* (Stevens and Sons, Ltd., 1953), Chapter 4, in particular, p. 125 elaborates:

... A reasonable and bona fide exercise of a right in such a case is one which is appropriate and necessary for the purpose of the right (*i.e.*, in furtherance of the interests which the right is intended to protect). It should at the same time be *fair and equitable as between the parties* and not one which is calculated to procure for one of them an unfair advantage in the light of the obligation assumed. A reasonable exercise of the right is regarded as compatible with the obligation. But the exercise of the right in such a manner as to prejudice the interests of the other contracting party arising out of the treaty is unreasonable and is considered as inconsistent with the bona fide execution of the treaty obligation, and a breach of the treaty. ... (emphasis added)

Also see, for example, Jennings and Watts (eds.), *Oppenheim's International Law*, 9th ed., Vol. I (Longman's, 1992), pp. 407-410, *Border and Transborder Armed Actions Case*, (1988) I.C.J. Rep. 105; *Rights of Nationals of the United States in Morocco Case*, (1952) I.C.J. Rep. 176; *Anglo-Norwegian Fisheries Case*, (1951) I.C.J. Rep. 142.

¹⁵⁷Vienna Convention, Article 31(3)(c).

arbitrary or unjustifiable manner. The standards of the chapeau, in our view, project both substantive and procedural requirements.

2. "Unjustifiable Discrimination"

161. We scrutinize first whether Section 609 has been applied in a manner constituting "unjustifiable discrimination between countries where the same conditions prevail". Perhaps the most conspicuous flaw in this measure's application relates to its intended and actual coercive effect on the specific policy decisions made by foreign governments, Members of the WTO. Section 609, in its application, is, in effect, an economic embargo which requires *all other exporting Members*, if they wish to exercise their GATT rights, to adopt *essentially the same* policy (together with an approved enforcement program) as that applied to, and enforced on, United States domestic shrimp trawlers. As enacted by the Congress of the United States, the *statutory* provisions of Section 609(b)(2)(A) and (B) do not, in themselves, *require* that other WTO Members adopt *essentially the same* policies and enforcement practices as the United States. Viewed alone, the statute appears to permit a degree of discretion or flexibility in how the standards for determining comparability might be applied, in practice, to other countries.¹⁵⁸ However, any flexibility that may have been intended by Congress when it enacted the statutory provision has been effectively eliminated in the implementation of that policy through the 1996 Guidelines promulgated by the Department of State and through the practice of the administrators in making certification determinations.

162. According to the 1996 Guidelines, certification "shall be made" under Section 609(b)(2)(A) and (B) if an exporting country's program includes a requirement that all commercial shrimp trawl vessels operating in waters in which there is a likelihood of intercepting sea turtles use, at all times, TEDs comparable in effectiveness to those used in the United States.¹⁵⁹ Under these Guidelines, any exceptions to the requirement of the use of TEDs must be comparable to those of the United States

import ban, if:

¹⁵⁸Pursuant to Section 609(b)(2), a harvesting nation may be certified, and thus exempted from the

(A) the government of the harvesting nation has provided documentary evidence of the adoption of a program governing the incidental taking of such sea turtles in the course of such harvesting that is comparable to that of the United States; and

(B) the average rate of that incidental taking by vessels of the harvesting nation is comparable to the average rate of incidental taking of sea turtles by United States vessels in the course of such harvesting...

¹⁵⁹1996 Guidelines, p. 17344.

program.¹⁶⁰ Furthermore, the harvesting country must have in place a "credible enforcement effort".¹⁶¹ The language in the 1996 Guidelines is mandatory: certification "shall be made" if these conditions are fulfilled. However, we understand that these rules are also applied in an *exclusive* manner. That is, the 1996 Guidelines specify the *only* way that a harvesting country's regulatory program can be deemed "comparable" to the United States' program, and, therefore, they define the *only* way that a harvesting nation can be certified under Section 609(b)(2)(A) and (B). Although the 1996 Guidelines state that, in making a comparability determination, the Department of State "shall also take into account other measures the harvesting nation undertakes to protect sea turtles"¹⁶², in practice, the competent government officials only look to see whether there is a regulatory program requiring the use of TEDs or one that comes within one of the extremely limited exceptions available to United States shrimp trawl vessels.¹⁶³

163. The actual *application* of the measure, through the implementation of the 1996 Guidelines and the regulatory practice of administrators, *requires* other WTO Members to adopt a regulatory program that is not merely *comparable*, but rather *essentially the same*, as that applied to the United States shrimp trawl vessels. Thus, the effect of the application of Section 609 is to establish a rigid and unbending standard by which United States officials determine whether or not countries will be certified, thus granting or refusing other countries the right to export shrimp to the United States. Other specific policies and measures that an exporting country may have adopted for the protection and conservation of sea turtles are not taken into account, in practice, by the administrators making the comparability determination.¹⁶⁴

164. We understand that the United States also applies a uniform standard throughout its territory, regardless of the particular conditions existing in certain parts of the country. The United States requires the use of approved TEDs at all times by domestic, commercial shrimp trawl vessels operating in waters where there is any likelihood that they may interact with sea turtles, regardless of the actual incidence of sea turtles in those waters, the species of those sea turtles, or other differences or disparities that may exist in different parts of the United States. It may be quite acceptable for a

¹⁶⁰As already noted, these exceptions are extremely limited and currently include only: vessels equipped exclusively with certain special types of gear; vessels whose nets are retrieved exclusively by manual rather than mechanical means; and, in exceptional circumstances, where the National Marine Fisheries Services determines that the use of TEDs would be impracticable because of special environmental conditions, vessels are permitted to restrict tow-times instead of using TEDs. See the 1996 Guidelines, p. 17343. In the oral hearing, the United States informed us that the exception for restricted tow-times is no longer available.

¹⁶¹1996 Guidelines, p. 17344.

¹⁶²*Ibid.*

¹⁶³Statements by the United States at the oral hearing.

¹⁶⁴Statement by the United States at the oral hearing.

government, in adopting and implementing a domestic policy, to adopt a single standard applicable to all its citizens throughout that country. However, it is not acceptable, in international trade relations, for one WTO Member to use an economic embargo to *require* other Members to adopt essentially the same comprehensive regulatory program, to achieve a certain policy goal, as that in force within that Member's territory, *without* taking into consideration different conditions which may occur in the territories of those other Members.

165. Furthermore, when this dispute was before the Panel and before us, the United States did not permit imports of shrimp harvested by commercial shrimp trawl vessels using TEDs comparable in effectiveness to those required in the United States if those shrimp originated in waters of countries not certified under Section 609. In other words, *shrimp caught using methods identical to those employed in the United States* have been excluded from the United States market solely because they have been caught in waters of *countries that have not been certified by the United States*. The resulting situation is difficult to reconcile with the declared policy objective of protecting and conserving sea turtles. This suggests to us that this measure, in its application, is more concerned with effectively influencing WTO Members to adopt essentially the same comprehensive regulatory regime as that applied by the United States to its domestic shrimp trawlers, even though many of those Members may be differently situated. We believe that discrimination results not only when countries in which the same conditions prevail are differently treated, but also when the application of the measure at issue does not allow for any inquiry into the appropriateness of the regulatory program for the conditions prevailing in those exporting countries.

166. Another aspect of the application of Section 609 that bears heavily in any appraisal of justifiable or unjustifiable discrimination is the failure of the United States to engage the appellees, as well as other Members exporting shrimp to the United States, in serious, across-the-board negotiations with the objective of concluding bilateral or multilateral agreements for the protection and conservation of sea turtles, before enforcing the import prohibition against the shrimp exports of those other Members. The relevant factual finding of the Panel reads:

... However, we have no evidence that the United States actually undertook negotiations on an agreement on sea turtle conservation techniques which would have included the complainants before the imposition of the import ban as a result of the CIT judgement. From the replies of the parties to our question on this subject, in particular that of the United States, we understand that the United States did not propose the negotiation of an agreement to any of the complainants until after the conclusion of negotiations on the Inter-American Convention for the Protection and Conservation of Sea Turtles, in September 1996, i.e. well after the deadline for the imposition of the import ban of 1 May 1996. Even then, it seems that the efforts made merely consisted of an exchange of documents. We therefore conclude that, in spite of the possibility offered by its legislation, the United States did not enter into negotiations before it imposed the import ban. As we consider that the measures sought by the United States were of the type that would normally require international cooperation, we do not find it necessary to examine whether parties entered into negotiations in good faith and whether the United States, absent any result, would have been entitled to adopt unilateral measures.¹⁶⁵ (emphasis added)

167. *A propos* this failure to have prior consistent recourse to diplomacy as an instrument of environmental protection policy, which produces discriminatory impacts on countries exporting shrimp to the United States with which no international agreements are reached or even seriously attempted, a number of points must be made. First, the Congress of the United States expressly recognized the importance of securing international agreements for the protection and conservation of the sea turtle species in enacting this law. Section 609(a) directs the Secretary of State to:

- (1) *initiate negotiations as soon as possible for the development of bilateral or multilateral agreements with other nations for the protection and conservation of such species of sea turtles;*
- (2) *initiate negotiations as soon as possible with all foreign governments which are engaged in, or which have persons or companies engaged in, commercial fishing operations which, as determined by the Secretary of Commerce, may affect adversely such species of sea turtles, for the purpose of entering into bilateral and multilateral treaties with such countries to protect such species of sea turtles;*
- (3) *encourage such other agreements to promote the purposes of this section with other nations for the protection of specific ocean and land regions which are of special significance to the health and stability of such species of sea turtles;*
- (4) *initiate the amendment of any existing international treaty for the protection and conservation of such species of sea turtles to which the United States is a party in order to make such treaty consistent with the purposes and policies of this section;* and

(5) provide to the Congress by not later than one year after the date of enactment of this section: ...

- (C) a full report on:
 - (i) the results of his efforts under this section; ...
 (emphasis added)

Apart from the negotiation of the Inter-American Convention for the Protection and Conservation of Sea Turtles¹⁶⁶ (the "Inter-American Convention") which concluded in 1996, the record before the Panel does not indicate any serious, substantial efforts to carry out these express directions of Congress.¹⁶⁷

168. Second, the protection and conservation of highly migratory species of sea turtles, that is, the very policy objective of the measure, demands concerted and cooperative efforts on the part of the many countries whose waters are traversed in the course of recurrent sea turtle migrations. The need for, and the appropriateness of, such efforts have been recognized in the WTO itself as well as in a significant number of other international instruments and declarations. As stated earlier, the Decision on Trade and Environment, which provided for the establishment of the CTE and set out its terms of reference, refers to both the Rio Declaration on Environment and Development and Agenda 21.¹⁶⁸ Of particular relevance is Principle 12 of the Rio Declaration on Environment and Development, which states, in part:

Unilateral actions to deal with environmental challenges outside the jurisdiction of the importing country should be avoided. *Environmental measures addressing transboundary or global environmental problems should, as far as possible, be based on international consensus.* (emphasis added)

In almost identical language, paragraph 2.22(i) of Agenda 21 provides:

Governments should encourage GATT, UNCTAD and other relevant international and regional economic institutions to examine, in accordance with their respective mandates and competences, the following propositions and principles: ...

- (i) Avoid unilateral action to deal with environmental challenges outside the jurisdiction of the importing country. *Environmental measures addressing transborder problems should, as far as possible, be based on an international consensus.* (emphasis added)

¹⁶⁶First written submission of the United States to the Panel, Exhibit AA.

¹⁶⁷Panel Report, para. 7.56.

¹⁶⁸See Decision on Trade and Environment, preamble and para. 2(b). See *Supra*, para. 154.

conservation and recovery of sea turtle populations and their habitats within such party's land territory and in maritime areas with respect to which it exercises sovereign rights or jurisdiction.¹⁷² Such measures include, notably,

[t]he reduction, to the greatest extent practicable, of the incidental capture, retention, harm or mortality of sea turtles in the course of fishing activities, through the appropriate regulation of such activities, as well as the development, improvement and use of appropriate gear, devices or techniques, including the use of turtle excluder devices (TEDs) pursuant to the provisions of Annex III [of the Convention].¹⁷³

Article XV of the Inter-American Convention also provides, in part:

Article XV
Trade Measures

1. *In implementing this Convention, the Parties shall act in accordance with the provisions of the Agreement establishing the World Trade Organization (WTO), as adopted at Marrakesh in 1994, including its annexes.*
2. *In particular, and with respect to the subject-matter of this Convention, the Parties shall act in accordance with the provisions of the Agreement on Technical Barriers to Trade contained in Annex I of the WTO Agreement, as well as Article XI of the General Agreement on Tariffs and Trade of 1994. ... (emphasis added)*

170. The juxtaposition of (a) the *consensual* undertakings to put in place regulations providing for, *inter alia*, use of TEDs *jointly determined* to be suitable for a particular party's maritime areas, with (b) the reaffirmation of the parties' obligations under the *WTO Agreement*, including the *Agreement on Technical Barriers to Trade* and Article XI of the GATT 1994, suggests that the parties to the Inter-American Convention together marked out the equilibrium line to which we referred earlier. The Inter-American Convention demonstrates the conviction of its signatories, including the United States, that consensual and multilateral procedures are available and feasible for the establishment of programs for the conservation of sea turtles. Moreover, the Inter-American Convention emphasizes the continuing validity and significance of Article XI of the GATT 1994, and of the obligations of the *WTO Agreement* generally, in maintaining the balance of rights and obligations under the *WTO Agreement* among the signatories of that Convention.

¹⁷²Inter-American Convention, Article IV.1.

¹⁷³Inter-American Convention, Article IV.2(h).

Moreover, we note that Article 5 of the Convention on Biological Diversity states:

... each contracting party shall, as far as possible and as appropriate, cooperate with other contracting parties directly or, where appropriate, through competent international organizations, in respect of areas beyond national jurisdiction and on other matters of mutual interest, for the conservation and sustainable use of biological diversity.

The Convention on the Conservation of Migratory Species of Wild Animals, which classifies the relevant species of sea turtles in its Annex I as "Endangered Migratory Species", states:

The contracting parties [are] convinced that conservation and effective management of migratory species of wild animals requires the concerted action of all States within the national boundaries of which such species spend any part of their life cycle.

Furthermore, we note that WTO Members in the Report of the CTE, forming part of the Report of the General Council to Ministers on the occasion of the Singapore Ministerial Conference, endorsed and supported:

... *multilateral solutions based on international cooperation and consensus as the best and most effective way for governments to tackle environmental problems of a transboundary or global nature.* WTO Agreements and multilateral environmental agreements (MEAs) are representative of efforts of the international community to pursue *shared goals*, and in the development of a mutually supportive relationship between them, *due respect must be afforded to both.*¹⁶⁹ (emphasis added)

169. Third, the United States did negotiate and conclude one regional international agreement for the protection and conservation of sea turtles: The Inter-American Convention. This Convention was opened for signature on 1 December 1996 and has been signed by five countries¹⁷⁰, in addition to the United States, and four of these countries are currently certified under Section 609.¹⁷¹ This Convention has not yet been ratified by any of its signatories. The Inter-American Convention provides that each party shall take "appropriate and necessary measures" for the protection,

¹⁶⁹Report (1996) of the Committee on Trade and Environment, WT/CTE/1, 12 November 1996, para. 171, Section VII of the Report of the General Council to the 1996 Ministerial Conference, WT/MIN(96)/2, 26 November 1996.

¹⁷⁰Brazil, Costa Rica, Mexico, Nicaragua and Venezuela.

¹⁷¹As of 1 January 1998, Brazil was among those countries certified as having adopted programs to reduce the incidental capture of sea turtles in shrimp fisheries comparable to the United States' program. See Panel Report, para. 2.16. However, according to information provided by the United States at the oral hearing, Brazil is not currently certified under Section 609.

171. The Inter-American Convention thus provides convincing demonstration that an alternative course of action was reasonably open to the United States for securing the legitimate policy goal of its measure, a course of action other than the unilateral and non-consensual procedures of the import prohibition under Section 609. It is relevant to observe that an import prohibition is, ordinarily, the heaviest "weapon" in a Member's armoury of trade measures. The record does not, however, show that serious efforts were made by the United States to negotiate similar agreements with any other country or group of countries before (and, as far as the record shows, after) Section 609 was enforced on a world-wide basis on 1 May 1996. Finally, the record also does not show that the appellant, the United States, attempted to have recourse to such international mechanisms as exist to achieve cooperative efforts to protect and conserve sea turtles¹⁷⁴ before imposing the import ban.

172. Clearly, the United States negotiated seriously with some, but not with other Members (including the appellees), that export shrimp to the United States. The effect is plainly discriminatory and, in our view, unjustifiable. The unjustifiable nature of this discrimination emerges clearly when we consider the cumulative effects of the failure of the United States to pursue negotiations for establishing consensual means of protection and conservation of the living marine resources here involved, notwithstanding the explicit statutory direction in Section 609 itself to initiate negotiations as soon as possible for the development of bilateral and multilateral agreements.¹⁷⁵ The principal consequence of this failure may be seen in the resulting unilateralism evident in the application of Section 609. As we have emphasized earlier, the policies relating to the necessity for use of particular kinds of TEDs in various maritime areas, and the operating details of these policies, are all shaped by the Department of State, without the participation of the exporting Members. The system and processes of certification are established and administered by the United States agencies alone. The decision-making involved in the grant, denial or withdrawal of certification to the exporting Members, is, accordingly, also unilateral. The unilateral character of the application of Section 609 heightens the disruptive and discriminatory influence of the import prohibition and underscores its unjustifiability.

173. The application of Section 609, through the implementing guidelines together with administrative practice, also resulted in other differential treatment among various countries desiring certification. Under the 1991 and 1993 Guidelines, to be certifiable, fourteen countries in the wider

¹⁷⁴While the United States is a party to CITES, it did not make any attempt to raise the issue of sea turtle mortality due to shrimp trawling in the CITES Standing Committee as a subject requiring concerted action by states. In this context, we note that the United States, for example, has not signed the Convention on the Conservation of Migratory Species of Wild Animals or UNCLOS, and has not ratified the Convention on Biological Diversity.

¹⁷⁵Section 609(a).

Caribbean/western Atlantic region had to commit themselves to require the use of TEDs on all commercial shrimp trawling vessels by 1 May 1994. These fourteen countries had a "phase-in" period of three years during which their respective shrimp trawling sectors could adjust to the requirement of the use of TEDs. With respect to all other countries exporting shrimp to the United States (including the appellees, India, Malaysia, Pakistan and Thailand), on 29 December 1995, the United States Court of International Trade directed the Department of State to apply the import ban on a world-wide basis not later than 1 May 1996.¹⁷⁶ On 19 April 1996, the 1996 Guidelines were issued by the Department of State bringing shrimp harvested in *all* foreign countries within the scope of Section 609, effective 1 May 1996. Thus, all countries that were not among the fourteen in the wider Caribbean/western Atlantic region had only four months to implement the requirement of compulsory use of TEDs. We acknowledge that the greatly differing periods for putting into operation the requirement for use of TEDs resulted from decisions of the Court of International Trade. Even so, this does not relieve the United States of the legal consequences of the discriminatory impact of the decisions of that Court. The United States, like all other Members of the WTO and of the general community of states, bears responsibility for acts of all its departments of government, including its judiciary.¹⁷⁷

174. The length of the "phase-in" period is not inconsequential for exporting countries desiring certification. That period relates directly to the onerousness of the burdens of complying with the requisites of certification and the practical feasibility of locating and developing alternative export markets for shrimp. The shorter that period, the heavier the burdens of compliance, particularly where an applicant has a large number of trawler vessels, and the greater the difficulties of re-orienting the harvesting country's shrimp exports. The shorter that period, in net effect, the heavier the influence of the import ban. The United States sought to explain the marked difference between "phase-in" periods granted to the fourteen wider Caribbean/western Atlantic countries and those allowed the rest of the shrimp exporting countries. The United States asserted that the longer time-period was justified by the then undeveloped character of TED technology, while the shorter period was later made possible by the improvements in that technology. This explanation is less than persuasive, for it does not address the administrative and financial costs and the difficulties of governments in putting together and enacting the necessary regulatory programs and "credible

¹⁷⁶*Earth Island Institute v. Warren Christopher*, 913 F. Supp. 559 (CIT 1995).

¹⁷⁷See *United States - Gasoline*, adopted 20 May 1996, WT/DS2/AB/R, p. 28. Also see, for example, Jennings and Watts (eds.), *Oppenheim's International Law*, 9th ed., Vol. I (Longman's 1992), p. 545; and I. Brownlie, *Principles of Public International Law*, 4th ed. (Clarendon Press, 1990), p. 450.

enforcement effort", and in implementing the compulsory use of TEDs on hundreds, if not thousands, of shrimp trawl vessels.¹⁷⁸

175. Differing treatment of different countries desiring certification is also observable in the differences in the levels of effort made by the United States in transferring the required TED technology to specific countries. Far greater efforts to transfer that technology successfully were made to certain exporting countries -- basically the fourteen wider Caribbean/western Atlantic countries cited earlier -- than to other exporting countries, including the appellees.¹⁷⁹ The level of these efforts is probably related to the length of the "phase-in" periods granted -- the longer the "phase-in" period, the higher the possible level of efforts at technology transfer. Because compliance with the requirements of certification realistically assumes successful TED technology transfer, low or merely nominal efforts at achieving that transfer will, in all probability, result in fewer countries being able to satisfy the certification requirements under Section 609, within the very limited "phase-in" periods allowed them.

176. When the foregoing differences in the means of application of Section 609 to various shrimp exporting countries are considered in their cumulative effect, we find, and so hold, that those differences in treatment constitute "unjustifiable discrimination" between exporting countries desiring certification in order to gain access to the United States shrimp market within the meaning of the chapeau of Article XX.

3. "Arbitrary Discrimination"

177. We next consider whether Section 609 has been applied in a manner constituting "arbitrary discrimination between countries where the same conditions prevail". We have already observed that Section 609, in its application, imposes a single, rigid and unbending requirement that countries applying for certification under Section 609(b)(2)(A) and (B) adopt a comprehensive regulatory program that is essentially the same as the United States' program, without inquiring into the appropriateness of that program for the conditions prevailing in the exporting countries.¹⁸⁰ Furthermore, there is little or no flexibility in how officials make the determination for certification

pursuant to these provisions.¹⁸¹ In our view, this rigidity and inflexibility also constitute "arbitrary discrimination" within the meaning of the chapeau.

178. Moreover, the description of the administration of Section 609 provided by the United States in the course of these proceedings highlights certain problematic aspects of the certification processes applied under Section 609(b). With respect to the first type of certification, under Section 609(b)(2)(A) and (B), the 1996 Guidelines set out certain elements of the procedures for acquiring certification, including the requirement to submit documentary evidence of the regulatory program adopted by the applicant country. This certification process also generally includes a visit by United States officials to the applicant country.¹⁸²

179. With respect to certifications under Section 609(b)(2)(C), the 1996 Guidelines state that the Department of State "shall certify" any harvesting nation under Section 609(b)(2)(C) if it meets the criteria in the 1996 Guidelines "without the need for action on the part of the government of the harvesting nation ...".¹⁸³ Nevertheless, the United States informed us that, in all cases where a country has not previously been certified under Section 609, it waits for an application to be made before making a determination on certification.¹⁸⁴ In the case of certifications under Section 609(b)(2)(C), there appear to be certain opportunities for the submission of written evidence, such as scientific documentation, in the course of the certification process.¹⁸⁵

180. However, with respect to neither type of certification under Section 609(b)(2) is there a transparent, predictable certification process that is followed by the competent United States government officials. The certification processes under Section 609 consist principally of administrative *ex parte* inquiry or verification by staff of the Office of Marine Conservation in the Department of State with staff of the United States National Marine Fisheries Service.¹⁸⁶ With respect to both types of certification, there is no formal opportunity for an applicant country to be heard, or to respond to any arguments that may be made against it, in the course of the certification process before a decision to grant or to deny certification is made. Moreover, no formal written,

¹⁸¹In the oral hearing, the United States stated that "as a policy matter, the United States government believes that all governments should require the use of turtle excluder devices on all shrimp trawler boats that operate in areas where there is a likelihood of intercepting sea turtles" and that "when it comes to shrimp trawling, we know of only one way of effectively protecting sea turtles, and that is through TEDs."

¹⁸²Statement by the United States at the oral hearing.

¹⁸³1996 Guidelines, p. 17343.

¹⁸⁴Statement by the United States at the oral hearing.

¹⁸⁵Statement by the United States at the oral hearing.

¹⁸⁶Statement by the United States at the oral hearing.

¹⁷⁸For example, at the oral hearing, India stated that its "number of mechanized nets is estimated at about 47,000. Most of these are mechanized vessels ..."

¹⁷⁹Response by the United States to questioning by the Panel; statements by the United States at the oral hearing.

¹⁸⁰*Supra*, paras. 161-164.

reasoned decision, whether of acceptance or rejection, is rendered on applications for either type of certification, whether under Section 609(b)(2)(A) and (B) or under Section 609(b)(2)(C).¹⁸⁷ Countries which are granted certification are included in a list of approved applications published in the Federal Register; however, they are not notified specifically. Countries whose applications are denied¹⁸⁸ also do not receive notice of such denial (other than by omission from the list of approved applications) or of the reasons for the denial.¹⁸⁹ No procedure for review of, or appeal from, a denial of an application is provided.¹⁹⁰

181. The certification processes followed by the United States thus appear to be singularly informal and casual, and to be conducted in a manner such that these processes could result in the negation of rights of Members. There appears to be no way that exporting Members can be certain whether the terms of Section 609, in particular, the 1996 Guidelines, are being applied in a fair and just manner by the appropriate governmental agencies of the United States. It appears to us that, effectively, exporting Members applying for certification whose applications are rejected are denied basic fairness and due process, and are discriminated against, *vis-à-vis* those Members which are granted certification.

182. The provisions of Article X:3¹⁹¹ of the GATT 1994 bear upon this matter. In our view, Section 609 falls within the "laws, regulations, judicial decisions and administrative rulings of general application" described in Article X:1. Inasmuch as there are due process requirements generally for measures that are otherwise imposed in compliance with WTO obligations, it is only reasonable that rigorous compliance with the fundamental requirements of due process should be required in the application and administration of a measure which purports to be an exception to the treaty obligations of the Member imposing the measure and which effectively results in a suspension *pro hac vice* of the treaty rights of other Members.

¹⁸⁷Statement by the United States at the oral hearing.

¹⁸⁸We were advised at the oral hearing by the United States that these include: Australia, Pakistan and Tunisia.

¹⁸⁹Statement by the United States at the oral hearing.

¹⁹⁰Statement by the United States at the oral hearing.

¹⁹¹Article X:3 states, in part:

(a) Each Member shall administer in a uniform, impartial and reasonable manner all its laws, regulations, decisions and rulings of the kind described in paragraph 1 of this Article.

(b) Each Member shall maintain, or institute as soon as practicable, judicial, arbitral or administrative tribunals or procedures for the purpose, *inter alia*, of the prompt review and correction of administrative action relating to customs matters

....

183. It is also clear to us that Article X:3 of the GATT 1994 establishes certain minimum standards for transparency and procedural fairness in the administration of trade regulations which, in our view, are not met here. The non-transparent and *ex parte* nature of the internal governmental procedures applied by the competent officials in the Office of Marine Conservation, the Department of State, and the United States National Marine Fisheries Service throughout the certification processes under Section 609, as well as the fact that countries whose applications are denied do not receive formal notice of such denial, nor of the reasons for the denial, and the fact, too, that there is no formal legal procedure for review of, or appeal from, a denial of an application, are all contrary to the spirit, if not the letter, of Article X:3 of the GATT 1994.

184. We find, accordingly, that the United States measure is applied in a manner which amounts to a means not just of "unjustifiable discrimination", but also of "arbitrary discrimination" between countries where the same conditions prevail, contrary to the requirements of the chapeau of Article XX. The measure, therefore, is not entitled to the justifying protection of Article XX of the GATT 1994. Having made this finding, it is not necessary for us to examine also whether the United States measure is applied in a manner that constitutes a "disguised restriction on international trade" under the chapeau of Article XX.

185. In reaching these conclusions, we wish to underscore what we have *not* decided in this appeal. We have *not* decided that the protection and preservation of the environment is of no significance to the Members of the WTO. Clearly, it is. We have *not* decided that the sovereign nations that are Members of the WTO cannot adopt effective measures to protect endangered species, such as sea turtles. Clearly, they can and should. And we have *not* decided that sovereign states should not act together bilaterally, plurilaterally or multilaterally, either within the WTO or in other international fora, to protect endangered species or to otherwise protect the environment. Clearly, they should and do.

186. What we *have* decided in this appeal is simply this: although the measure of the United States in dispute in this appeal serves an environmental objective that is recognized as legitimate under paragraph (g) of Article XX of the GATT 1994, this measure has been applied by the United States in a manner which constitutes arbitrary and unjustifiable discrimination between Members of the WTO, contrary to the requirements of the chapeau of Article XX. For all of the specific reasons outlined in this Report, this measure does not qualify for the exemption that Article XX of the GATT 1994 affords to measures which serve certain recognized, legitimate environmental purposes but which, at the same time, are not applied in a manner that constitutes a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail or a disguised restriction on

international trade. As we emphasized in *United States – Gasoline*, WTO Members are free to adopt their own policies aimed at protecting the environment as long as, in so doing, they fulfill their obligations and respect the rights of other Members under the *WTO Agreement*.¹⁹²

Signed in the original at Geneva this 8th day of October 1998 by:

VII. Findings and Conclusions

187. For the reasons set out in this Report, the Appellate Body:

- (a) reverses the Panel's finding that accepting non-requested information from non-governmental sources is incompatible with the provisions of the DSU;
- (b) reverses the Panel's finding that the United States measure at issue is not within the scope of measures permitted under the chapeau of Article XX of the GATT 1994, and
- (c) concludes that the United States measure, while qualifying for provisional justification under Article XX(g), fails to meet the requirements of the chapeau of Article XX, and, therefore, is not justified under Article XX of the GATT 1994.

188. The Appellate Body *recommends* that the DSB request the United States to bring its measure found in the Panel Report to be inconsistent with Article XI of the GATT 1994, and found in this Report to be not justified under Article XX of the GATT 1994, into conformity with the obligations of the United States under that Agreement.

World Trade Organization

**Korea – Measures Affecting Imports of Fresh, Chilled and
Frozen Beef**

Report of the Appellate Body, 11 December 2000

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KOREA – MEASURES AFFECTING IMPORTS OF FRESH,
CHILLED AND FROZEN BEEF

AB-2000-8

Report of the Appellate Body

WORLD TRADE ORGANIZATION
APPELLATE BODY

**Korea – Measures Affecting Imports of
Fresh, Chilled and Frozen Beef**

Korea, *Appellant*
Australia, *Appellee*
United States, *Appellee*
Canada, *Third Participant*
New Zealand, *Third Participant*

AB-2000-8

Present:

Ehlermann, Presiding Member
Abi-Saab, Member
Feliciano, Member

Marketing Organization (the "LPMO") results in quantitative restrictions being applied to grass-fed beef, contrary to Articles II:1, III:4, XI:1 and XVII of the GATT 1994; that discharge procedures for LPMO beef are contrary to Articles III, XI and XVII of the GATT 1994 and Article 4.2 of the *Agreement on Agriculture*; that restrictions on sales of beef imported by the LPMO are contrary to Article III:4 of the GATT 1994; that Korea applies a mark-up on beef imported under the "Simultaneous Buy/Sell" ("SBS") system which is inconsistent with Korea's obligations under Articles II or III of the GATT 1994; that the SBS system applies limitations on the import and distribution of imported beef, and imposes labelling, reporting and record-keeping requirements, that are contrary to Articles III and XI of the GATT 1994; and that, in 1997, Korea provided domestic support to its beef industry which resulted in Korea's Current Total Aggregate Measurement of Support ("AMS") for 1997 being in excess of its reduction commitments for that year, contrary to Articles 3, 6 and 7 of the *Agreement on Agriculture*.³

3. The Panel also considered claims by the United States that Korea's requirement that imported beef be sold only in specialized imported beef stores, and its laws and regulations restricting the resale and distribution of imported beef by SBS super-groups, retailers, customers, and end-users are inconsistent with its obligations under Article III:4 of the GATT 1994; that Korea's discretionary import regime, as well as the LPMO's establishment of minimum import prices and delay of both invitations to tender as well as quota allocations, are inconsistent with its obligations under Article XI:1 of the GATT 1994, Article 4.2 of the *Agreement on Agriculture*, and Articles 1 and 3 of the *Agreement on Import Licensing Procedures*; that Korea's imposition of other duties or charges in the form of a mark-up not provided for in Korea's Schedule LX is inconsistent with its obligations under Article II:1 of the GATT 1994; and that Korea has failed to fulfill its reduction commitment for domestic support for 1997 and 1998, and has, thus, acted inconsistently with its obligations under Articles 3, 6, and 7 of the *Agreement on Agriculture*.⁴

4. The Panel Report was circulated to the Members of the World Trade Organization (the "WTO") on 31 July 2000.

5. The Panel concluded that certain of the measures at issue are included in "the remaining restrictions" within the meaning of Note 6(e) of Korea's Schedule and thus benefit from a transitional period until 1 January 2001, by which date they shall be eliminated or otherwise brought into conformity with the *Marrakesh Agreement Establishing the World Trade Organization* (the "*WTO Agreement*"); that the dual retail system for beef (including the obligation for department

³Panel Report, para. 49.

⁴*Ibid.*, para. 51.

I. Introduction

1. Korea appeals certain issues of law and legal interpretations in the Panel Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef* (the "Panel Report").¹ The Panel was established to consider a complaint by Australia and the United States with respect to Korean measures that affect the importation of certain beef products. The aspects of these measures relevant for this appeal relate to, first, domestic support provided to the beef industry and to the Korean agriculture sector more generally, and, second, the separate retail distribution channels that exist for certain imported and domestic beef products (the so-called "dual retail system") and related measures. The dual retail system is given legal effect by the *Management Guideline for Imported Beef* (the "*Management Guideline*").² The factual aspects of this dispute are described in detail in paragraphs 8 through 29 of the Panel Report.

2. The Panel considered claims by Australia that the requirements imposed on the retail sale of imported beef are contrary to Articles III and XI of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994"); that the tendering process adopted by the Livestock Products

¹WT/DS161/R, WT/DS169/R, 31 July 2000.

²The essential features of the Korean dual retail system for beef are found in the *Guidelines Concerning Registration and Operation of Specialized Imported Beef Stores*, (61550-81) 29 January 1990, modified on 15 March 1994; and the *Regulations Concerning Sales of Imported Beef*, (51550-100), modified on 27 March 1993, 7 April 1994, and 29 June 1998. On 1 October 1999, these two instruments were replaced by the *Management Guideline for Imported Beef*, (Ministry of Agriculture Notice 1999-67), which maintained, however, the basic principles of the dual retail system. The *Management Guideline* is an elaboration of Article 25 of the *Livestock Act (Revised)*, as amended by Act No. 5720 on 29 January 1999.

stores and supermarkets authorized to sell imported beef to hold a separate display, and the obligation for foreign beef shops to bear a sign with the words "Specialized Imported Beef Store" is inconsistent with the provisions of Article III:4 of the GATT 1994 in that it treats imported beef less favourably than domestic beef, and cannot be justified pursuant to Article XX(d) of the GATT 1994; that the requirement that the supply of beef from the LPMO's wholesale market be limited to specialized imported beef stores is inconsistent with Article III:4 of the GATT 1994 and cannot be justified pursuant to Article XX(d) of the GATT 1994; that the imposition of more stringent record-keeping requirements on those who purchase foreign beef imported by the LPMO than on those who purchase domestic beef is inconsistent with Article III:4 of the GATT 1994; that the prohibition against cross-trading between end-users of the SBS system is inconsistent with Article III:4 of the GATT 1994; that any additional labelling requirements imposed on foreign beef imported through the SBS system that are not also imposed on domestic beef, such as the requirement that the end-consumer, the contract number and super-group importer be identified and indicated on the imported beef, are inconsistent with Article III:4 of the GATT 1994; that the LPMO's lack of, and delays in, calling for tenders, and its discharge practices between November 1997 and the end of May 1998, constitute import restrictions on foreign beef, inconsistent with Article XI of the GATT 1994, and the same practices are also inconsistent with Article 4.2 of the *Agreement on Agriculture* and its footnote; that even if the LPMO had not had monopoly rights over the import and distribution of its share of Korea's beef import, the LPMO's lack of, and delays in, calling for tenders during the same period constituted an import restriction inconsistent with Article XI of the GATT 1994 through the application of the Ad Note to Articles XI, XII, XIII, XIV and XVIII of the GATT 1994, and that the LPMO's discharge practices during the same period were inconsistent with Article XVII:1(a) of the GATT 1994; that the LPMO's calls for tenders that are made subject to grass-fed or grain-fed distinctions impose import restrictions inconsistent with Article XI of the GATT 1994, and treat imports of grass-fed beef less favourably than is provided for in Korea's Schedule, contrary to Article II:1(a) of the GATT 1994; that Korea's domestic support for beef for 1997 and 1998 was not correctly calculated and exceeded the *de minimis* level, contrary to Article 6 of the *Agreement on Agriculture*, and was not included in Korea's Current Total AMS, contrary to Article 7.2(a) of the *Agreement on Agriculture*; that Korea's total domestic support (Current Total AMS) for 1997 and 1998 exceeded Korea's commitment levels, as specified in Part IV, Section I of its Schedule, contrary to Article 3.2 of the *Agreement on Agriculture*.⁵

⁵Panel Report, para. 845.

6. The Panel recommended that the Dispute Settlement Body ("DSB") request Korea to bring its measures into conformity with its obligations under the *WTO Agreement*.⁶
7. On 11 September 2000, Korea notified the DSB of its intention to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, pursuant to paragraph 4 of Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), and filed a Notice of Appeal pursuant to Rule 20 of the *Working Procedures for Appellate Review* (the "*Working Procedures*"). On 21 September 2000, Korea filed its appellant's submission.⁷ On 6 October 2000, Australia and the United States⁸ each filed an appellee's submission. On the same day, Canada and New Zealand each filed a third participant's submission.⁹
8. The oral hearing in the appeal was held on 23 and 24 October 2000. The participants and third participants presented oral arguments and responded to questions put to them by the Members of the Division hearing the appeal.

II. Arguments of the Participants and the Third Participants

A. Korea – Appellant

1. Terms of Reference

9. Korea claims that the Panel erred by making two findings that were outside its terms of reference. First, the Panel erred by ruling on Part IV, Section I of Korea's Schedule LX, in particular by considering which set of numbers in Schedule LX constitutes Korea's commitment levels. Neither the United States nor Australia challenged Korea's Schedule LX in their requests for the establishment of a panel. As Schedule LX is not mentioned in these panel requests, the complaining parties have not met the "minimum prerequisite" established by the Appellate Body for panel requests under Article 6.2 of the DSU, that treaty provisions claimed to have been violated must be identified, and, therefore, Korea should be considered *per se* to have suffered prejudice.

10. Second, neither the United States nor Australia, in their panel requests, identified Annex 3 of the *Agreement on Agriculture* as a treaty provision claimed to have been violated in the context of

⁶Panel Report, para. 847.

⁷Pursuant to Rule 21(1) of the *Working Procedures*.

⁸Pursuant to Rule 22 of the *Working Procedures*.

⁹Pursuant to Rule 24 of the *Working Procedures*.

Korea's calculation methodology for domestic support to the cattle industry. Consequently, the Panel acted outside its terms of reference when it ruled that Annex 3 provided the basis for calculating Korea's current domestic support for beef. Further, the complaining parties have not met the "minimum prerequisite" established by the Appellate Body for panel requests under Article 6.2 of the DSU.

2. Domestic Support Under the *Agreement on Agriculture*

11. Korea believes the Panel erred in finding that, by virtue of Articles I(a)(ii) and I(h)(ii) of the *Agreement on Agriculture*, Korea is bound by the provisions of Annex 3 of that Agreement in its calculation of Current AMS for beef, since it did not have any "constituent data and methodology" for beef in its Schedule. The Panel's interpretation of Articles I(a)(ii) and I(h)(ii) leads to an unfair outcome and ignores the object and purpose of the *Agreement on Agriculture*. WTO Members' Schedules on the reduction of subsidies for agricultural products can be understood as multi-year equations. One side of the equation includes the commitment level for a given year, while the other side of the equation includes the actual AMS provided for the same year. Thus, for the equation to be meaningful, both sides of the equation should be based on the same set of data and methodology. Using one methodology for commitment levels and another methodology for actual AMS undermines comparability between the two, and leads to unfair results. All the commitment levels set out in Korea's Schedule and all the actual AMS provided by Korea are calculated on the basis of a consistent methodology, which relies on the base years of 1989-1991 (with an exception for rice) and an "actual purchase" definition of eligible production. However, according to the Panel's ruling, Korea should calculate its Current AMS for beef according to different base years and a different definition of eligible production than was used for calculating commitment levels. Korea argues that this leads to unfair results.

12. Furthermore, Korea contends the Panel's interpretation would frustrate the object and purpose of the *Agreement on Agriculture*, which is, in part, to provide for substantial progressive reduction in agricultural support and protection over an agreed period of time. The Panel's interpretation would make it impossible correctly to determine whether a Member has abided by its reduction commitments or not.

13. Moreover, the Panel's interpretation of Articles I(a)(ii) and I(h)(ii) of the *Agreement on Agriculture* would render inutile important parts of these provisions. If the calculation methods of Annex 3 were mandatory, as the Panel suggests, the reference in Articles I(a)(ii) and I(h)(ii) to the constituent data and methodology in the tables of supporting material would be reduced to redundancy and inutility. The Panel found that support to Korea's cattle industry should be calculated

solely on the basis of Annex 3, because support to the cattle industry was not included in Korea's Schedule. However, Articles I(a)(ii) and I(h)(ii) do not make a distinction between products which are already contained in the Schedule of a Member and those which are not.

14. In addition, in Korea's view, the Panel erred in finding that Korea's annual AMS commitment levels in its Schedule LX were not the figures in brackets, but rather the figures not in brackets. The Panel was fundamentally in error when it found that "Korea did not identify" which of the two sets of figures for annual commitment levels (figures in brackets or figures not in brackets) constitutes Korea's obligation. The Panel failed to apply the general rule of interpretation expressed in Article 31 of the *Vienna Convention on the Law of Treaties*¹⁰ (the "*Vienna Convention*") by not taking into account the context of the terms of Korea's Schedule LX, in particular Note 1 to Korea's Schedule LX, which refers to Note 1 of Supporting Table 6. In addition, the Panel's finding on this point would reduce the figures in brackets, Note 1 to Schedule LX, and Note 1 in Supporting Table 6 to inutility, again contrary to the customary rules of treaty interpretation and previous Appellate Body rulings.

15. Korea also submits that Korea's commitment levels were "public knowledge". Korea's Schedule, including Part IV, Section I, was reviewed by all the negotiating parties during the Uruguay Round. Also, the amount of Korea's subsidy to agricultural products was notified to the Committee on Agriculture every year since 1996. In each notification, Korea used the figures within brackets as Korea's commitment level for the given year. Korea considers that its consistent and amply documented position on this issue has been a matter of public record since 1996 and the very first meeting of the Committee on Agriculture to review Members' notifications under the *Agreement on Agriculture*. Thus, the "subsequent practice" of the parties following the Uruguay Round sustains Korea's position on this point of interpretation. Korea also believes that its position is supported by the manner in which the United States and Australia treated this issue in their first submissions to the Panel.

3. Dual Retail System

(a) Article III.4 of the GATT 1994

16. To Korea, the Panel fundamentally misinterpreted and misapplied Article III.4 of the GATT 1994 when it concluded that the dual retail system maintained by Korea is inconsistent with that provision. Article III.4 requires that WTO Members provide equal conditions of competition to both domestic and foreign like products. Article III.4 is an "obligation of result": the result that must be achieved is "no less favourable treatment for foreign goods". The particular method of achieving

¹⁰Done at Vienna, 23 May 1969, 1155 U.N.T.S. 331; 8 International Legal Materials 679.

this result is irrelevant. Article III:4 neither imposes nor prohibits any particular means that Members employ to provide equal conditions of competition. According to Korea, its dual retail system does provide "no less favourable treatment to foreign goods", and, therefore, achieves the result required by Article III:4. The Panel erroneously concluded that the dual retail system "constitutes in itself differential treatment."

17. Korea submits that a proper analysis of Korea's obligation under Article III:4 requires review of both *de jure* and *de facto* discrimination. The dual retail system does not amount to either *de jure* or *de facto* discrimination. With regard to *de jure* discrimination, Korea's dual retail system assures perfect regulatory symmetry between imports and domestic products. Imported beef is sold only in stores that choose to sell imported beef, and domestic beef is sold only in stores choosing to sell domestic beef. In addition, there is total freedom on the part of retailers to switch from one category of shops to the other. Thus, the Panel failed to demonstrate that there is any discrimination "demonstrated on the basis of the words of the relevant legislation, regulation or other legal instrument," the standard for a finding of *de jure* discrimination.

18. To demonstrate the presence or absence of *de facto* discrimination, the Panel should have undertaken an analysis of the market as part of an examination of the "total configuration of the facts". Instead, the Panel resorted to "speculation". An examination of the facts of the Korean beef market demonstrates that imported and domestic goods experience equal competitive conditions. The absence of such a factual analysis means that the Panel's finding on the dual retail system under Article III:4 is in error.

19. Korea also argues that the Panel erred in finding the display sign requirement to be inconsistent with Article III:4. The first ground offered by the Panel is that the display sign requirement would necessarily be inconsistent with Article III:4 since the dual retail system had already been found to be inconsistent. However, the Panel itself stated that the display sign requirement is a related measure "which the Panel addresses separately in Section 3 hereinafter." In other words, the Panel did not include the display sign requirement in its review of the dual retail system.

20. The second ground cited by the Panel is that the display sign requirement goes beyond the indication of origin of goods. Quoting from a 1956 Working Party Report, the Panel argues that such requirements are inconsistent with Article III:4 of the GATT. To Korea, the legal status of this report is unclear. The language of the report suggests that it was not intended to be binding or to provide an authoritative interpretation of the GATT.

(b) Article XX(d) of the GATT 1994

21. Should the Appellate Body disagree with Korea's claim that the dual retail system is consistent with Article III:4, then Korea submits that the Panel erred in ruling that the dual retail system was not justified under Article XX(d) of the GATT 1994.

22. The Panel found that Korea did not apply a dual retail system for other products in respect of which fraudulent sales have occurred. According to the Panel, such failure was evidence that the dual retail system was not "necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement" under Article XX(d). Korea submits that to decide whether a particular measure is necessary under Article XX(d), panels must simply examine whether another means exists which is less restrictive than the one used, and which can reach the objective sought. Consistency among regulations applicable to different products is irrelevant for establishing whether the means chosen by a WTO Member is necessary to achieve the objective of the regulation.

23. Furthermore, the Panel, in analyzing alternative, less restrictive means, did not take into account the level of enforcement sought. Korea's goal is not simply the "reduction or limitation" of deceptive practices, but their "elimination". The Panel considered four less trade-restrictive alternatives, which are investigations, fines, record-keeping and policing. In view of the fact that all four alternatives already comprise a package of policy tools used by Korea, along with the dual retail system, the Panel should have examined the facts to see whether, if the dual retail system were withdrawn, Korea's regulatory goal of the *elimination* of deceptive practices would be satisfied. Instead, the Panel narrowly focused its review on whether the less restrictive option is reasonably available. The Panel failed to link the means of implementation used to the objective sought.

24. Korea's dual retail system satisfies the requirements of the introductory clause of Article XX of the GATT 1994 as well. As the Appellate Body has held, the introductory clause of Article XX is concerned with the "even-handedness" underlying the application of national legislation. In other words, national legislation must be applied "even-handedly" between and among trading partners. Korea's dual retail system does not differentiate between Korea's trading partners. In fact, the dual retail system imposes, in practice, a much heavier burden on domestic beef producers.

25. Furthermore, in Korea's view, the display sign requirement is justified under Article XX(d) of the GATT 1994 as it is "necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement". To require shop-owners to display a sign that

their store engages in selling imported beef imposes a "proportional burden" in view of the objective sought. Korea considered an alternative measure, but it would not have achieved Korea's objective.

26. Finally, Korea argues that the Panel failed to examine whether the display sign requirement was justified under Article XX(d) of the GATT 1994. The Panel did not explain its failure to examine the display sign requirement under Article XX(d), despite the fact that Korea had made clear that its Article XX defense extended to the display sign requirement as well. Korea submits that, were the Appellate Body to complete the analysis left undone by the Panel, the Appellate Body will find that the display sign requirement is fully justified under Article XX.

B. *Australia – Appellee*

1. Terms of Reference

27. Australia considers that Korea's claim that the Panel ruled outside its terms of reference in making findings as to the commitment levels and the AMS calculation methodology used by Korea to calculate the Current AMS, is unfounded. In Australia's view, the Panel correctly ruled that Australia's panel request meets the requirements of Article 6.2 of the DSU because Australia identified the specific measures at issue and provided a brief summary of the legal basis of the complaint sufficient to present the problem clearly.

28. In respect of the commitment levels, Australia argues that as Articles 3, 6 and 7 of the *Agreement on Agriculture* specifically refer to a Member's Schedule, consideration of Korea's commitment levels contained in Part IV, Section I of Korea's Schedule was within the Panel's terms of reference. A determination as to which of Korea's two sets of commitment levels constituted the figures against which its Current Total AMS should be compared was necessary to the Panel's legal examination of claims under Articles 3, 6 and 7 of the *Agreement on Agriculture*.

29. With regard to the AMS calculation methodology, Australia submits that the Panel took into account the linkages between the obligations contained in Articles 3, 6 and 7 of the *Agreement on Agriculture* and the relevant definitions contained in Article 1 of that Agreement, which include specific reference to methodologies contained in Annex 3. The Panel correctly concluded that it could not assess whether Korea had met its obligations under Articles 3, 6 and 7 without examining the calculation prescriptions for AMS contained in Annex 3.

30. Furthermore, Australia contends that Korea has failed to show any prejudice arising from a deficiency in Australia's request for a panel. Korea appears to have been informed sufficiently well of the claims being made to prepare a defence. Korea seems to have understood the nature of the legal

claims sufficiently well for the purposes of its first submission, in which it argued at length that its calculation methodology was in fact consistent with the *Agreement on Agriculture*. It was not until the final meeting with the Panel that Korea claimed that its ability to defend itself had been prejudiced. Korea has also not shown that third parties were prejudiced.

2. Domestic Support Under the *Agreement on Agriculture*

31. Australia submits that Korea's argument, that the Panel's interpretation of Articles 1(a)(ii) and 1(h)(ii) of the *Agreement on Agriculture* is unfair, illogical and results in inappropriate comparisons between a WTO Member's reduction commitments and support provided, is without substance. Korea's arguments evidence a misunderstanding of the concepts of Current AMS, Current Total AMS and Annual and Final Bound Reduction Commitments, as defined in the *Agreement on Agriculture*. Australia states that the two figures involved in the comparison will not necessarily be based on the same product mix, as the categories of products that are subsidized may change from year to year.

32. Australia considers that Korea's interpretation that Current AMS should be calculated based on the constituent data and methodology in Korea's Schedule would render the reference to Annex 3 in Articles 1(a)(ii) and 1(h)(ii) inutile. The Panel correctly found that for products where no support was included in the base period, there is no relevant "constituent data or methodology" in the tables of supporting material. Calculations based on Annex 3 are, therefore, mandatory.

33. With regard to the two sets of commitment levels in Korea's Schedule, Australia argues that a treaty interpreter is not required to give effect to treaty terms which are invalid. The Panel noted that Korea is the only WTO Member whose Part IV domestic support Schedule contains two sets of annual commitment levels, and that no provision of the *Agreement on Agriculture* authorizes such a departure from the norm or practice. For this reason, the Panel was under no obligation to give effect to the commitment level figures in brackets.

34. Australia also contends that the question of whether Korea's commitment levels were "public knowledge" is beyond the Appellate Body's mandate under Article 17.6 of the DSU to address "issues of law covered in the panel report and legal interpretations developed by the panel", as Korea did not present any such evidence to the Panel. In any case, public knowledge of a WTO-inconsistent Schedule commitment does not validate that commitment. Finally, Korea did not meet its burden of demonstrating that "subsequent practice" of WTO Members establishes the agreement of Members regarding the interpretation of Korea's Schedule.

3. Dual Retail System

(a) Article III:4 of the GATT 1994

35. In Australia's view, Korea's claim that proper analysis of its obligation under Article III:4 requires a two-step review of whether *de jure* or *de facto* discrimination is at issue is legally flawed and should be rejected. According to Australia, the legal standard imposed by the phrase "less favourable treatment" has long been settled: a panel must consider whether imported products are being accorded effective equality of competitive opportunities.

36. Australia contends that the Panel was correct when it found that the design and architecture of the dual retail system and related measures clearly provide less favourable treatment for imported beef. Australia states that stores selling imported beef face restrictions on volumes, price and types of beef available for sale, additional record-keeping, recording and signage requirements, and the commercial disadvantage of having to dismantle their current business in domestic beef if they wish to test the market for imported beef. Fundamentally, imported beef is prevented from being sold in the same stores, under the same conditions, as domestic beef. Thus, the claim by Korea that "regulatory symmetry" exists cannot be sustained.

37. In Australia's view, the Panel correctly concluded that the dual retail system constitutes, in and of itself, differential treatment. This differential treatment unavoidably results in imported beef being less favourably treated on the Korean market than like domestic products, and the segregation of imported beef provides the domestic product with a competitive advantage over the imported product.

(b) Article XX(d) of the GATT 1994

38. Australia claims the Panel was correct in finding that, even if the dual retail system had been instituted to prevent the fraudulent misrepresentation of imported beef as domestic beef, the measure was not "necessary" to accomplish that purpose, within the meaning of Article XX(d). The Panel explored the alternatives available to Korea, including alternatives currently applied to situations of alleged country of origin fraud involving other foodstuffs where price differentials prevail. This approach reflects the ordinary meaning of the term "necessary" that no reasonable alternative exists, as well as past GATT and WTO practice.

39. Australia submits that the burden is on Korea to demonstrate a *prima facie* case that the dual retail system falls within one of the exceptions of Article XX, and that it meets the requirements of the introductory clause. Korea has to demonstrate that there was no other alternative measure it could

reasonably employ, which was WTO-consistent or less WTO-inconsistent, to secure compliance with the *Unfair Competition Act*. In the particular circumstances of the Korean market for imported beef, where it is otherwise impossible to distinguish between domestic and imported beef, where there is no dual wholesale system and where no record-keeping by stores selling domestic beef is required, it is impossible to conclude that the dual retail system has any serious impact on the prevention or elimination of fraud.

40. Even if the Panel erred in law in finding that the dual retail system did not qualify for the exception provided by Article XX(d), the Appellate Body has sufficient facts and legal argument to complete the Panel's inquiry. In doing so, the Appellate Body should find that the dual retail system does not meet the requirements of the introductory clause of Article XX. Australia considers relevant the fact that Korea only applies the dual retail system to imported beef, despite the fact that the problem of fraud also exists in relation to different types of beef and to a range of other agricultural products where a price differential exists between imported and domestic products. Furthermore, the dual retail system is not an isolated measure in an otherwise non-discriminatory environment for imported beef. Rather, the dual retail system is part of the regulatory framework for imported beef under which the importation, distribution and sale of imported beef is tightly regulated and heavily restricted by the Korean government, and substantial subsidies are provided to domestic producers, consistent with the government's stabilisation policies for domestic beef. Consideration of the dual retail system in this context reveals its protective purpose.

41. According to Australia, Korea is incorrect when it asserts that the Panel did not consider the display sign requirement in its review of the dual retail system. The Panel agreed with Korea that the sign requirement was "essentially ancillary to the dual retail system", and considered the two requirements together under Article XX(d). Thus, the Panel subsumed its findings related to the display sign requirement within its findings related to the dual retail system as a whole.

C. *United States – Appellee*

1. Terms of Reference

42. According to the United States, its panel request clearly states its claim that Korea has increased the level of domestic support for its cattle industry to the point that the total domestic support provided by Korea exceeds its AMS commitment levels. Based on Articles 3, 6 and 7 of the *Agreement on Agriculture*, Korea's current total domestic support is greater than the AMS commitment levels set out in the *Agreement on Agriculture*. All of the pertinent provisions of the *Agreement on Agriculture*, including Annex 3, had to be examined. The determination of the level of

Current Total AMS, requires the application of the provisions of Annex 3, as Annex 3 is "intrinsic" to the calculation of the Current Total AMS.

43. Similarly, the commitment levels in Korea's Schedule also had to be examined. As the Current Total AMS was to be compared to Korea's commitment levels, it was first necessary to determine which set of figures in Korea's Schedule constituted Korea's commitment levels.

44. The United States notes that the Appellate Body has previously stated that a panel is obliged to consider provisions that are "directly linked" to the provisions cited in the panel request. In this case, Annex 3 and the commitment levels in Korea's Schedule are "directly linked" to the claim set out in the panel request, and therefore must be considered.

45. Furthermore, Korea suffered no prejudice on this issue as a result of the complaining parties' panel requests. In fact, Korea, in its first submission, submitted detailed explanations on how it had calculated its AMS for beef. Thus, Korea clearly understood the matter at issue.

2. Domestic Support Under the *Agreement on Agriculture*

46. According to the United States, the Panel was correct in its finding that Korea's Current AMS for beef must be calculated in accordance with the requirements of Annex 3 of the *Agreement on Agriculture*. The specific language of Article 1(a)(ii) makes clear that the Current AMS calculation must be made in accordance with the provisions of Annex 3. While additional guidance is provided in this provision, to the effect that the "constituent data and methodology" in Korea's Schedule must be taken into account, this cannot be construed to nullify the express requirement that the Current AMS calculation be performed in accordance with Annex 3.

47. If Korea's Current AMS for beef is calculated correctly, it is more than *de minimis* under Article 6.4 of the *Agreement on Agriculture*, and must therefore be included in the calculations for Current Total AMS. When Current AMS for beef is included in Current Total AMS, Current Total AMS exceeds Korea's AMS commitment levels set out in its Schedule.

48. The United States contends that Korea, by including an alternative set of commitment levels in its Schedule, is trying to modify unilaterally the terms of the *Agreement on Agriculture* to substitute a domestic support commitment that is not in accordance with Annex 3. In effect, by claiming that the figures in brackets represent its commitment levels, Korea is attempting to inflate the amount of its annual AMS commitment level. The methodology used by Korea is not consistent with the obligations under the *Agreement on Agriculture*. The United States notes that a

WTO Member may not, in its Schedule, act inconsistently with its WTO obligations. WTO Members may yield rights and grant benefits in their Schedules, but may not diminish their obligations.

49. Korea has argued that WTO Members knew of the contents of Korea's Schedule, and, therefore, they implicitly accepted the figures in the Schedule. The United States contends that this argument is untenable, for two reasons. First, in making this argument, Korea raises new factual allegations, which may not be addressed by the Appellate Body on appeal. Second, WTO Members did not waive their rights to dispute settlement with regard to other Members' Schedules as a result of the signing of the *WTO Agreement*.

3. Dual Retail System

(a) Article III:4 of the GATT 1994

50. According to the United States, the Panel correctly found that the dual retail system in itself constituted "less favourable treatment" inconsistent with Article III:4. Article III:4 is concerned with preserving the "effective equality of opportunities" for imported products. With regard to the dual retail system, the notion of effective equality of opportunities means that there must be a possibility for imported beef to be physically present with "like" domestic beef at the point of sale to the consumer. By excluding imported beef from the existing retail system for domestic beef, the dual retail system limits the potential market opportunities for imported beef. Since imported beef does not enjoy the same competitive opportunity to be sold in the same manner and in the same stores in which Korean beef is sold, it is treated less favourably than domestic beef.

51. The United States argues that Korea's defense of the dual retail system as providing "regulatory symmetry" between imported and domestic beef must fail. The Panel found that, in fact, the dual retail system, in conjunction with certain restrictions on imports, more onerous record-keeping requirements for imported beef sellers, and the display sign requirement imposed on imported beef sellers, resulted in less favourable treatment for imported beef.

52. Furthermore, the United States contends, the Panel's additional conclusion that the dual retail system involves *de facto* discrimination against imported beef was also correct. The Panel noted the following factors as relevant: the separate store requirement limits the ability of consumers to make side-by-side comparisons of imported and domestic beef and to make purchasing decisions based on differences in quality, characteristics and prices of the respective products; imported beef is segregated due to the obstacles confronted by a store owner who wishes to sell imported beef; and there are fewer imported than domestic beef stores. The Panel found that the segregation of domestic

and imported beef provides domestic beef with a competitive advantage over the imported product. In the view of the United States, this finding of the Panel should be upheld.

53. Article 9 of the *Management Guideline* requires that imported beef stores display a sign indicating that the beef sold in the store is imported. According to the United States, given the undisputed difference in treatment resulting from Article 9 of the Guidelines, Korea bears the burden of demonstrating that the dual retail system does not result in less favourable treatment, and Korea has failed to meet its burden. The Panel's finding that the display sign requirement was "ancillary" to the dual retail system was accurate. The 1956 Working Party Report was simply invoked to "reinforce" the Panel's view, not as a basis for its finding.

(b) Article XX(d) of the GATT 1994

54. The United States argues that the Panel correctly concluded that Korea failed to sustain its burden of justifying its dual retail system under Article XX(d) of the GATT 1994. The Panel determined that in order to benefit from the Article XX(d) exception, Korea had to demonstrate that its dual retail regime: (1) was in place in order to "secure compliance" with laws or regulations that are themselves not inconsistent with the GATT 1994; (2) was "necessary" to secure compliance with those laws or regulations; and (3) was applied in conformity with the requirements of the introductory clause of Article XX. The Panel found that the dual retail system was in place in order to "secure compliance" with laws or regulations that are themselves not inconsistent with the GATT 1994, in particular, the *Unfair Competition Act*. However, the Panel found that Korea did not demonstrate that the dual retail system is "necessary" to secure compliance with Korea's *Unfair Competition Act*.

55. In particular, Korea failed to demonstrate that the WTO-consistent alternatives shown by the complaining parties to be available were inadequate to secure compliance with the *Unfair Competition Act* with regard to imported beef. The Panel found that Korea employed traditional and WTO-consistent means, such as inspections, investigations and prosecutions, to enforce the *Unfair Competition Act* with respect to other imported food products. The Panel regarded this as evidence that Korea could eliminate any fraud involving beef with the same measures.

56. The United States contends that, contrary to Korea's claims, the Panel did not establish a "consistency" standard requiring that uniform measures be used to secure compliance. Rather, the Panel properly examined the enforcement practices used generally by Korea to obtain compliance with the *Unfair Competition Act* to determine whether means other than the dual retail system were

reasonably available. Korea's practice with regard to other products was simply one factor to be taken into account as part of this analysis.

57. In addition, the United States argues that if the Appellate Body finds Korea's dual retail system to be "necessary" in terms of Article XX(d), Korea still cannot benefit from the Article XX exception, as Korea has failed to demonstrate that the dual retail system was designed to "secure compliance" with the *Unfair Competition Act*. The dual retail system does not prevent actions that would be illegal under the provisions of the *Unfair Competition Act* relating to fair trade practices. At most, the dual retail system serves the same objectives as the *Unfair Competition Act*.

58. The United States also submits that the dual retail system does not satisfy the requirements of the introductory clause of Article XX. For reasons of judicial economy, the Panel did not consider this issue. However, if the Appellate Body were to reverse the Panel's finding regarding whether the dual retail system is "necessary" to secure compliance with the *Unfair Competition Act*, the Appellate Body should then complete the legal analysis and find that the dual retail system does not satisfy the requirements of the introductory clause, as that system constitutes "unjustifiable discrimination" within the meaning of the introductory clause.

59. Korea criticizes the Panel for not separately addressing Korea's assertion that the display sign requirement is entitled to an exception under Article XX(d). However, the Panel concluded that the display sign requirement is ancillary to the separate store requirement, and therefore is subject to the same analysis and legal conclusions. Thus, in the view of the United States, the Panel's examination of the dual retail system under Article XX(d) is pertinent to both the separate store requirement and to the display sign requirement.

60. Finally, the United States argues, it was for Korea to demonstrate that the display sign requirement was justified under Article XX(d). However, Korea offered no evidence or reasoning to support a finding that the display sign requirement is independently necessary to secure compliance with the *Unfair Competition Act*.

D. *Arguments of the Third Participants*

1. Canada

(a) Dual Retail System

(i) Article III:4 of the GATT 1994

61. Canada agrees with the Panel's finding that the dual retail system constitutes in itself differential treatment which leads to "less favourable treatment" for imported products under the terms of Article III:4 of the GATT 1994. The dual retail system reduces "direct competition" between imported and domestic beef. In effect, only domestic beef can compete directly against other domestic beef. In these circumstances, imported beef does not benefit from "equal conditions of competition" as compared to domestic beef.

62. Canada supports the Panel's finding that the display sign requirement is "ancillary" to the dual retail system, and thus is also inconsistent with Article III:4 of the GATT 1994. The measure would be inconsistent even if it existed independently of the dual retail system, as it treats imported beef differently than domestic beef, in contravention of Article III:4.

(ii) Article XX(d) of the GATT 1994

63. Canada also agrees with the Panel's finding with regard to Article XX(d).

2. New Zealand

(a) Terms of Reference

64. In New Zealand's view, it is within the Panel's terms of reference to examine the calculation methodology of AMS in order to determine whether Korea's Current Total AMS exceeds its commitment levels, in violation of Articles 3, 6 and 7 of the *Agreement on Agriculture*. Although Annex 3 of the *Agreement on Agriculture* is not specifically referred to in the complaining parties' panel requests in this dispute, Article 6 of the *Agreement on Agriculture*, which is referred to in the panel requests, defines AMS by reference to Article 1. Article 1, in turn, refers to the calculation of AMS in terms of Annex 3. Thus, the provisions of Annex 3 are necessary to determine whether Korea has met its domestic support commitments under Articles 3, 6 and 7.

65. Furthermore, the complaining parties have not made a separate claim regarding Annex 3. Rather, the claim they have made is under Articles 3, 6 and 7 of the *Agreement on Agriculture*, and the references to Annex 3 are simply arguments in support of this claim. Since the claim under

Articles 3, 6 and 7 of the *Agreement on Agriculture* is within the Panel's terms of reference, arguments in support of that claim are within the terms of reference as well.

66. New Zealand also argues that Korea has failed to demonstrate that it has been prejudiced by the omission of a reference to Annex 3 in the panel request. The calculation methods set out in Annex 3 are linked to Articles 3, 6 and 7 of the *Agreement on Agriculture*. New Zealand, as a third party to the dispute, was able to determine the measure and claims at issue and respond accordingly based on the reference in the panel request to "domestic support". Korea has not demonstrated that it could not do the same.

67. Finally, New Zealand contends that Korea failed to bring its procedural objections before the Panel in a timely manner.

(b) Domestic Support Under the *Agreement on Agriculture*

68. New Zealand notes that, according to Article 1(a)(ii) of the *Agreement on Agriculture*, the AMS is to be calculated "in accordance with" Annex 3, but "taking into account" the constituent data and methodology in the supporting tables in a Member's Schedule. Thus, a Member is to calculate the AMS according to Annex 3, but may also use the relevant and applicable constituent data and methodology set out in the supporting tables of its Schedule. However, resort to such data and methodology does not absolve a Member of the obligation of correctly calculating the AMS in a manner consistent with Annex 3.

69. New Zealand further submits that a Member can only take into account the constituent data and methodology where it exists. As there was no data or methodology for beef set out in the supporting tables of Part IV of Korea's Schedule, the Panel was correct to calculate AMS by relying on Annex 3 exclusively.

70. Finally, New Zealand argues that AMS calculations under Annex 3 are based on "eligible" production, as required by that provision. Thus, the argument of Korea that "actual" purchases are properly the basis of its AMS calculation should be rejected.

(c) Dual Retail system

(i) Article III:4 of the GATT 1994

71. New Zealand submits that the term "less favourable treatment" under Article III:4 requires that imported and domestic goods receive "effective equality of opportunities". New Zealand supports the Panel's finding that, in the circumstances of this case, Korea's dual retail system for beef

results in competitive disadvantages for imported beef, as imported beef is denied the opportunity to compete in the framework of an integrated market. As the Panel concluded, the existence of a dual retail system, in circumstances where there is an extensive existing retail system, in itself constitutes a violation of Article III:4.

72. Furthermore, New Zealand agrees with the Panel's finding that the display sign requirement, being ancillary to the dual retail system, is also inconsistent with Article III:4. While the Panel chose to consider this aspect of the dual retail system separately, it is nevertheless one of the components of the dual retail system.

(ii) Article XX(d) of the GATT 1994

73. New Zealand supports the Panel's finding that Korea failed to show that the dual retail system was "necessary" within the meaning of Article XX(d) to accomplish Korea's desired level of fraud prevention. As stated by the Panel, practices used in other sectors to address deceptive practices are relevant for a determination of whether certain practices are "necessary" in the beef sector.

74. New Zealand also contends that the dual retail system is not consistent with the requirements of the introductory clause of Article XX. The dual retail system enables the Korean Government to protect Korea's domestic beef producers from import competition by limiting the terms on which imported products may be sold in the market, and therefore constitutes a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, within the meaning of the introductory clause of Article XX.

III. Issues Raised in this Appeal

75. The issues raised in this appeal are the following:

- (a) whether examination of Korea's Schedule LX and Annex 3 of the *Agreement on Agriculture* was within the Panel's terms of reference;
- (b) whether the Panel erred in calculating Korea's Current AMS for beef based on Annex 3 of the *Agreement on Agriculture*, and whether the resulting Current Total AMS exceeded Korea's AMS commitment levels for 1997 and 1998;
- (c) whether the "dual retail system", which requires the sale of imported beef in specialized stores, was inconsistent with Article III:4 of the GATT 1994; and

(d) whether the "dual retail system", if inconsistent with Article III:4 of the GATT 1994, can nevertheless be justified under Article XX(d).

IV. Terms of Reference

76. Before the Panel, Korea argued that its Schedule LX is not mentioned in the complaining parties' panel requests and, therefore, no violation can be claimed with regard to the Schedule.¹¹ Korea further contended that the panel requests were insufficiently detailed and specific to encompass the complaining parties' claims based on Annex 3 of the *Agreement on Agriculture*.¹²

77. The Panel held that, when examining claims regarding Articles 3, 6 and 7 of the *Agreement on Agriculture*, "its terms of reference require it to examine Korea's Schedule LX to assess whether its domestic support in 1997 and 1998 exceeded the reduction commitments contained in its Schedule"¹³, and that "its assessment of the compatibility of Korea's domestic support with Articles 3, 6 and 7 requires that the Panel compares the effective support provided by Korea as determined using the calculation parameters of Annex 3."¹⁴ Therefore, an examination of Korea's Schedule LX and Annex 3 of the *Agreement on Agriculture* for this purpose was not outside the Panel's terms of reference.

78. On appeal, Korea argues that the Panel erred by ruling on two claims that were outside of its terms of reference. In particular, Korea refers to the Panel's finding as to which set of numbers in its Schedule LX constitutes Korea's levels of commitment¹⁵; and to the Panel's finding that Korea's methodology for calculating Current Aggregate Measurement of Support ("AMS") for beef was not consistent with the methodology provided in Annex 3 of the *Agreement on Agriculture*.¹⁶

79. In this dispute, the Panel's terms of reference were defined as follows:

¹¹Panel Report, para. 787.

¹²*Ibid.*

¹³*Ibid.*, para. 803.

¹⁴*Ibid.*, para. 815.

¹⁵Korea's appellant's submission, paras. 15-25.

¹⁶*Ibid.*, paras. 65-70.

To examine, in the light of the relevant provisions of the covered agreements cited by the United States in document WT/DS/161/5 and by Australia in document WT/DS/169/5, the matter referred to the DSB by the United States and Australia in those documents and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements.¹⁷

Thus, the Panel's terms of reference required it to examine the "matter" referred to the DSB by the complaining parties in the requests for the establishment of a panel by the United States and Australia, respectively.¹⁸ The "matter" referred to the DSB is the set of claims made in these requests.¹⁹

80. In its panel request, Australia stated, in respect of Korea's agricultural domestic support, that:

Korea has also increased the level of domestic support for its cattle industry in amounts which result in the total domestic support provided by Korea exceeding its Aggregate Measurement of Support (AMS) under the Agreement on Agriculture.

Australia went on to state that Korea was acting inconsistently with obligations under, *inter alia*, Articles 3, 6 and 7 of the *Agreement on Agriculture*.

81. The United States, in its panel request, stated, in very similar terms:

At the same time, Korea has increased the level of domestic support for its cattle industry to the point that the total domestic support provided by Korea exceeds its Aggregate Measurement of Support (AMS) under the Agreement on Agriculture.

The United States also referred to Korea's measures as being inconsistent with, *inter alia*, Articles 3, 6, and 7 of the *Agreement on Agriculture*.

82. Thus, the claim made by both complaining parties was that Korea's domestic support for its cattle industry had increased to the point that Korea exceeded its AMS commitment levels for certain years, in contravention of Articles 3, 6 and 7 of the *Agreement on Agriculture*.

¹⁷WT/DS161/6, WT/DS169/6; see also Article 7.1 of the DSU.

¹⁸WT/DS161/5, WT/DS169/5.

¹⁹See Appellate Body Report, *Brazil – Measures Affecting Desiccated Coconut*, WT/DS22/AB/R, adopted 20 March 1997, p. 22; Appellate Body Report, *Guatemala – Anti-Dumping Investigation Regarding Portland Cement from Mexico*, WT/DS60/AB/R, adopted 25 November 1998, para. 72.

83. With respect to Korea's claim that the Panel acted outside its terms of reference in examining the "commitment levels" in Korea's Schedule, the following paragraphs of Articles 3 and 6 of the *Agreement on Agriculture* are of particular importance. Article 3.2 obligates Members not to exceed the support levels they had specified in their Schedules:

Subject to the provisions of Article 6, a Member shall not provide support in favour of domestic producers in excess of the commitment levels specified in Section I of Part IV of its Schedule. (emphasis added)

Article 6.3 in turn states:

A Member shall be considered to be in compliance with its domestic support reduction commitments in any year in which its domestic support in favour of agricultural producers expressed in terms of Current Total AMS does not exceed the corresponding annual or final bound commitment level specified in Part IV of the Member's Schedule. (emphasis added)

Articles 3.2 and 6.3 both refer explicitly to the "commitment level" specified in Part IV of a Member's Schedule. In order to make a finding on the complaining parties' claim, the Panel had no choice but to determine the appropriate "commitment levels" in Korea's Schedule.

84. With respect to Korea's claim²⁰ that the Panel acted outside its terms of reference in examining Annex 3 of the *Agreement on Agriculture*, we note that Article 6.4 provides:

(a) A Member shall not be required to include in the calculation of its Current Total AMS and shall not be required to reduce:

(i) product-specific domestic support which would otherwise be required to be included in a Member's calculation of its Current AMS where such support does not exceed 5 per cent of that Member's total value of production of a basic agricultural product during the relevant year;

...

(b) For developing country Members, the *de minimis* percentage under this paragraph shall be 10 per cent.

Article 7.2(a) states:

²⁰*Supra*, para. 78.

Any domestic support measure in favour of agricultural producers, including any modification to such measure, and any measure that is subsequently introduced that cannot be shown to satisfy the criteria in Annex 2 to this Agreement or to be exempt from reduction by reason of any other provision of this Agreement shall be included in the Member's calculation of its Current Total AMS.

Both Articles 6 and 7, claimed by the complaining parties to have been violated by Korea, refer explicitly to Current AMS and/or Current Total AMS.

85. AMS and Total AMS are defined in Article 1 of the *Agreement on Agriculture*, entitled "Definition of Terms". According to Article 1(a)

"Aggregate Measurement of Support" and "AMS" mean the annual level of support, expressed in monetary terms, provided for an agricultural product in favour of the producers of the basic agricultural product ... which is:

...

(ii) with respect to support provided during any year of the implementation period and thereafter, *calculated in accordance with the provisions of Annex 3 of this Agreement* and taking into account the constituent data and methodology used in the tables of supporting material incorporated by reference in Part IV of the Member's Schedule; (emphasis added)

According to Article 1(h)

"Total Aggregate Measurement of Support" and "Total AMS" mean the sum of all domestic support provided in favour of agricultural producers, calculated as the sum of all aggregate measurements of support for basic agricultural products, ... which is:

...

(ii) with respect to the level of support actually provided during any year of the implementation period and thereafter (i.e. the "Current Total AMS"), *calculated in accordance with the provisions of this Agreement*, including Article 6, and with the constituent data and methodology used in the tables of supporting material incorporated by reference in Part IV of the Member's Schedule; (emphasis added)

86. While Article 1(h)(ii) uses the terms "provisions of this Agreement", Article 1(a)(ii) is more specific and refers precisely to "*the provisions of Annex 3 of this Agreement*". Annex 3 is entitled "Domestic Support: Calculation of Aggregate Measurement of Support". Through the definitions set

out in Article 1, Annex 3 thus becomes part of Articles 6 and 7. In examining the claims under Articles 3, 6 and 7, the Panel, therefore, had to examine the terms of Annex 3 as well. The Panel had to calculate Current AMS for beef "*in accordance with the provisions of Annex 3 ...*" and taking into account the constituent data and methodology ... " to determine whether Current AMS for beef was to be included in Current Total AMS. Thus, in order to reach a finding on the complaining parties' claim, the Panel in this case had to ascertain the appropriate "commitment levels" in Korea's Schedule, and had to calculate Current AMS for beef "in accordance with the provisions of Annex 3 ... " to determine whether Current AMS for beef was to be included in Current Total AMS.

87. It is true that, as Korea states, the panel requests in this dispute do not explicitly refer to the "commitment levels" in Korea's Schedule or to "Annex 3" of the *Agreement on Agriculture*. In *Argentina – Safeguard Measures on Imports of Footwear*, however, we held that the "terms of Article 4.2(c) of the *Agreement on Safeguards* expressly incorporate the provisions of Article 3" of that Agreement.²¹ In that case, we stated that "we find it difficult to see how a panel could examine whether a Member had complied with Article 4.2(c) without also referring to the provisions of Article 3 of the *Agreement on Safeguards*."²² We believe the same approach appropriately applies here. Although the "commitment levels" in Korea's Schedule and "Annex 3" of the *Agreement on Agriculture* were *not explicitly* referred to in the panel requests in this dispute, it is clear that Articles 3 and 6 of the *Agreement on Agriculture*, which were referred to in the panel requests, incorporate those terms, either directly through Articles 3.2 and 6.3, in the case of the "commitment levels", or indirectly through Article 1(a)(ii), in the case of "Annex 3". In our view, the commitment levels in Korea's Schedule and the provisions of Annex 3 were in effect referred to in the complaining parties' panel requests, and were, therefore, within the Panel's terms of reference.

88. It is useful to add that, in deciding which set of figures in Korea's Schedule constituted the true and effective commitment levels of Korea and in determining how Current AMS should be calculated under Annex 3, the Panel did not rule on a separate "claim".²³ Rather, it examined specific arguments related to the claim that Korea's domestic support exceeded its AMS commitment levels.

²¹Appellate Body Report, WT/DS121/AB/R, adopted 12 January 2000, para. 74.

²²*Ibid.*

²³We note that in paragraph 800 of its Report, the Panel addressed the United States' "claim" that the Base Total AMS specified in Part IV, Section I of Korea's Schedule was initially miscalculated. The Panel considered that this "claim" was not properly before it. It concluded "that the only measure at issue is Korea's current domestic support for its beef industry in the context of Korea's scheduled commitment levels on domestic support under the *Agreement on Agriculture*". This conclusion of the Panel has not been appealed and is not before us.

In this context, it seems useful to recall our statement in *European Communities – Regime for the Importation, Sale and Distribution of Bananas* that:

... there is a significant difference between the *claims* identified in the request for the establishment of a panel, which establish the panel's terms of reference under Article 7 of the DSU, and the *arguments* supporting those claims, which are set out and progressively clarified in the first written submissions, the rebuttal submissions and the first and second panel meetings with the parties.²⁴

The claim of the complaining parties was that Korea's domestic support for beef had increased to the point that this support exceeded Korea's commitment levels for certain specified years. This claim was made under Articles 3, 6 and 7 of the *Agreement on Agriculture*, as stated in both panel requests, and was clearly within the Panel's terms of reference. The Panel's examination of the commitment levels in Korea's Schedule and the calculation methodology in Annex 3 was carried out in the course of assessing arguments related to the complaining parties' claim.

89. For these reasons, we conclude that the Panel did not err in finding that the issue of which set of figures constituted Korea's commitment levels and the issue of whether Current AMS for beef must be calculated in accordance with Annex 3 were within its terms of reference.

V. Domestic Support under the *Agreement on Agriculture*

90. In the Panel proceedings, the complaining parties claimed that Korea provided domestic support to its beef industry, measured by Current AMS, in amounts which exceeded *de minimis* levels in 1997 and 1998 and which, therefore, were required to be included in Korea's calculation of Current Total AMS for those years. When domestic support for beef was included in Current Total AMS, they contended, Korea's Current Total AMS exceeded its commitment levels set out in Part IV of its Schedule for those years, contrary to Articles 3 and 6 of the *Agreement on Agriculture*.²⁵

91. In addressing the above claim, the Panel ascertained both Korea's commitment levels for 1997 and 1998 and Korea's Current Total AMS for those years. With regard to Korea's commitment levels, the Panel noted that there were two sets of figures in Korea's Schedule in the column entitled "Annual

and final bound commitments level 1995-2004", with one set in brackets and the other set not in brackets. The Panel concluded that the figures *not* in brackets constituted Korea's commitment levels.²⁶ With regard to Current Total AMS for 1997 and 1998, the Panel first examined whether Current AMS for beef exceeded the 10 per cent *de minimis* level set out in Article 6.4 of the *Agreement on Agriculture*. The Panel found that Current AMS for beef exceeded the *de minimis* level, and, therefore, was required to be included in Current Total AMS, and that Korea's failure to include Current AMS for beef in Current Total AMS was inconsistent with Article 7.2(a) of the *Agreement on Agriculture*.²⁷ The Panel then compared Current Total AMS for 1997 and 1998 with Korea's commitment levels for those years, and concluded that Current Total AMS exceeded the commitment levels, contrary to Article 3.2 of the *Agreement on Agriculture*.²⁸

92. On appeal, Korea argues that the Panel's conclusion that Korea exceeded its commitment levels for 1997 and 1998 was in error, for two reasons. First, Korea's view is that the Panel's finding that Korea's commitment levels, as set out in its Schedule, comprise the figures not in brackets is wrong. According to Korea, the commitment levels are, in fact, embodied in the figures in brackets, as Note 1 of Supporting Table 6 of Korea's Schedule makes clear.²⁹ Second, Korea contends that the Panel's conclusion that Current AMS for beef must be included in Current Total AMS was also wrong. According to Korea, the Panel mistakenly looked to Annex 3 of the *Agreement on Agriculture* in order to calculate the Current AMS for beef, failing to rely instead on the "constituent data and methodology" provided in Korea's Schedule, as required by Articles 1(a)(ii) and 1(h)(ii). Korea claims that its Current AMS for beef was properly calculated, on the basis of "constituent data and methodology" in its Schedule, and is less than the *de minimis* level established in Article 6.4 of the *Agreement on Agriculture*. Therefore, Korea argues, Current AMS for beef need not be included in Current Total AMS.³⁰

93. The issue before us on appeal has two parts: did the Panel err in finding, firstly, that Korea failed to include Current AMS for beef in Current Total AMS, contrary to Article 7.2(a) of the *Agreement on Agriculture*, and in finding, secondly, that, contrary to Article 3.2 of the *Agreement on Agriculture*, Korea's Current Total AMS exceeds the commitment levels in Part IV of its Schedule for 1997 and 1998? In examining the component parts of this issue, it is necessary for us to ascertain two sets of figures: the figures which constitute Korea's commitment levels for 1997 and 1998, and

²⁶Panel Report, para. 821.

²⁷*Ibid.*, para. 841.

²⁸*Ibid.*, para. 843.

²⁹Korea's appellant's submission, paras. 26-54.

³⁰*Ibid.*, paras. 79-90.

²⁴WT/DS27/AB/R, adopted 25 September 1997, para. 141.

²⁵See Panel Report, paras. 49, 51 and 818. Australia argued that Korea exceeded its commitment levels only for 1997, whereas the United States argued that Korea exceeded its commitment levels for both 1997 and 1998.

for 1998 is 1,627.17 billion won.³³ On appeal, Korea argues that the Panel's conclusion was in error.³⁴

96. Examining this issue requires us to interpret Korea's Schedule. At the outset, we note, as we have previously stated in *European Communities – Customs Classification of Certain Computer Equipment*, that:

A Schedule is ... an integral part of the GATT 1994 Therefore, the concessions provided for in that schedule are part of the terms of the treaty. As such, the only rules which may be applied in interpreting the meaning of a concession are the general rules of treaty interpretation set out in the *Vienna Convention*.

Thus, we now examine Korea's Schedule in light of the rules of treaty interpretation. We begin with the ordinary meaning of the terms of the Schedule, in their context and in the light of the object and purpose of the treaty, in accordance with Article 31(1) of the *Vienna Convention*.

97. The Panel examined the two sets of figures provided by Korea, as well as the figure for "Base Total AMS". However, as is clear from the table in Korea's Schedule LX, Part IV, Section I, which has been reprinted in paragraph 94 above, the two sets of figures do not exist in isolation. Rather, to the right of the two sets of figures is the notation "* Note 1". At the bottom of Korea's Schedule, there is "* Note 1" which states: "Refer to Note 1 of Supporting Table 6 about the numbers in parentheses." The Panel, in its reasoning, referred to the set of figures in Column 1 and Column 2, but did *not* refer to "* Note 1", nor did it consider the terms of "* Note 1".³⁶ An examination of the ordinary meaning of the terms of a treaty must take into account *all* of those terms, and, accordingly, we proceed with an examination of Korea's Schedule, including Note 1 of Supporting Table 6. In our view, the Panel's examination of the "ordinary meaning" of Korea's Schedule was not done in accordance with the rules of interpretation of general international law as codified in the *Vienna Convention*.

98. Supporting Table 6 is entitled "Aggregate Measurements of Support: Market Price Support". This table provides the supporting figures for the commitment levels set out in Part IV, Section I of Korea's Schedule LX, that is, the figures used to calculate the commitment levels. Supporting figures are provided for rice, barley, soybean, maize (corn) and rape seeds. In respect of each product, the AMS for each of the years 1989-1991 is provided, along with an average AMS level for the years

³³See Panel Report, para. 843.

³⁴Korea's appellant's submission, paras. 26-54.

³⁵Appellate Body Report, WT/DS62/AB/R, WT/DS67/AB/R, WT/DS68/AB/R, adopted 22 June 1998, para. 84.

³⁶See Panel Report, paras. 820-823.

the figures for Korea's Current Total AMS for 1997 and 1998. We turn first to an examination of Korea's commitment levels for 1997 and 1998.

A. *Korea's Commitment Levels for 1997 and 1998*

94. In Korea's Schedule LX, Part IV, Section I, entitled "Domestic Support: Total AMS Commitments", Korea has provided annual bound commitment levels for domestic support for agriculture for the period 1995-2004. The Schedule contains three columns, as follows:

Base Total AMS	Annual and final bound commitments level 1995 - 2004		Relevant Supporting Tables and document reference
	1	2	
bil. ₩ 1,718.6		bil. ₩	AGST/KOR (Supporting Table 4, 5, 6, 7, 8 and 10)
	1995: 1,695.74	(2,182.55)	*Note 1
	1996: 1,672.90	(2,105.60)	
	1997: 1,650.03	(2,028.65)	
	1998: 1,627.17	(1,951.70)	
	1999: 1,604.32	(1,874.75)	
	2000: 1,581.46	(1,797.80)	
	2001: 1,558.60	(1,720.85)	
	2002: 1,535.74	(1,643.90)	
	2003: 1,512.89	(1,566.95)	
	2004: 1,490.00	(1,490.00)	

₩ = Korean Won

*Note 1: Refer to Note 1 of Supporting Table 6 about the numbers in parentheses.

Korea's commitment levels are in Column 2, entitled "Annual and final bound commitments level 1995-2004". This column contains two sets of figures pertaining to the years 1995-2004: one set in brackets, and one set not in brackets.

95. In its findings, the Panel referred to part of Korea's Schedule. In particular, the Panel referred to the figures in Column 1 and Column 2. However, the Panel did not refer to "* Note 1" in Column 2, nor to the explanatory information set out in Note 1, and did not reprint Column 3.³¹ The Panel concluded that the set of figures not in brackets constitutes Korea's commitment levels. In support of its conclusion, the Panel noted that "the unbracketed figures in Korea's Schedule are derived from, and directly linked to, the 'Base Total AMS'". By contrast, the figures in the column with brackets "bear no such relationship to the specified 'Base Total AMS' of 1,718.60 billion won."³²

Therefore, Korea's commitment level for 1997 is 1,650.03 billion won, while the commitment level

³¹Panel Report, para. 820.

³²*Ibid.*, para. 822.

1989-1991. For rice, AMS figures for 1993 are given as well. The figures for each product were combined in order to obtain a Base Total AMS figure which could then be used to determine commitment levels for the years 1995-2004.

99. Note 1 of Supporting Table 6 reads as follows:

The AMS for rice has been calculated based on 1993 market price support instead of 1989-1991 average. The Final Bound Commitment level in 2004, however, is the level reduced by 13.3% from the 1989-1991 average Base Total AMS.³⁷

As the Panel did not consider Note 1 at the bottom of Korea's Schedule LX, Part IV, Section I, it did not consider Note 1 of Supporting Table 6 either.

100. In interpreting Note 1 of Supporting Table 6, we look again at its ordinary meaning. The first sentence of this Note indicates that the AMS calculations for *rice* are based on 1993 figures, whereas for products other than rice, the AMS figures are based on the 1989-1991 average amounts.

101. The second sentence of Note 1 of Supporting Table 6 makes clear that the final bound commitment level for 2004 has been determined by reducing the 1989-1991 average Base Total AMS by 13.3 per cent.

102. We note that the use of the term "however" ordinarily indicates a contrast between two things, and lends support to Korea's position. The contrast here is the following: whereas the starting AMS amount is calculated using the 1989-1991 figures for products other than rice and the 1993 figures for rice, the Final Bound Commitment level for 2004 is calculated based on the 1989-1991 average Base Total AMS, which relies on 1989-1991 figures for *all* products, including rice. It appears to us that what Korea stated in Note 1 of Supporting Table 6 was this: the starting AMS commitment level for 1995 is determined by using AMS calculations relying on base years of 1989-1991 for all products except rice, and 1993 for rice; "however", the final target commitment level for 2004 is based on the Base Total AMS figure which was derived by using the base years 1989-1991 for *all* products. The starting AMS commitment level figure for 1995 (2182.55 billion won) was reduced in equal annual amounts over the period from 1995 to 2004 in order to reach the final target commitment level for 2004 (1490.00 billion won). The reduced commitment levels for each year over the period 1995-2004, the calculation of which has been described by Korea in Note 1 of Supporting Table 6, are set

out in the figures in brackets. It follows from the wording of Korea's Schedule LX, Part IV, Section I, read together with Note 1 of the Supporting Table 6, that Korea's AMS commitment levels for 1995-2004 are not represented, as the Panel concluded, by the figures not in brackets, but, rather, as Korea contends, by the figures in brackets.

103. The above view is reflected in Korea's subsequent statements before the Committee on Agriculture. At a November 1996 Committee on Agriculture meeting, New Zealand asked Korea this question: "Noted that Korea's Schedule contains two sets of figures regarding annual and final bound commitment levels. Which set is accurate?" Korea responded as follows:

*The figures in brackets correspond to Korea's real annual commitment level, using the 1993 base period for rice and the 1989-1991 base period for other products, as indicated in the footnote of Korea's Schedule LX. The said calculation and annual commitment level of AMS were already reviewed and agreed upon by Member countries in March 1994. The other set of figures corresponds to the annual commitment using the base period of 1989-1991 for all the products.*³⁸ (emphasis added)

104. Furthermore, in its official annual Notifications to the Committee on Agriculture concerning domestic support commitments for 1995 to 1998, Korea made reference to its commitment level for the period in question. In each Notification, the figure Korea provided was the relevant commitment level from Korea's Schedule set out in the figures in brackets. Next to the AMS figure in each Notification is a note which says "See Note 1 of Supporting Table 6 in G/AG/AGST/KOR".³⁹

105. For these reasons, we conclude that Korea's commitment levels in Part IV, Section I of its Schedule LX are denoted by the figures in the Column entitled "Annual and final bound commitments level 1995-2004" which are in brackets. Thus, Korea's commitment level is 2,028.65 billion won for the year 1997, and 1,951.70 billion won for the year 1998.

106. We turn next to an examination of Korea's Current Total AMS for 1997 and 1998, to determine whether Korea's Current Total AMS for these years exceeded its commitment levels for those same years.

³⁸G/AG/R/9, 17 January 1997.

³⁹See G/AG/N/KOR/24, 25 August 1999; G/AG/N/KOR/18, 16 September 1998; G/AG/N/KOR/14, 15 September 1997; G/AG/N/KOR/7, 18 November 1996.

³⁷G/AG/AGST/KOR, p. 8.

B. *Korea's Current Total AMS for 1997 and 1998*

107. In its Notifications to the Committee on Agriculture for 1997 and 1998, Korea provided figures for the Current Total AMS for those years. Korea claimed that for 1997 it provided Current Total AMS of 1,936.95 billion won, and for 1998 it provided 1,562.77 billion won.⁴⁰ The complaining parties argue that Korea's Current Total AMS as provided in its Notifications was calculated improperly, as Korea did not include Current AMS for beef in its Current Total AMS. The United States contends that when Current AMS for beef is included in Current Total AMS, as required, Current Total AMS for both 1997 and 1998 exceeded Korea's commitment levels for 1997 and 1998, whereas Australia limits its contention to 1997.⁴¹

108. The Panel found that Korea's Current AMS for beef did exceed the *de minimis* level for 1997 and 1998, and, therefore, was required to be included in Current Total AMS, under Article 7.2(a) of the *Agreement on Agriculture*.⁴² The Panel then compared Korea's Current Total AMS to Korea's commitment levels for 1997 and 1998, and concluded that Current Total AMS exceeded the commitment levels, contrary to Article 3.2 of the *Agreement on Agriculture*.⁴³

109. On appeal, Korea contends that the Panel's conclusion that Current AMS for beef must be included in Current Total AMS is incorrect. According to Korea, the Panel mistakenly looked to Annex 3 of the *Agreement on Agriculture* in order to calculate the Current AMS for beef, while failing to take into account the "constituent data and methodology" provided in Korea's Schedule, as required by Articles 1(a)(ii) and 1(h)(i) of the *Agreement on Agriculture*. Korea claims that its Current AMS for beef was properly calculated in its Notifications to the Committee on Agriculture, based on the "constituent data and methodology" in its Schedule, and that consequently this Current AMS fell below the *de minimis* level established in Article 6.4 of the *Agreement on Agriculture*. Therefore, Korea argues, the Current AMS for beef need not be included in the Current Total AMS, and Current Total AMS was properly calculated in its Notifications.⁴⁴

110. In examining this issue, we need to determine first whether Current AMS for beef for 1997 and 1998 must be included in Korea's Current Total AMS for those years. We recall that Article 6.4 of the *Agreement on Agriculture* states that:

⁴⁰See G/AGN/KOR/24, 25 August 1999; G/AGN/KOR/18, 16 September 1998.

⁴¹See *supra*, footnote 25.

⁴²Panel Report, para. 841.

⁴³*Ibid.*, para. 843.

⁴⁴Korea's appellant's submission, paras. 79-90.

A Member shall not be required to include in the calculation of its Current Total AMS and shall not be required to reduce:

- (i) product-specific domestic support which would otherwise be required to be included in a Member's calculation of its Current AMS where such support does not exceed 5 per cent of that Member's total value of production of a basic agricultural product during the relevant year;

...

For developing country Members the *de minimis* percentage level under this paragraph is 10 per cent.⁴⁵ Thus, Korea's Current AMS for beef must be included in Current Total AMS only if the Current AMS for beef exceeds the 10 per cent *de minimis* requirement applicable in respect of developing country Members.

111. To determine whether Korea's Current AMS for beef exceeds 10 per cent of total value of beef production, we refer again to Article 1(a)(ii) of the *Agreement on Agriculture*, which defines Current AMS. Under this provision, Current AMS is to be

calculated *in accordance with* the provisions of Annex 3 of this Agreement and *taking into account* the constituent data and methodology used in the tables of supporting material incorporated by reference in Part IV of the Member's Schedule; ... (emphasis added)

Article 1(a)(ii) contains two express requirements for calculating Current AMS. First, Current AMS is to be "calculated *in accordance with* the provisions of Annex 3 of this Agreement". The ordinary meaning of "accordance" is "agreement, conformity, harmony".⁴⁶ Thus, Current AMS must be calculated in "conformity" with the provisions of Annex 3. Second, Article 1(a)(ii) provides that the calculation of Current AMS is to be made while "taking into account the constituent data and methodology used in the tables of supporting material incorporated by reference in Part IV of the Member's Schedule." "Take into account" is defined as "take into consideration, notice".⁴⁷ Thus, when Current AMS is calculated, the "constituent data and methodology" in a Member's Schedule must be "taken into account", that is, it must be "considered".⁴⁸

⁴⁵Article 6.4(b) of the *Agreement on Agriculture*.

⁴⁶*The New Shorter Oxford English Dictionary*, (Clarendon Press, 1993), Vol. I, p. 15.

⁴⁷*Ibid.*

⁴⁸We note that this difference is not reflected in the wording of the definition of Current Total AMS in Article 1(h). Article 1(h)(ii) provides that Current Total AMS is to be calculated "in accordance with the provisions of this Agreement, including Article 6, and with the constituent data and methodology used in the tables of supporting material incorporated by reference in Part IV of the Member's Schedule". (emphasis added)

112. Looking at the wording of Article 1(a)(ii) itself, it seems to us that this provision attributes higher priority to "the provisions of Annex 3" than to the "constituent data and methodology". From the viewpoint of ordinary meaning, the term "in accordance with" reflects a more rigorous standard than the term "taking into account".

113. We note, however, that the Panel did not base its reasoning on this apparent hierarchy as between "the provisions of Annex 3" and the "constituent data and methodology".⁴⁹ Instead, the Panel considered that where no support was included in the base period calculation for a given product, there is no "constituent data or methodology" to refer to, so that the only means available for calculating domestic support is that provided in Annex 3.⁵⁰ As beef had not been included in Supporting Table 6 of Korea's Schedule LX, Part IV, Section I, the Panel concluded that Annex 3 alone is applicable for the purposes of calculating current non-exempt support in respect of Korean beef.⁵¹

114. In the circumstances of the present case, it is not necessary to decide how a conflict between "the provisions of Annex 3" and the "constituent data and methodology used in the tables of supporting material incorporated by reference in Part IV of the Member's Schedule" would have to be resolved in principle. As the Panel has found, in this case, there simply are no constituent data and methodology for beef.⁵² Assuming *arguendo* that one would be justified – in spite of the wording of Article 1(a)(ii) – to give priority to constituent data and methodology used in the tables of supporting material over the guidance of Annex 3, for products entering into the calculation of the Base Total AMS, such a step would seem to us to be unwarranted in calculating Current AMS for a product which did *not* enter into the Base Total AMS calculation. We do not believe that the *Agreement on Agriculture* would sustain such an extrapolation. We, therefore, agree with the Panel that, in this case, Current AMS for beef has to be calculated in accordance with the provisions of Annex 3, and with these provisions alone.

115. Korea has argued that:

⁴⁹On the contrary, the Panel opines that the "constituent data and methodology" has an important role to play in ensuring that the calculation of support to any given product is calculated in subsequent years consistently with support calculated in the base period. Panel Report, para. 811.

⁵⁰*Ibid.*

⁵¹*Ibid.*, para. 812.

⁵²*Ibid.* In other words, there is no *data* (product) in respect of which the *methodology* of Schedule LX of Korea (that is, the use of figures for the years 1989-1991) could be applied, in so far as beef is concerned.

National schedules on the reduction of subsidies in favour of agricultural products ... can be understood as multi-year equations. One side of the equation includes the commitment level for a given year, while the other side of the equation includes the actual AMS for the same year. Thus, for the equation to be meaningful, both sides of the equation should be based on the same sets of data and methodology. ... Using one methodology for commitment levels and another methodology for actual AMS undermines comparability between the two, and leads to unfair results.⁵³

We believe that it is not necessary or appropriate to conceive of the pertinent provisions of the *Agreement on Agriculture* as establishing "multi-year equations". The treaty definitions of both AMS and Total AMS, set out in Articles 1(a) and 1(h) respectively, do provide a specific methodology for calculating Current AMS and Current Total AMS in respect of a particular year during the implementation period. However, with respect to the other side of a hypothetical equation, the relevant treaty provisions do *not* provide for any particular mode of calculation of the "Base Total AMS", from which figure the commitment levels for particular years of the implementation period are arithmetically derived. Article 1(a)(i) of the *Agreement on Agriculture* dealing with AMS states that "with respect to support provided during the base period", a treaty interpreter needs only to go to "the relevant tables of supporting material incorporated by reference in Part IV of a Member's Schedule ...". (emphasis added) Similarly, Article 1(h)(i) dealing with Total AMS, states that "with respect to support provided during the base period (i.e., the 'Base Total AMS') and the maximum support permitted to be provided during any year of the implementation period or thereafter (i.e., the 'Annual and Final Bound Commitment Levels')", a treaty interpreter needs only to go to what is "specified in Part IV of a Member's Schedule ...". (emphasis added) Thus, for purposes of determining whether a Member has exceeded its commitment levels, Base Total AMS, and the commitment levels resulting or derived therefrom, are not themselves formulae to be worked out, but simply absolute figures set out in the Schedule of the Member concerned. As a result, Current Total AMS which is calculated according to Annex 3, is compared to the commitment level for a given year that is already specified as a given, absolute, figure in the Member's Schedule.

116. We examine next Annex 3, entitled: "Domestic Support: Calculation of Aggregate Measurement of Support". Paragraphs 8 and 9 of Annex 3 provide the following definition of "market price support", the particular form of domestic support at issue here:

⁵³Korea's appellant's submission, para. 63.

... *market price support* shall be calculated using the gap between a fixed external reference price and the applied administered price multiplied by the *quantity of production eligible to receive* the applied administered price. Budgetary payments made to maintain this gap, such as buying-in or storage costs, shall not be included in the AMS.

The *fixed external reference price* shall be based on the years 1986 to 1988 and shall generally be the average f.o.b. unit value for the basic agricultural product concerned in a net exporting country and the average c.i.f. unit value for the basic agricultural product concerned in a net importing country in the base period. The fixed reference price may be adjusted for quality differences as necessary. (emphasis added)

Thus, under Annex 3, "market price support" is calculated by taking the difference between a fixed external reference price and the applied administered price, and multiplying that difference by "the quantity of *production eligible* to receive the applied administered price". (emphasis added) The fixed external reference price "shall be based on the years 1986 to 1988". (emphasis added)

117. The Panel found that in both 1997 and 1998 Korea miscalculated its fixed external reference price, contrary to Article 6 and paragraph 9 of Annex 3, by using a fixed external reference price based on data for 1989-1991.⁵⁴ Korea justifies this choice by invoking the "constituent data and methodology" used in its Supporting Table 6 for all products other than rice, i.e., for barley, soybean, maize (corn) and rape seeds. In Supporting Table 6, all these products use the period 1989-1991 for the fixed external reference price.⁵⁵

118. We have already explained above that we share the Panel's view with respect to Korea's argument on "constituent data and methodology" used in the table of supporting material. We agree with the Panel that, in this case, Current AMS for beef has to be calculated in accordance with Annex 3. According to Annex 3, "[t]he fixed external reference price shall be based on the years 1986 to 1988". We, therefore, also agree with the Panel that in calculating the product specific AMS for beef for the years 1997 and 1998, Korea should have used an external reference price based on data for 1986-1988, instead of data for 1989-1991.

119. The Panel found that, in calculating the Current AMS for beef for the years 1997 and 1998, Korea made a further mistake. In determining its market price support for beef, Korea used the quantity of Hanwoo cattle actually purchased. The Panel found that "[t]he actual quantity of purchases is not relevant in the calculation of market price support. Korea, by indicating its intent to

purchase specified quantities, made them eligible to receive the applied administered price, and consequently affected and supported the price of all such products".⁵⁶

120. We share the Panel's view that the words "production *eligible* to receive the applied administered price" in paragraph 8 of Annex 3 have a different meaning in ordinary usage from "production *actually purchased*". The ordinary meaning of "eligible" is "fit or *entitled* to be chosen".⁵⁷ Thus, "production eligible" refers to production that is "fit or entitled" to be purchased rather than production that was actually purchased. In establishing its program for future market price support, a government is able to define and to limit "eligible" production. Production actually purchased may often be less than eligible production.

121. In the present case, Korea, in effect, declared the quantity of "eligible production" when it announced in January, 1997, that it would purchase 500 head per day of Hanwoo cattle above 500 kg within the 27 January to 31 December 1997 period, which would be 170,000 head of cattle for the 1997 calendar year.⁵⁸ That figure, under paragraph 8 of Annex 3, accordingly constitutes the quantity of "eligible production". While there may be nothing under the *Agreement on Agriculture* to prevent Korea from changing the quantity of "eligible production", Korea did not do so, so far as the record of this case shows. Korea instead simply purchased a lesser number of cattle by ceasing its purchases.

122. Korea argues that it is entitled to calculate market price support in 1997 and 1998 by using actual purchases, because it used actual purchases in its calculations in the tables of supporting material in its Schedule. We recall that we share the Panel's view that for beef, "constituent data and methodology" do not exist in the Schedule, as beef did not enter into the calculation of Korea's initial Base Total AMS. We, therefore, agree with the Panel's finding that Korea erred in calculating market price support in 1997 and 1998 by using the amount of production actually purchased, instead of production declared eligible to receive the applied administered price, according to the provisions of paragraph 8 of Annex 3.

123. Having reached the conclusion that Korea had miscalculated its market price support in 1997 and 1998, the Panel attempted to evaluate correctly Korea's Current AMS for beef. In doing so, the Panel stated that "[f]or reasons of clarity and simplicity", it would rely on market price support

⁵⁶Panel Report, para. 831.

⁵⁷*The Concise Oxford English Dictionary*, (Clarendon Press, 1995), p. 438.

⁵⁸Panel Report, para. 834.

⁵⁴Panel Report, para. 830.

⁵⁵Korea's appellant's submission, paras. 79-80.

calculations submitted by New Zealand for Korea's Current AMS for beef.⁵⁹ Based on these calculations, the Panel found that Korea's AMS for beef had exceeded the 10 per cent *de minimis* threshold referred to in Article 6.4(b) of the *Agreement on Agriculture* in 1997 and 1998.⁶⁰

124. We note that in calculating Korea's Current AMS for beef, New Zealand uses – like Korea – a fixed external reference price based on 1989-1991 data. As we have found above, the use of such an external reference price is incompatible with paragraph 9 of Annex 3, which requires an external reference price based on the years 1986-1988.

125. The Panel was aware of this incompatibility, but seemed to assume that New Zealand's reference to 1989-1991 data benefitted, rather than harmed, Korea.⁶¹ This could be the case if the 1989-1991 data would result in a higher external reference price than the one prescribed by paragraph 9 of Annex 3, i.e., the external reference price based on the years 1986-1988. There is, however, no indication in the Panel Report of the level of the external reference price for the years 1986-1988. Furthermore, neither the Panel Report nor the Panel record contain any elements which might allow us to determine the level of such an external reference price.⁶²

126. We, therefore, must reverse the Panel's finding that Korea exceeded the 10 per cent *de minimis* threshold of Current AMS for beef in 1997 and 1998, and the consequent finding that the failure to include Current AMS for beef in Current Total AMS in these years is inconsistent with Articles 6 and 7.2(a) of the *Agreement on Agriculture*.

127. As a consequence, we must also reverse the Panel's finding that, in 1997 and 1998, Korea's Current Total AMS exceeded Korea's commitment levels, as specified in Part IV, Section I of its Schedule, in violation of Article 3.2 of the *Agreement on Agriculture*.

⁵⁹Panel Report, para. 838.

⁶⁰*Ibid.*, para. 840.

⁶¹This seems to be the meaning of the words "inflating Korea's legitimate level of domestic support" in footnote 442 of the Panel Report which reads as follows:

The Panel notes that for this recalculation of Korea's FERP, New Zealand even used 1989-1991 data (inflating Korea's legitimate level of domestic support), contrary to the Panel's conclusion that pursuant to Annex 3 a 1986-1988 FERP should have been employed.

⁶²In *Australia – Measures Affecting the Importation of Salmon* we stated that where we have reversed a finding of a panel, we should attempt to complete a panel's legal analysis "to the extent possible on the basis of the factual findings of the Panel and/or of undisputed facts in the Panel record". Appellate Body Report, WT/DS18/AB/R, adopted 6 November 1998, para. 118. See also, Appellate Body Report, *Canada – Certain Measures Affecting the Automotive Industry*, WT/DS139/AB/R, WT/DS142/AB/R, adopted 19 June 2000, para. 133.

128. We should, however, stress that, as there is insufficient information in the Panel record to allow determination of whether Current AMS for beef exceeded the *de minimis* threshold in 1997 and 1998, and, therefore, had to be included in Current Total AMS, we reach no conclusion as to whether or not Korea acted inconsistently with Articles 6 and 7.2(a) of the *Agreement on Agriculture*.

129. Furthermore, as a determination of Current Total AMS cannot be made without first ascertaining Current AMS for beef, no Current Total AMS can be calculated for 1997 and 1998. As a result, there is no basis on which we can reach a conclusion on the issue of whether or not Korea exceeded its commitment levels in Part IV of its Schedule for 1997 and 1998, contrary to Article 3.2 of the *Agreement on Agriculture*.

VI. Dual Retail System

A. Article III:4 of the GATT 1994

130. The Panel found that Korea's dual retail system for beef accords treatment less favourable to imported beef than to like Korean beef, and is, thus, inconsistent with Article III:4 of the GATT 1994. This finding was based on the Panel's view that any measure based exclusively on criteria relating to the origin of a product is inconsistent with Article III:4.⁶³ The finding was also based on the Panel's assessment of how the dual retail system modifies the conditions of competition between imported and like domestic beef in the Korean market.⁶⁴

131. Korea argues on appeal that the dual retail system does not accord treatment less favourable to imported beef than to like domestic beef. For Korea, the dual retail system does not *on its face* violate Article III:4, since there is "perfect regulatory symmetry" in the separation of imported and domestic beef at the retail level, and there is "no regulatory barrier" which prevents traders from converting from one type of retail store to another.⁶⁵ Nor, Korea argues, does the dual retail system violate Article III:4 *de facto*, and the Panel's conclusion to the contrary was not based on a proper empirical analysis of the Korean beef market.⁶⁶

⁶³Panel Report, para. 627.

⁶⁴*Ibid.*, paras. 631-637.

⁶⁵Korea's appellant's submission, paras. 119-126.

⁶⁶*Ibid.*, paras. 127-156.

132. Article III:4 of the GATT 1994 reads in relevant part:

The products of the territory of any Member imported into the territory of any other Member shall be accorded *treatment no less favourable* than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use. (emphasis added)

133. For a violation of Article III:4 to be established, three elements must be satisfied: that the imported and domestic products at issue are "like products"; that the measure at issue is a "law, regulation, or requirement affecting their internal sale, offering for sale, purchase, transportation, distribution, or use"; and that the imported products are accorded "less favourable" treatment than that accorded to like domestic products. Only the last element – "less favourable" treatment – is disputed by the parties and is at issue in this appeal.

134. The Panel began its analysis of the phrase "treatment no less favourable" by reviewing past GATT and WTO cases. It found that "treatment no less favourable" under Article III:4 requires that a Member accord to imported products "effective equality of opportunities" with like domestic products in respect of the application of laws, regulations and requirements.⁶⁷ The Panel concluded its review of the case law by stating:

Any regulatory distinction that is based exclusively on criteria relating to the nationality or the origin of the products is incompatible with Article III and this conclusion can be reached even in the absence of any imports (as hypothetical imports can be used to reach this conclusion) confirming that there is no need to demonstrate the actual and specific trade effects of a measure for it to be found in violation of Article III. The object of Article III:4 is, thus, to guarantee effective market access to imported products and to ensure that the latter are offered the same market opportunities as domestic products.⁶⁸

135. The Panel stated that "any regulatory distinction that is based exclusively on criteria relating to the nationality or origin" of products is incompatible with Article III:4. We observe, however, that

Article III:4 requires only that a measure accord treatment to imported products that is "no less favourable" than that accorded to like domestic products. A measure that provides treatment to imported products that is *different* from that accorded to like domestic products is not necessarily inconsistent with Article III:4, as long as the treatment provided by the measure is "no less favourable". According to "treatment no less favourable" means, as we have previously said, according to *conditions of competition* no less favourable to the imported product than to the like domestic product. In *Japan – Taxes on Alcoholic Beverages*, we described the legal standard in Article III as follows:

The broad and fundamental purpose of Article III is to avoid protectionism in the application of internal tax and regulatory measures. More specifically, the purpose of Article III "is to ensure that internal measures 'not be applied to imported or domestic products so as to afford protection to domestic production'". Toward this end, Article III obliges Members of the WTO to provide *equality of competitive conditions* for imported products in relation to domestic products. "[T]he intention of the drafters of the Agreement was clearly to treat the imported products in the same way as the like domestic products once they had been cleared through customs. Otherwise indirect protection could be given".⁶⁹ (emphasis added)

136. This interpretation, which focuses on the *conditions of competition* between imported and domestic like products, implies that a measure according formally *different* treatment to imported products does not *per se*, that is, necessarily, violate Article III:4. In *United States – Section 337*, this point was persuasively made. In that case, the panel had to determine whether United States patent enforcement procedures, which were formally different for imported and for domestic products, violated Article III:4. That panel said:

⁶⁹Appellate Body Report, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, pp. 16-17. The original passage contains footnotes. The second sentence is footnoted to *United States – Section 337 of the Tariff Act of 1930* ("United States – Section 337"), BISD 36S/345, para. 5.10. The third sentence is footnoted to *United States – Taxes on Petroleum and Certain Imported Substances*, BISD 34S/136, para. 5.1.9; and *Japan – Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages*, BISD 34S/83, para. 5.5(b). The fifth sentence is footnoted to *Italian Discrimination Against Imported Agricultural Machinery*, BISD 7S/60, para. 11.

⁶⁷Panel Report, para. 624.

⁶⁸*Ibid.*, para. 627. (footnotes omitted)

On the one hand, contracting parties may apply to imported products *different* formal legal requirements if doing so would accord imported products more favourable treatment. On the other hand, it also has to be recognised that there may be cases where the application of formally *identical* legal provisions would in practice accord less favourable treatment to imported products and a contracting party might thus have to apply different legal provisions to imported products to ensure that the treatment accorded them is in fact no less favourable. For these reasons, the mere fact that imported products are subject under Section 337 to legal provisions that are different from those applying to products of national origin is in itself not conclusive in establishing inconsistency with Article III:4.⁷⁰ (emphasis added)

137. A formal difference in treatment between imported and like domestic products is thus neither necessary, nor sufficient, to show a violation of Article III:4. Whether or not imported products are treated "less favourably" than like domestic products should be assessed instead by examining whether a measure modifies the *conditions of competition* in the relevant market to the detriment of imported products.

138. We conclude that the Panel erred in its general interpretation that "[a]ny regulatory distinction that is based exclusively on criteria relating to the nationality or the origin of the products is incompatible with Article III."⁷¹

139. The Panel went on, however, to examine the conditions of competition between imported and like domestic beef in the Korean market. The Panel gave several reasons why it believed that the dual retail system alters the conditions of competition in the Korean market in favour of domestic beef. First, it found that the dual retail system would "limit the possibility for consumers to compare imported and domestic products", and thereby "reduce opportunities for imported products to compete directly with domestic products".⁷² Second, the Panel found that, under the dual retail system, "the only way an imported product can get on the shelves is if the retailer agrees to substitute it, not only for one but for all existing like domestic products." This disadvantage would be more serious when the market share of imports (as is the case with imported beef) is small.⁷³ Third, the Panel found that the dual retail system, by excluding imported beef from "the vast majority of sales outlets", limits the potential market opportunities for imported beef. This would apply particularly to products

"consumed on a daily basis", like beef, where consumers may not be willing to "shop around".⁷⁴ Fourth, the Panel found that the dual retail system imposes more costs on the imported product, since the domestic product will tend to continue to be sold from existing retail stores, whereas imported beef will require new stores to be established.⁷⁵ Fifth, the Panel found that the dual retail system "encourages the perception that imported and domestic beef are different, when they are in fact like products belonging to the same market", which gives a competitive advantage to domestic beef, "based on criteria not related to the products themselves".⁷⁶ Sixth, the Panel found that the dual retail system "facilitates the maintenance of a price differential" to the advantage of domestic beef.⁷⁷

140. On appeal, Korea argues that the Panel's analysis of the conditions of competition in the Korean market is seriously flawed, relying largely on speculation rather than on factual analysis. Korea maintains that the dual retail system does not deny consumers the possibility to make comparisons, and the numbers of outlets selling imported beef, as compared with outlets selling domestic beef, does not support the Panel's findings. Korea argues, furthermore, that the dual retail system neither adds to the costs of, nor shelters high prices for, domestic beef.⁷⁸

141. It will be seen below that we share the ultimate conclusion of the Panel in respect of the consistency of the dual retail system for beef with Article III:4 of the GATT 1994. Portions, however, of the Panel's analysis *en route* to that conclusion appear to us problematic. For instance, while limitation of the ability to compare visually two products, local and imported, at the point of sale may have resulted from the dual retail system, such limitation does not, in our view, necessarily reduce the opportunity for the imported product to compete "directly" or on "an equal footing" with the domestic product.⁷⁹ Again, even if we were to accept that the dual retail system "encourages" the perception of consumers that imported and domestic beef are "different", we do not think it has been demonstrated that such encouragement necessarily implies a competitive advantage for domestic beef.⁸⁰ Circumstances like limitation of "side-by-side" comparison and "encouragement" of consumer perceptions of "differences" may be simply incidental effects of the dual retail system without decisive implications for the issue of consistency with Article III:4.

⁷⁴Panel Report, para. 633.

⁷⁵*Ibid.*, para. 634.

⁷⁶*Ibid.*

⁷⁷*Ibid.*

⁷⁸Korea's appellant's submission, paras. 101, 127-156.

⁷⁹See Panel Report, para. 633.

⁸⁰*Ibid.*, para. 634.

⁷⁰*United States – Section 337, supra*, footnote 69, paragraph 5.11.

⁷¹Panel Report, para. 627.

⁷²*Ibid.*, para. 631.

⁷³*Ibid.*, para. 632.

142. We believe that a more direct, and perhaps simpler, approach to the dual retail system of Korea may be usefully followed in the present case. In the following paragraphs, we seek to focus on what appears to us to be the fundamental thrust and effect of the measure itself.

143. Korean law in effect requires the existence of two distinct retail distribution systems so far as beef is concerned: one system for the retail sale of domestic beef and another system for the retail sale of imported beef.⁸¹ A small retailer (that is, a non-supermarket or non-department store) which is a "Specialized Imported Beef Store" may sell any meat *except domestic beef*; any other small retailer may sell any meat *except imported beef*.⁸² A large retailer (that is, a supermarket or department store) may sell both imported and domestic beef, as long as the imported beef and domestic beef are sold in separate sales areas.⁸³ A retailer selling imported beef is required to display a sign reading "Specialized Imported Beef Store".⁸⁴

144. Thus, the Korean measure formally separates the selling of imported beef and domestic beef. However, that formal separation, *in and of itself*, does not necessarily compel the conclusion that the treatment thus accorded to imported beef is less favourable than the treatment accorded to domestic beef.⁸⁵ To determine whether the treatment given to imported beef is less favourable than that given to domestic beef, we must, as earlier indicated, inquire into whether or not the Korean dual retail system for beef modifies the *conditions of competition* in the Korean beef market to the disadvantage of the imported product.

145. When beef was first imported into Korea in 1988, the new product simply entered into the pre-existing distribution system that had been handling domestic beef. The beef retail system was a unitary one, and the conditions of competition affecting the sale of beef were the same for both the domestic and the imported product. In 1990, Korea promulgated its dual retail system for beef.⁸⁶

⁸¹The essential features of the Korean dual retail system for beef are found in the *Guidelines Concerning Registration and Operation of Specialized Imported Beef Stores*, (61550-81) 29 January 1990, modified on 15 March 1994; and the *Regulations Concerning Sales of Imported Beef*, (51550-100), modified on 27 March 1993, 7 April 1994, and 29 June 1998. On 1 October 1999, these two instruments were replaced by the *Management Guideline for Imported Beef*, (Ministry of Agriculture Notice 1999-67), which maintained, however, the basic principles of the dual retail system.

⁸²*Guidelines Concerning Registration and Operation of Specialized Imported Beef Stores*, Art. 5(C); *Regulations Concerning Sales of Imported Beef*, Art. 14(5); *Management Guideline for Imported Beef*, Art. 15.

⁸³*Guidelines Concerning Registration and Operation of Specialized Imported Beef Stores*, Art. 3(A); *Management Guideline for Imported Beef*, Art. 9(5).

⁸⁴*Guidelines Concerning Registration and Operation of Specialized Imported Beef Stores*, Art. 5(A); *Regulations Concerning Sales of Imported Beef*, Art. 14(5); *Management Guideline for Imported Beef*, Art. 9(6).

⁸⁵Apart from the display sign requirement, dealt with in para. 151.

⁸⁶See Panel Report, para. 630.

Accordingly, the existing small retailers had to choose between, on the one hand, continuing to sell domestic beef and renouncing the sale of imported beef or, on the other hand, ceasing to sell domestic beef in order to be allowed to sell the imported product. Apparently, the vast majority of the small meat retailers chose the first option.⁸⁷ The result was the virtual exclusion of imported beef from the retail distribution channels through which domestic beef (and until then, imported beef, too) was distributed to Korean households and other consumers throughout the country. Accordingly, a new and separate retail system had to be established and gradually built from the ground up for bringing the imported product to the same households and other consumers if the imported product was to compete at all with the domestic product. Put in slightly different terms, the putting into legal effect of the dual retail system for beef meant, in direct practical effect, so far as imported beef was concerned, the sudden cutting off of access to the normal, that is, the previously existing, distribution outlets through which the domestic product continued to flow to consumers in the urban centers and countryside that make up the Korean national territory. The central consequence of the dual retail system can only be reasonably construed, in our view, as the imposition of a drastic reduction of commercial opportunity to reach, and hence to generate sales to, the same consumers served by the traditional retail channels for domestic beef. In 1998, when this case began, eight years after the dual retail system was first prescribed, the consequent reduction of commercial opportunity was reflected in the much smaller number of specialized imported beef shops (approximately 5,000 shops) as compared with the number of retailers (approximately 45,000 shops) selling domestic beef.⁸⁸

146. We are aware that the dramatic reduction in number of retail outlets for imported beef followed from the decisions of individual retailers who could choose freely to sell the domestic product or the imported product. The legal necessity of making a choice was, however, imposed by the measure itself. The restricted nature of that choice should be noted. The choice given to the meat retailers was *not* an option between remaining with the pre-existing unified distribution set-up or going to a dual retail system. The choice was limited to selling domestic beef only or imported beef only. Thus, the reduction of access to normal retail channels is, in legal contemplation, the effect of that measure. In these circumstances, the intervention of some element of private choice does not relieve Korea of responsibility under the GATT 1994 for the resulting establishment of competitive conditions less favourable for the imported product than for the domestic product.

⁸⁷Panel Report, para. 633.

⁸⁸The number of imported beef shops is noted by the Panel in footnote 347 of the Panel Report; the number of domestic beef shops has been provided by the United States in para. 175 of the Panel Report, and has not been contested by Korea.

147. We also note that the reduction of competitive opportunity through the restriction of access to consumers results from the imposition of the dual retail system for beef, notwithstanding the "perfect regulatory symmetry" of that system⁸⁹, and is not a function of the limited volume of foreign beef actually imported into Korea. The fact that the WTO-consistent quota for beef has, save for two years, been fully utilized does not detract from the lack of equality of competitive conditions entailed by the dual retail system.

148. We believe, and so hold, that the treatment accorded to imported beef, as a consequence of the dual retail system established for beef by Korean law and regulation, is less favourable than the treatment given to like domestic beef and is, accordingly, not consistent with the requirements of Article III:4 of the GATT 1994.

149. It may finally be useful to indicate, however broadly, what we are *not* saying in reaching our above conclusion. We are *not* holding that a dual or parallel distribution system that is *not* imposed directly or indirectly by law or governmental regulation, but is rather solely the result of private entrepreneurs acting on their own calculations of comparative costs and benefits of differentiated distribution systems, is unlawful under Article III:4 of the GATT 1994. What is addressed by Article III:4 is merely the *governmental* intervention that affects the conditions under which like goods, domestic and imported, compete in the market within a Member's territory.

150. Finally, we note that Korea requires that imported beef be sold in a store displaying a sign declaring "Specialized Imported Beef Store". The Panel found that the sign requirement was "essentially ancillary to the dual retail system", and, since the dual retail system was inconsistent with Article III:4, the Panel found that the sign requirement was as well.⁹⁰ The Panel found also that, since the sign requirement went beyond an obligation to indicate origin, it was inconsistent with statements contained in a 1956 GATT Working Party Report.⁹¹ On appeal, Korea claims that the Panel used "erroneous logic" in its conclusion based on the ancillary character of the sign requirement, and that the statement in the Working Party Report did not apply to the sign requirement.⁹²

151. Without a system of specialized imported beef stores, the sign requirement would have no meaning and would not be required. When considered independently from a dual retail system, a sign

⁸⁹The notion of "perfect regulatory symmetry" is set out in Korea's appellant's submission, para. 95. See also *supra*, para. 17.

⁹⁰Panel Report, para. 641.

⁹¹Working Party Report, *Certificates of Origin, Marks of Origin, Consular Formalities*, adopted 17 November 1956, BISD 5S/102, para. 13.

⁹²Korea's appellant's submission, paras. 206-213.

requirement might or might not be characterized legally as consistent with Article III:4 of the GATT 1994. On the other hand, when considered simply as a detail of the dual retail system, the sign requirement partakes of the legal characterization given to that system itself. We believe it unnecessary to pass upon separately the consistency of the display sign requirement with Article III:4 of the GATT 1994.

B. *Article XX(d) of the GATT 1994*

152. The Panel went on to conclude that the dual retail system, which it found to be inconsistent with Article III:4, could *not* be justified pursuant to Article XX(d) of the GATT 1994. The Panel found that the dual retail system is a disproportionate measure not necessary to secure compliance with the Korean law against deceptive practices.⁹³

153. The Panel began its examination of Korea's dual retail system under Article XX(d) by finding that the dual retail system was designed to "secure compliance" with the *Unfair Competition Act*, a law consistent on its face with WTO provisions.⁹⁴ The Panel then focused on whether the dual retail system is "necessary" to secure compliance with that law. It examined enforcement measures taken by Korea for related products where fraudulent misrepresentation or passing of one product for another has occurred, and found that in these areas a dual retail system was not used. Instead, in respect of such product areas, Korea uses traditional enforcement measures, consistent with WTO rules, which include record-keeping, investigations, policing and fines. The Panel next inquired into whether these alternative, WTO-consistent measures were "reasonably available" to Korea to meet Korea's desired level of enforcement of laws against fraudulent misrepresentation in the retail beef sector. The Panel concluded that these measures are "reasonably available" alternative measures, and that Korea therefore cannot justify the dual retail system as "necessary" under Article XX(d).⁹⁵

154. Korea appeals the Panel's conclusion. Korea argues that the Panel incorrectly interpreted the term "necessary" in Article XX(d) as requiring *consistency* among enforcement measures taken in related product areas.⁹⁶ Further, according to Korea, the Panel neglected to take into account the *level of enforcement* that Korea sought with respect to preventing the fraudulent sale of imported beef.⁹⁷

⁹³Panel Report, para. 675.

⁹⁴*Ibid.*, para. 658.

⁹⁵*Ibid.*, paras. 660-674.

⁹⁶Korea's appellant's submission, paras. 166-180.

⁹⁷*Ibid.*, paras. 181-193.

155. Article XX(d), together with the introductory clause of Article XX, reads as follows:

Article XX

General Exceptions

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Member of measures:

...

(d) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including those relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the protection of patents, trade marks and copyrights, and the prevention of deceptive practices;

156. We note that in examining the Korean dual retail system under Article XX, the Panel followed the appropriate sequence of steps outlined in *United States – Standards for Reformulated and Conventional Gasoline* ("United States – Gasoline"). There we said:

In order that the justifying protection of Article XX may be extended to it, the measure at issue must not only come under one or another of the particular exceptions -- paragraphs (a) to (j) -- listed under Article XX; it must also satisfy the requirements imposed by the opening clauses of Article XX. *The analysis is, in other words, two-tiered: first, provisional justification by reason of characterization of the measure under XX(g); second, further appraisal of the same measure under the introductory clauses of Article XX.*⁹⁸ (emphasis added)

The Panel concentrated its analysis on paragraph (d), that is, the first-tier analysis. Having found that the dual retail system did not fulfill the requirements of paragraph (d), the Panel correctly considered that it did not need to proceed to the second-tier analysis, that is, to examine the application in this case of the requirements of the introductory clause of Article XX.

157. For a measure, otherwise inconsistent with GATT 1994, to be justified provisionally under paragraph (d) of Article XX, two elements must be shown. First, the measure must be one designed to "secure compliance" with laws or regulations that are not themselves inconsistent with some

⁹⁸ Appellate Body Report, WT/DS2/AB/R, adopted 20 May 1996, p. 22. See also, Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products* ("United States – Shrimp"), WT/DS58/AB/R, adopted 6 November 1998, paras. 119-121.

provision of the GATT 1994. Second, the measure must be "necessary" to secure such compliance. A Member who invokes Article XX(d) as a justification has the burden of demonstrating that these two requirements are met.⁹⁹

158. The Panel examined these two aspects one after the other. The Panel found, "despite ... troublesome aspects, ... that the dual retail system was put in place, at least in part, in order to secure compliance with the Korean legislation against deceptive practices to the extent that it serves to prevent acts inconsistent with the *Unfair Competition Act*."¹⁰⁰ It recognized that the system was established at a time when acts of misrepresentation of origin were widespread in the beef sector. It also acknowledged that the dual retail system "does appear to reduce the opportunities and thus the temptations for butchers to misrepresent [less expensive] foreign beef for [more expensive] domestic beef".¹⁰¹ The parties did not appeal these findings of the Panel.

159. We turn, therefore, to the question of whether the dual retail system is "necessary" to secure compliance with the *Unfair Competition Act*. Once again, we look first to the ordinary meaning of the word "necessary", in its context and in the light of the object and purpose of Article XX, in accordance with Article 31(1) of the *Vienna Convention*.

160. The word "necessary" normally denotes something "that cannot be dispensed with or done without, requisite, essential, needful".¹⁰² We note, however, that a standard law dictionary cautions that:

[T]his word must be considered in the connection in which it is used, as it is a word susceptible of various meanings. It may import absolute physical necessity or inevitability, or it may import that which is only convenient, useful, appropriate, suitable, proper, or conducive to the end sought. It is an adjective expressing degrees, and may express mere convenience or that which is indispensable or an absolute physical necessity.¹⁰³

⁹⁹ Appellate Body Report, *United States – Gasoline*, *supra*, footnote 98, pp. 22-23; Appellate Body Report, *United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India*, WT/DS33/AB/R, adopted 23 May 1997, pp. 14-16; Panel report, *United States – Section 337*, *supra*, footnote 69, para. 5.27.

¹⁰⁰ Panel Report, para. 658.

¹⁰¹ *Ibid*.

¹⁰² *The New Shorter Oxford English Dictionary*, (Clarendon Press, 1993), Vol. II, p. 1895.

¹⁰³ *Black's Law Dictionary*, (West Publishing, 1995), p. 1029.

161. We believe that, as used in the context of Article XX(d), the reach of the word "necessary" is not limited to that which is "indispensable" or "of absolute necessity" or "inevitable". Measures which are indispensable or of absolute necessity or inevitable to secure compliance certainly fulfil the requirements of Article XX(d). But other measures, too, may fall within the ambit of this exception. As used in Article XX(d), the term "necessary" refers, in our view, to a range of degrees of necessity. At one end of this continuum lies "necessary" understood as "indispensable"; at the other end, is "necessary" taken to mean as "making a contribution to." We consider that a "necessary" measure is, in this continuum, located significantly closer to the pole of "indispensable" than to the opposite pole of simply "making a contribution to".¹⁰⁴

162. In appraising the "necessity" of a measure in these terms, it is useful to bear in mind the context in which "necessary" is found in Article XX(d). The measure at stake has to be "necessary to ensure compliance with laws and regulations . . . , including those relating to customs enforcement, the enforcement of [lawful] monopolies . . . , the protection of patents, trade marks and copyrights, and the prevention of deceptive practices". (emphasis added) Clearly, Article XX(d) is susceptible of application in respect of a wide variety of "laws and regulations" to be enforced. It seems to us that a treaty interpreter assessing a measure claimed to be necessary to secure compliance of a WTO-consistent law or regulation may, in appropriate cases, take into account the relative importance of the common interests or values that the law or regulation to be enforced is intended to protect. The more vital or important those common interests or values are, the easier it would be to accept as "necessary" a measure designed as an enforcement instrument.

163. There are other aspects of the enforcement measure to be considered in evaluating that measure as "necessary". One is the extent to which the measure contributes to the realization of the end pursued, the securing of compliance with the law or regulation at issue. The greater the contribution, the more easily a measure might be considered to be "necessary". Another aspect is the extent to which the compliance measure produces restrictive effects on international commerce,¹⁰⁵ that is, in respect of a measure inconsistent with Article III-4, restrictive effects on *imported goods*.

¹⁰⁴We recall that we have twice interpreted Article XX(g), which requires a measure "relating to the conservation of exhaustible natural resources". (emphasis added). This requirement is more flexible textually than the "necessity" requirement found in Article XX(d). We note that, under the more flexible "relating to" standard of Article XX(g), we accepted in *United States – Gasoline* a measure because it presented a "substantial relationship", (emphasis added) i.e., a close and genuine relationship of ends and means, with the conservation of clean air. *Supra*, footnote 98, p.19. In *United States – Shrimp* we accepted a measure because it was "reasonably related" to the protection and conservation of sea turtles. *Supra*, footnote 98, at para. 141.

¹⁰⁵We recall that the last paragraph of the Preamble of the GATT of 1994 reads as follows: "Being desirous of contributing to these objectives by entering into reciprocal and mutually advantageous arrangements directed to the substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international commerce". (emphasis added)

A measure with a relatively slight impact upon imported products might more easily be considered as "necessary" than a measure with intense or broader restrictive effects.

164. In sum, determination of whether a measure, which is not "indispensable", may nevertheless be "necessary" within the contemplation of Article XX(d), involves in every case a process of weighing and balancing a series of factors which prominently include the contribution made by the compliance measure to the enforcement of the law or regulation at issue, the importance of the common interests or values protected by that law or regulation, and the accompanying impact of the law or regulation on imports or exports.

165. The panel in *United States – Section 337* described the applicable standard for evaluating whether a measure is "necessary" under Article XX(d) in the following terms:

It was clear to the Panel that a contracting party cannot justify a measure inconsistent with another GATT provision as "necessary" in terms of Article XX(d) if an alternative measure which it could reasonably be expected to employ and which is not inconsistent with other GATT provisions is available to it. By the same token, in cases where a measure consistent with other GATT provisions is not reasonably available, a contracting party is bound to use, among the measures reasonably available to it, that which entails the least degree of inconsistency with other GATT provisions.¹⁰⁶

166. The standard described by the panel in *United States – Section 337* encapsulates the general considerations we have adverted to above. In our view, the weighing and balancing process we have outlined is comprehended in the determination of whether a WTO-consistent alternative measure which the Member concerned could "reasonably be expected to employ" is available, or whether a less WTO-inconsistent measure is "reasonably available".

167. The Panel followed the standard identified by the panel in *United States – Section 337*. It started scrutinizing whether the dual retail system is "necessary" under paragraph (d) of Article XX by stating:

Korea has to convince the Panel that, contrary to what was alleged by Australia and the United States, no alternative measure consistent with the WTO Agreement is reasonably available at present in order to deal with misrepresentation in the retail market as to the origin of beef.¹⁰⁷

¹⁰⁶Panel report, *United States – Section 337*, *supra*, footnote 69, para. 5.26.

¹⁰⁷Panel Report, para. 659.

168. The Panel first considered a range of possible alternative measures, by examining measures taken by Korea with respect to situations involving, or which could involve, deceptive practices similar to those which in 1989-1990 had affected the retail sale of foreign beef. The Panel found that Korea does not require a dual retail system in *related product areas*, but relies instead on traditional enforcement procedures. There is no requirement, for example, for a dual retail system separating domestic Hanwoo beef from domestic dairy cattle beef.¹⁰⁸ Nor is there a requirement for a dual retail system for any other meat or food product, such as pork or seafood.¹⁰⁹ Finally, there is no requirement for a system of separate restaurants, depending on whether they serve domestic or imported beef, even though approximately 45 per cent of the beef imported into Korea is sold in restaurants.¹¹⁰ Yet, in all of these cases, the Panel found that there were numerous cases of fraudulent misrepresentation.¹¹¹ For the Panel, these examples indicated that misrepresentation of origin could, in principle, be dealt with "on the basis of basic methods . . . such as normal policing under the Korean *Unfair Competition Act*."¹¹²

169. Korea argues, on appeal, that the Panel, by drawing conclusions from the absence of any requirement for a dual retail system in related product areas, introduces an illegitimate "consistency test" into Article XX(d). For Korea, the proper test for "necessary" under Article XX(d):

... is to see whether another means exists which is less restrictive than the one used and which can reach the objective sought. Whether such means will be applied *consistently* to other products or not is not a matter of concern for the necessity requirement under Article XX(d).¹¹³

170. Examining enforcement measures applicable to the same illegal behaviour relating to like, or at least similar, products does not necessarily imply the introduction of a "consistency" requirement into the "necessary" concept of Article XX(d). Examining such enforcement measures may provide useful input in the course of determining whether an alternative measure which could "reasonably be expected" to be utilized, is available or not.

¹⁰⁸In 1998, domestic dairy cattle beef amounted to 12 percent of total beef consumption in Korea. Panel Report, para. 661.

¹⁰⁹*Ibid.*, para. 662.

¹¹⁰*Ibid.*, para. 663.

¹¹¹*Ibid.*, paras. 661-663, including footnote 366, in which the Panel noted "that the Livestock Times reported that the deceptive beef marketing practice was widespread in restaurants (where price differential was 58 per cent)".

¹¹²*Ibid.*, para. 664.

¹¹³Korea's appellant's submission, para. 167.

171. The enforcement measures that the Panel examined were measures taken to enforce the same law, the *Unfair Competition Act*.¹¹⁴ This law provides for penal and other sanctions¹¹⁵ against any "unfair competitive act", which includes any:

*Act misleading the public to understand the place of origin of any goods either by falsely marking that place on any commercial document or communication, in said goods or any advertisement thereof or in any manner of misleading the general public, or by selling, distributing, importing or exporting goods bearing such mark;*¹¹⁶ (emphasis added)

The language used in this law to define an "unfair competitive act" – "any manner of misleading the general public" – is broad. It applies to all the examples raised by the Panel – domestic dairy beef sold as Hanwoo beef, foreign pork or seafood sold as domestic product, as well as to imported beef served as domestic beef in restaurants.

172. The application by a Member of WTO-compatible enforcement measures to the same kind of illegal behaviour – the passing off of one product for another – for like or at least similar products, provides a suggestive indication that an alternative measure which could "reasonably be expected" to be employed may well be available. The application of such measures for the control of the same illegal behaviour for like, or at least similar, products raises doubts with respect to the objective necessity of a different, much stricter, and WTO-inconsistent enforcement measure. The Panel was, in our opinion, entitled to consider that the "examples taken from outside as well as within the beef sector indicate that misrepresentation of origin can indeed be dealt with on the basis of basic methods, consistent with the *WTO Agreement*, and thus less trade restrictive and less market intrusive, such as normal policing under the Korean *Unfair Competition Act*."¹¹⁷

173. Having found that possible alternative enforcement measures, consistent with the *WTO Agreement*, existed in other related product areas, the Panel went on to state that:

¹¹⁴In GATT case law, comparisons have been made between enforcement measures taken in different jurisdictions. In the *United States – Measures Affecting Alcoholic and Malt Beverages* case, the panel said that "[t]he fact that not all fifty states maintain discriminatory distribution systems indicates to the Panel that alternative measure for enforcement of state excise tax laws do indeed exist." Adopted 19 June 1992, BISD 39S/206, para. 5.43. In the *United States – Section 337* case, the panel "did not consider that a different scheme for imports alleged to infringe process patents is necessary, since many countries grant to their civil courts jurisdiction over imports of products manufactured abroad under processes protected by patents of the importing country". *Supra*, footnote 69, para. 5.28.

¹¹⁵*Unfair Competition Prevention and Business Secret Protection Act*, Article 2(1)(c), Article 8.

¹¹⁶*Unfair Competition Prevention and Business Secret Protection Act*, Article 2(1)(c) (from translation provided by Korea as Exhibit 28 of its second submission to the Panel).

¹¹⁷Panel Report, para. 664.

... it is for Korea to demonstrate that such an alternative measure is not reasonably available or is unreasonably burdensome, financially or technically, taking into account a variety of factors including the domestic costs of such alternative measure, to ensure that consumers are not misled as to the origin of beef.¹¹⁸

174. The Panel proceeded to examine whether the alternative measures or "basic methods" – investigations, prosecutions, fines, and record-keeping – which were used in related product areas, were "reasonably available" to Korea to secure compliance with the *Unfair Competition Act*. The Panel concluded "that Korea has not demonstrated to the satisfaction of the Panel that alternative measures consistent with the WTO Agreement were not reasonably available".¹¹⁹ Thus, as noted at the outset, the Panel found that the dual retail system was "a disproportionate measure not necessary to secure compliance with the Korean law against deceptive practices".¹²⁰ The dual retail system was, therefore, not justified under Article XX(d).¹²¹

175. Korea also argues on appeal that the Panel erred in applying Article XX(d) because it did not "pay due attention to the level of enforcement sought."¹²² For Korea, under Article XX(d), a panel must:

... examine whether a means reasonably available to the WTO Member could have been used in order to reach the objective sought without putting into question the level of enforcement sought.¹²³

For Korea, alternative measures must not only be reasonably available, but must also *guarantee* the level of enforcement sought which, in the case of the dual retail system, is the *elimination* of fraud in the beef retail market.¹²⁴ With respect to investigations, Korea argues that this tool can only reveal fraud *ex post*, whereas the dual retail system can combat fraudulent practices *ex ante*.¹²⁵ Korea contends that *ex post* investigations do not *guarantee* the level of enforcement that Korea has chosen, and therefore should not be considered. With respect to policing, Korea believes that this option is not "reasonably available", because Korea lacks the resources to police thousands of shops on a round-the-clock basis.

¹¹⁸ Panel Report, para. 665.

¹¹⁹ *Ibid.*, para. 674.

¹²⁰ *Ibid.*, para. 675.

¹²¹ *Ibid.*

¹²² Korea's appellant's submission, para. 182.

¹²³ *Ibid.*, para. 181.

¹²⁴ *Ibid.*, paras. 181, 185.

¹²⁵ *Ibid.*, para. 192.

176. It is not open to doubt that Members of the WTO have the right to determine for themselves the level of enforcement of their WTO-consistent laws and regulations. We note that this has also been recognized by the panel in *United States – Section 337*, where it said: "The Panel wished to make it clear that this [the obligation to choose a reasonably available GATT-consistent or less inconsistent measure] does not mean that a contracting party could be asked to change its substantive patent law or its desired *level of enforcement* of that law" (emphasis added) The panel added, however, the caveat that "provided that such law and such *level of enforcement* are the same for imported and domestically-produced products".¹²⁶

177. We recognize that, in establishing the dual retail system, Korea could well have intended to secure a higher level of enforcement of the prohibition, provided by the *Unfair Competition Act*, of acts misleading the public *about the origin of beef* (domestic or imported) *sold by retailers*, than the level of enforcement of the same prohibition of the *Unfair Competition Act* with respect to *beef served in restaurants*, or the sale by *retailers of other meat or food products*, such as *pork or seafood*.

178. We think it unlikely that Korea intended to establish a level of protection that *totally eliminates* fraud with respect to the origin of beef (domestic or foreign) sold by retailers. The total elimination of fraud would probably require a total ban of imports. Consequently, we assume that in effect Korea intended to *reduce considerably* the number of cases of fraud occurring with respect to the origin of beef sold by retailers. The Panel did find that the dual retail system "does appear to reduce the opportunities and thus the temptations for butchers to misrepresent foreign beef for domestic beef".¹²⁷ And we accept Korea's argument that the dual retail system *facilitates* control and permits combatting fraudulent practices *ex ante*. Nevertheless, it must be noted that the dual retail system is only an *instrument* to achieve a significant reduction of violations of the *Unfair Competition Act*. Therefore, the question remains whether other, conventional and WTO-consistent instruments can not reasonably be expected to be employed to achieve the same result.

179. Turning to investigations, the Panel found that Korea, in the past, had been able to distinguish imported beef from domestic beef, and had, in fact, published figures on the amount of imported beef fraudulently sold as domestic beef. This meant that Korea was able, in fact, to detect fraud.¹²⁸ On fines, the Panel found that these could be an effective deterrent, as long as they outweighed the

¹²⁶ Panel report, *United States – Section 337*, *supra*, footnote 69, para. 5.26.

¹²⁷ Panel Report, para. 658.

¹²⁸ *Ibid.*, para. 668.

potential profits from fraud.¹²⁹ On record-keeping, the Panel felt that if beef traders at all levels were required to keep records of their transactions, then effective investigations could be carried out.¹³⁰ Finally, on policing, the Panel noted that Korea had not demonstrated that the costs would be too high.¹³¹ For all these reasons, the Panel considered "that Korea has not demonstrated to the satisfaction of the Panel that alternative measures consistent with the WTO Agreement were not reasonably available".¹³² Thus, as already noted, the Panel found that the dual retail system was "a disproportionate measure not necessary to secure compliance with the Korean law against deceptive practices".¹³³

180. We share the Panel's conclusion. We are not persuaded that Korea could not achieve its desired level of enforcement of the *Unfair Competition Act* with respect to the origin of beef sold by retailers by using conventional WTO-consistent enforcement measures, if Korea would devote more resources to its enforcement efforts on the beef sector. It might also be added that Korea's argument about the lack of resources to police thousands of shops on a round-the-clock basis is, in the end, not sufficiently persuasive. Violations of laws and regulations like the Korean *Unfair Competition Act* can be expected to be routinely investigated and detected through selective, but well-targeted, controls of potential wrongdoers. The control of records will assist in selecting the shops to which the police could pay particular attention.

181. There is still another aspect that should be noted relating to both the method actually chosen by Korea – its dual retail system for beef – and alternative traditional enforcement measures. Securing through conventional, WTO-consistent measures a higher level of enforcement of the *Unfair Competition Act* with respect to the retail sale of beef, could well entail higher enforcement costs for the national budget. It is pertinent to observe that, through its dual retail system, Korea has in effect shifted all, or the great bulk, of these potential costs of enforcement (translated into a drastic reduction of competitive access to consumers) to imported goods and retailers of imported goods, instead of evenly distributing such costs between the domestic and imported products. In contrast, the more conventional, WTO-consistent measures of enforcement do not involve such onerous shifting of enforcement costs which ordinarily are borne by the Member's public purse.

¹²⁹Panel Report, para. 669.

¹³⁰*Ibid.*, para. 672.

¹³¹*Ibid.*, para. 673.

¹³²*Ibid.*, para. 674.

¹³³*Ibid.*, para. 675.

182. For these reasons, we uphold the conclusion of the Panel that Korea has not discharged its burden of demonstrating under Article XX(d) that alternative WTO-consistent measures were not "reasonably available" in order to detect and suppress deceptive practices in the beef retail sector¹³⁴, and that the dual retail system is therefore not justified by Article XX(d).¹³⁵

183. Korea further argues, on appeal, that the Panel did not make a separate finding on whether the display sign requirement was justified by Article XX(d), and requests that, should the Appellate Body uphold the Panel's finding that the sign requirement was inconsistent with Article III:4, it should proceed to consider the issue of its justification under Article XX(d).¹³⁶

184. We recall that Korean law requires an imported beef retailer to display a sign reading "Specialized Imported Beef Store".¹³⁷ Since the Panel correctly regarded the sign requirement as merely ancillary to the dual retail system, we consider that it is unnecessary to examine separately whether the display sign requirement can be justified under Article XX(d).

185. In sum, we uphold the Panel's conclusion that the dual retail system, which is inconsistent with Article III:4, is not justified under Article XX(d) of the GATT 1994.

VII. Findings and Conclusions

186. For the reasons set out in this Report, the Appellate Body:

- (a) upholds the Panel's conclusion that, under the Panel's terms of reference, the Panel was required to examine, pursuant to the complaining parties' claims, the commitment levels in Korea's Schedule and Annex 3 of the *Agreement on Agriculture*;
- (b) upholds the Panel's conclusion that Korea's domestic support for beef for 1997 and 1998 was not correctly calculated pursuant to Article 1(a)(ii) and Annex 3 of the *Agreement on Agriculture*;
- (c) reverses the Panel's finding on recalculated amounts of Korea's domestic support for beef in 1997 and 1998, as the Panel used, for these recalculations, a methodology inconsistent with Article 1(a)(ii) and Annex 3 of the *Agreement on Agriculture*; and

¹³⁴Panel Report, para. 674.

¹³⁵*Ibid.*, para. 675.

¹³⁶Korea's appellant's submission, paras. 217-223.

¹³⁷Panel Report, paras. 642-643.

reverses, therefore, the Panel's following conclusions, based on these recalculated amounts: (i) that Korea's domestic support for beef in 1997 and 1998 exceeded the *de minimis* level contrary to Article 6 of the *Agreement on Agriculture*; (ii) that Korea's failure to include Current AMS for beef in Korea's Current Total AMS was contrary to Article 7.2(a) of that Agreement; and (iii) that Korea's total domestic support for 1997 and 1998 exceeded Korea's commitment levels contrary to Article 3.2 of the *Agreement on Agriculture*;

- (d) is unable, in view of the insufficient factual findings made by the Panel, to complete the legal analysis of: (i) whether Korea's domestic support for beef exceeds the *de minimis* level contrary to Article 6 of the *Agreement on Agriculture*; (ii) whether the failure to include Current AMS for beef in Korea's Current Total AMS was contrary to Article 7.2(a) of that Agreement; and (iii) whether Korea's total domestic support for 1997 and 1998 exceeded Korea's commitment levels contrary to Article 3.2 of the *Agreement on Agriculture*;
- (e) upholds the Panel's ultimate conclusion that Korea's dual retail system for beef is inconsistent with Article III:4 of the GATT 1994;
- (f) upholds the Panel's conclusion that Korea's dual retail system for beef is not justified under Article XX(d) of the GATT 1994; and
- (g) finds it unnecessary to pass upon separately whether the ancillary sign requirement is consistent with Article III:4 or justified under Article XX(d) of the GATT 1994.

187. The Appellate Body recommends that the DSB request that Korea bring its measures found in this Report, and in the Panel Report as modified by this Report, to be inconsistent with Korea's obligations under the GATT 1994 and the *Agreement on Agriculture* into conformity with its obligations under those Agreements.

Signed in the original at Geneva this 2nd day of December 2000 by:

Claus-Dieter Ehlermann
Presiding Member

Florentino P. Feliciano
Member

Georges-Michel Abi-Saab
Member

World Trade Organization

India – Measures Affecting the Automotive Sector

Report of the Appellate Body, 19 March 2002

WORLD TRADE ORGANIZATION
APPELLATE BODY

India – Measures Affecting the Automotive Sector

AB-2002-1

Present:

India – *Appellant*
European Communities – *Appellee*
United States – *Appellee*

Ganesan, Presiding Member
Sacerdoti, Member
Taniguchi, Member

Korea – *Third Participant*

INDIA – MEASURES AFFECTING THE AUTOMOTIVE SECTOR

AB-2002-1

1. This appeal concerns the Panel Report, *India – Measures Affecting the Automotive Sector* (the "Panel Report").¹ The Panel was established to consider complaints by the United States and the European Communities relating to certain aspects of India's automotive components licensing policy as set forth in India's Public Notice No. 60² and the Memoranda of Understanding signed pursuant thereto. Public Notice No. 60 required each passenger car manufacturer in India to sign a Memorandum of Understanding ("MOU") with the Director General of Foreign Trade, and specified a number of conditions to be included in such MOUs.³

2. This dispute concerns two of the conditions stipulated by Public Notice No. 60 and included in each MOU, namely: (i) an "indigenization" requirement, whereby each car manufacturer was obliged to achieve indigenization, or local content, of a minimum level of 50 percent by the third year from the date of its first import of cars in the form of completely and semi-knocked down kits ("CKD/SKD kits"), or certain automobile components, and 70 percent by the fifth year from that date; and (ii) a "trade balancing requirement", whereby each car manufacturer was obliged to balance, over the period of the MOU, the value of its imports of CKD/SKD kits and components with the value of its exports of cars and components.⁴ At the time Public Notice No. 60 was issued, India maintained import restrictions and a discretionary import licensing scheme for, *inter alia*, automobile CKD/SKD kits and components. A manufacturer that failed to comply with the conditions set forth in Public Notice No. 60 and the MOUs could be denied a licence to import CKD/SKD kits and components.

Report of the Appellate Body

¹WT/DS146/R, WT/DS175/R, 21 December 2001.

²Public Notice No. 60 was issued on 12 December 1997 by the Government of India's Ministry of Commerce, acting pursuant to the Foreign Trade (Development and Regulation) Act of 1992. (Panel Report, para. 2.4)

³Panel Report, paras. 2.4 and 2.5 and Annex Tables 1 and 2.

⁴*Ibid.*

India abolished its import restrictions and related discretionary import licensing scheme, including the restrictions and licensing requirements applicable to CKD/SKD kits and components, on 1 April 2001. This occurred during the course of the Panel proceedings. The relevant factual aspects of this dispute are set out in greater detail in paragraphs 2.1 through 2.5 of the Panel Report.

3. On 15 May 2000, the United States requested the establishment of a panel to examine the consistency of the measures at issue with Articles III:4 and XI:1 of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994"), and Articles 2.1 and 2.2 of the *Agreement on Trade-Related Investment Measures* (the "*TRIMS Agreement*").⁵ On 12 October 2000, the European Communities requested the establishment of a panel to examine the consistency of the measures at issue with Articles III:4 and XI:1 of the GATT 1994, and Article 2.1 of the *TRIMS Agreement*.⁶ The European Communities also specifically requested the Panel to find that the measures at issue were inconsistent with these provisions of the covered agreements as of the date of establishment of the Panel, and that they had remained so after 1 April 2001.⁷ Pursuant to Article 10.2 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), Korea and Japan reserved their third party rights in the dispute.⁸

4. In its Report, circulated on 21 December 2001, the Panel found that:

- (a) India acted inconsistently with its obligations under Article III:4 of the GATT 1994 by imposing on automotive manufacturers, under the terms of Public Notice No. 60 and the MOUs signed thereunder, an obligation to use a certain proportion of local parts and components in the manufacture of cars and automotive vehicles ("indigenization" condition);
- (b) India acted inconsistently with its obligations under Article XI of the GATT 1994 by imposing on automotive manufacturers, under the terms of Public Notice No. 60 and the MOUs signed thereunder, an obligation to balance any importation of certain kits and components with exports of equivalent value ("trade balancing" condition); [and]

⁵ WT/DS175/4.

⁶ WT/DS146/4. At its meeting on 17 November 2000, the Dispute Settlement Body agreed, in accordance with Article 9.1 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes*, that the Panel established on 27 July 2000 to examine the complaint by the United States should also examine the complaint by the European Communities. (Panel Report, para. 1.4; WT/DSB/M/92)

⁷ Panel Report, para. 3.5.

⁸ *Ibid.*, para. 1.6.

(c) India acted inconsistently with its obligations under Article III:4 of the GATT 1994 by imposing, in the context of the trade balancing condition under the terms of Public Notice No. 60 and the MOUs signed thereunder, an obligation to offset the amount of any purchases of previously imported restricted kits and components on the Indian market, by exports of equivalent value.⁹

5. In the light of its findings that the measures at issue were inconsistent with Articles III:4 and XI:1 of the GATT 1994, the Panel was of the view that it was not necessary to address the claims made by the European Communities and the United States under the *TRIMS Agreement*.¹⁰

6. The Panel then went on to give "separate consideration" to:

... whether the events which took place subsequently, including on or after 1 April 2001, might have affected the existence of any violations identified and ... whether those events affect the nature or range of any recommendations [the Panel] may make to the DSB in accordance with Article 19.1 of the DSU.¹¹

7. More specifically, the Panel:

... felt that it would not be making an "objective assessment of the matter before it", or assisting the DSB in discharging its responsibilities under the DSU in accordance with Article 11 of the DSU, had it chosen not to address the impact of events having taken place in the course of the proceedings, in assessing the appropriateness of making a recommendation under Article 19.1 of the DSU.¹²

8. Having considered the events that took place during the Panel proceedings, the Panel found that:

... the indigenization conditions contained in Public Notice No. 60 and in the MOUs, as they have continued to exist and apply after 1 April 2001, have remained in violation of the relevant GATT provisions.¹³

⁹ Panel Report, para. 8.1.

¹⁰ *Ibid.*, para. 7.324.

¹¹ *Ibid.*, para. 8.3.

¹² *Ibid.*, para. 8.28.

¹³ *Ibid.*, para. 8.47.

... the trade balancing conditions contained in Public Notice No. 60 and in the MOUs, as they have continued to exist and apply after 1 April 2001, have remained in violation of the relevant GATT provisions.¹⁴

9. The Panel consequently recommended that the Dispute Settlement Body (the "DSB") request India to bring its measures into conformity with its obligations under the *Marrakesh Agreement Establishing the World Trade Organization* (the "*WTO Agreement*").¹⁵

10. On 31 January 2002, India notified the DSB of its decision to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, pursuant to paragraph 4 of Article 16 of the DSU, and filed a Notice of Appeal with the Appellate Body pursuant to Rule 20 of the *Working Procedures for Appellate Review* (the "*Working Procedures*"). In this Notice of Appeal, India stated that:

India seeks review by the Appellate Body of the Panel's conclusion that Articles 11 and 19.1 of the DSU required it to address the question of whether the measures found [to] be inconsistent with Articles III:4 and XI:1 of the General Agreement on Tariffs and Trade 1994 ("GATT") had been brought into conformity with the GATT as a result of measures taken by India during the course of the proceedings.

India further seeks review by the Appellate Body of the Panel's conclusion that the enforcement of the export obligations that automobile manufacturers incurred until 1 April 2001 under India's former import licensing scheme is inconsistent with Articles III:4 and XI:1 of the GATT.

India considers these conclusions of the Panel to be in error and based upon erroneous findings on issues of law and related legal interpretations.¹⁶

11. On 11 February 2002, India filed an appellant's submission.¹⁷ The European Communities and the United States each filed an appellee's submission on 25 February 2002.¹⁸ On the same day, Korea filed a third participant's submission.¹⁹

¹⁴Panel Report, para. 8.61.

¹⁵*Ibid.*, para. 8.65.

¹⁶WT/DS146/8, WT/DS175/8, 31 January 2002.

¹⁷Pursuant to Rule 21(1) of the *Working Procedures*.

¹⁸Pursuant to Rule 22(1) of the *Working Procedures*.

¹⁹Pursuant to Rule 24 of the *Working Procedures*.

12. On 25 February 2002, the Appellate Body received a letter from Japan indicating that Japan would not be filing a written submission in this appeal, but that Japan wished to attend the oral hearing.²⁰ By letter dated 27 February 2002, the Appellate Body Secretariat informed Japan, the participants and the third participant that the Division hearing this appeal was "inclined to allow Japan to attend the oral hearing as a passive observer, if none of the participants or third participants object." On 1 March 2002 and 4 March 2002, respectively, the Appellate Body received written responses from the European Communities and the United States.

13. Taking account of the views expressed by the European Communities and the United States, the Division on 5 March 2002 informed Japan, the participants, and the third participant, that although Japan had not filed a written submission as a third participant, Japan would be allowed to attend the oral hearing as a passive observer, that is, to attend the oral hearing and hear the oral statements and responses to questioning by the participants and the third participant in this appeal.

14. In accordance with the Working Schedule for Appeal communicated to the parties and the third parties on 1 February 2002, the oral hearing in the appeal was scheduled to be held on 15 March 2002.²¹

15. On 14 March 2002, the Appellate Body received a letter from India, in which India stated that:

Pursuant to Rule 30(1) of the *Working Procedures for Appellate Review*, this is to inform the Appellate Body that India is withdrawing the above-mentioned appeal; oral hearing on this is scheduled for 15 March 2002. Inconvenience caused to the Appellate Body, Secretariat, the other parties and the third participants is deeply regretted.

16. Rule 30(1) of the *Working Procedures* provides that:

At any time during an appeal, the appellant may withdraw its appeal by notifying the Appellate Body, which shall forthwith notify the DSB.

17. Upon receipt of India's letter of 14 March 2002, the Appellate Body on the same day notified the DSB, pursuant to Rule 30(1) of the *Working Procedures*, that India "has notified the Appellate Body that India is withdrawing its appeal" in this dispute²², and simultaneously informed India, the

²⁰Japan had reserved its rights to participate as a third party in the proceedings before the Panel; Panel Report, para. 1.6.

²¹Pursuant to Rule 27 of the *Working Procedures*.

²²WT/DS146/9, WT/DS175/9, 14 March 2002.

European Communities, the United States, Korea and Japan that the oral hearing in this appeal was cancelled.

18. In view of India's withdrawal of the appeal by its letter of 14 March 2002, the Appellate Body hereby completes its work in this appeal.

Signed in the original at Geneva this 15th day of March 2002 by:

A. V. Ganesan
Presiding Member

Giorgio Sacerdoti
Member

Yasuhei Tamiguchi
Member

World Trade Organization

**European Communities – Conditions for the Granting of
Tariff Preferences to Developing Countries**

Report of the Appellate Body, 7 April 2004

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EUROPEAN COMMUNITIES – CONDITIONS FOR THE GRANTING
OF TARIFF PREFERENCES TO DEVELOPING COUNTRIES

AB-2004-1

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Argentina – Footwear (EC)	Appellate Body Report, <i>Argentina – Safeguard Measures on Imports of Footwear</i> , WT/DS121/AB/R, adopted 12 January 2000, DSR 2000:1, 515	US – Certain EC Products	Appellate Body Report, <i>United States – Import Measures on Certain Products from the European Communities</i> , WT/DS165/AB/R, adopted 10 January 2001, DSR 2001:1, 373
Brazil – Aircraft	Appellate Body Report, <i>Brazil – Export Financing Programme for Aircraft</i> , WT/DS46/AB/R, adopted 20 August 1999, DSR 1999:III, 1161	US – Customs User Fee	GATT Panel Report, <i>United States – Customs User Fee</i> , L/6264, adopted 2 February 1988, BISD 35S/245
Brazil – Desiccated Coconut	Appellate Body Report, <i>Brazil – Measures Affecting Desiccated Coconut</i> , WT/DS22/AB/R, adopted 20 March 1997, DSR 1997:1, 167	US – FSC	Appellate Body Report, <i>United States – Tax Treatment for “Foreign Sales Corporations”</i> , WT/DS108/AB/R, adopted 20 March 2000, DSR 2000:III, 1619
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Canada – FIRA	GATT Panel Report, <i>Canada – Administration of the Foreign Investment Review Act</i> , L/5504, adopted 7 February 1984, BISD 30S/140	US – Gasoline	Appellate Body Report, <i>United States – Standards for Reformulated and Conventional Gasoline</i> , WT/DS2/AB/R, adopted 20 May 1996, DSR 1996:1, 3
Canada – Ice Cream and Yoghurt	GATT Panel Report, <i>Canada – Import Restrictions on Ice Cream and Yoghurt</i> , L/6568, adopted 5 December 1989, BISD 36S/68	US – Gasoline	Panel Report, <i>United States – Standards for Reformulated and Conventional Gasoline</i> , WT/DS2/R, adopted 20 May 1996, as modified by the Appellate Body Report, WT/DS2/AB/R, DSR 1996:1, 29
Chile – Price Band System	Appellate Body Report, <i>Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products</i> , WT/DS207/AB/R, adopted 23 October 2002	US – Malt Beverages	GATT Panel Report, <i>United States – Measures Affecting Alcoholic and Malt Beverages</i> , DS23/R, adopted 19 June 1992, BISD 39S/206
EC – Bananas III	Appellate Body Report, <i>European Communities – Regime for the Importation, Sale and Distribution of Bananas</i> , WT/DS27/AB/R, adopted 25 September 1997, DSR 1997:II, 591	US – MFN Footwear	GATT Panel Report, <i>United States – Denial of Most-Favoured-Nation Treatment as to Non-Rubber Footwear from Brazil</i> , DS18/R, adopted 19 June 1992, BISD 39S/128
EC – Hormones	Appellate Body Report, <i>EC Measures Concerning Meat and Meat Products (Hormones)</i> , WT/DS26/AB/R, WT/DS48/AB/R, adopted 13 February 1998, DSR 1998:1, 135	US – Section 337	GATT Panel Report, <i>United States Section 337 of the Tariff Act of 1930</i> , L/6439, adopted 7 November 1989, BISD 36S/345
EC – Sardines	Appellate Body Report, <i>European Communities – Trade Description of Sardines</i> , WT/DS231/AB/R, adopted 23 October 2002	US – Section 211 Appropriations Act	Appellate Body Report, <i>United States – Section 211 Omnibus Appropriations Act of 1998</i> , WT/DS176/AB/R, adopted 1 February 2002
EC – Tariff Preferences	Panel Report, <i>European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries</i> , WT/DS246/R, circulated to Members 1 December 2003	US – Shrimp	Appellate Body Report, <i>United States – Import Prohibition of Certain Shrimp and Shrimp Products</i> , WT/DS58/AB/R, adopted 6 November 1998, DSR 1998:VII, 2755
EEC – Dessert Apples	GATT Panel Report, <i>European Economic Community – Restrictions on Imports of Dessert Apples – Complaint by Chile</i> , L/6491, adopted 22 June 1989, BISD 36S/93	US – Wool Shirts and Blouses	Appellate Body Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/AB/R and Corr.1, adopted 23 May 1997, DSR 1997:1, 323
Guatemala – Cement I	Appellate Body Report, <i>Guatemala – Anti-Dumping Investigation Regarding Portland Cement from Mexico</i> , WT/DS60/AB/R, adopted 25 November 1998, DSR 1998:IX, 3767	US – Wool Shirts and Blouses	Panel Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/R, adopted 23 May 1997, as upheld by the Appellate Body Report, WT/DS33/AB/R, DSR 1997:1, 343
India – Quantitative Restrictions	Appellate Body Report, <i>India – Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products</i> , WT/DS90/AB/R, adopted 22 September 1999, DSR 1999:IV, 1763	US – Wool Shirts and Blouses	
Japan – Agricultural Products I	GATT Panel Report, <i>Japan – Restrictions on Imports of Certain Agricultural Products</i> , L/6253, adopted 2 March 1988, BISD 35S/163		
Korea – Dairy	Appellate Body Report, <i>Korea – Definitive Safeguard Measure on Imports of Certain Dairy Products</i> , WT/DS98/AB/R, adopted 12 January 2000, DSR 2000:1, 3		
US – Carbon Steel	Appellate Body Report, <i>United States – Countervailing Duties on Certain Corrosion-Resistant Carbon Steel Flat Products from Germany</i> , WT/DS213/AB/R and Corr.1, adopted 19 December 2002		

WORLD TRADE ORGANIZATION
APPELLATE BODY

TABLE OF ABBREVIATIONS USED IN THIS REPORT

Abbreviation	Description
1971 Waiver Decision	Waiver Decision on the Generalized System of Preferences, GATT Document L/3545, 25 June 1971, BISD 18S/24 (attached as Annex D-2 to the Panel Report)
1999 LDC Waiver	Waiver Decision on Preferential Tariff Treatment for Least-Developed Countries, WT/L/304, 15 June 1999
Agreed Conclusions	Agreed Conclusions of the UNCTAD Special Committee on Preferences (attached as Annex D-4 to the Panel Report)
Charter of Algiers	Charter of Algiers, TD/38, adopted at the Ministerial Meeting of the Group of 77 on 24 October 1967
Drug Arrangements	Special arrangements to combat drug production and trafficking, contained in the Regulation
DSU	<i>Understanding on Rules and Procedures Governing the Settlement of Disputes</i>
Enabling Clause	Decision on Differential and More Favourable Treatment, Reciprocity, and Fuller Participation of Developing Countries, GATT Document L/4903, 28 November 1979, BISD 26S/203 (attached as Annex 2 to this Report)
GATT 1947	<i>General Agreement on Tariffs and Trade 1947</i>
GATT 1994	<i>General Agreement on Tariffs and Trade 1994</i>
General Arrangements	General arrangements described in Article 7 of the Regulation
General Principle Eight	General Principle Eight contained in the Final Act and Report adopted at the First Session of UNCTAD on 15 June 1964, at p. 20 (Exhibit EC-20 submitted by the European Communities to the Panel)
GSP	Generalized System of Preferences
MFN	Most-favoured-nation
OECD Special Report	Report of the Special Group of the Organization for Economic Co-operation and Development (OECD) on Trade with Developing Countries, TD/56, 29 January 1968
Regulation	Council Regulation (EC) No. 2501/2001 of 10 December 2001 applying a scheme of generalised tariff preferences for the period from 1 January 2002 to 31 December 2004, <i>Official Journal of the European Communities</i> , L Series, No. 346 (31 December 2001), p. 1 (Exhibit India-6 submitted by India to the Panel)
Resolution 21(II)	Resolution 21(II) of the Second Session of UNCTAD, entitled "Expansion and Diversification of Exports of Manufactures and Semi-Manufactures of Developing Countries" (attached as Annex D-3 to the Panel Report)
SCM Agreement	<i>Agreement on Subsidies and Countervailing Measures</i>
SPS Agreement	<i>Agreement on the Application of Sanitary and Phytosanitary Measures</i>
UNCTAD	United Nations Conference on Trade and Development
<i>Vienna Convention</i>	<i>Vienna Convention on the Law of Treaties</i> , done at Vienna, 23 May 1969, 1155 U.N.T.S. 331; 8 International Legal Materials 679
<i>Working Procedures</i>	<i>Working Procedures for Appellate Review</i> , WT/AB/WP/7, 1 May 2003
WTO	World Trade Organization
<i>WTO Agreement</i>	<i>Marrakesh Agreement Establishing the World Trade Organization</i>

AB-2004-1

Present:

Abi-Saab, Presiding Member
Baptista, Member
Sacerdoti, Member

European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries

European Communities, *Appellant*
India, *Appellee*

Bolivia, *Third Participant*
Brazil, *Third Participant*
Colombia, *Third Participant*
Costa Rica, *Third Participant*
Cuba, *Third Participant*
Ecuador, *Third Participant*
El Salvador, *Third Participant*
Guatemala, *Third Participant*
Honduras, *Third Participant*
Mauritius, *Third Participant*
Nicaragua, *Third Participant*
Pakistan, *Third Participant*
Panama, *Third Participant*
Paraguay, *Third Participant*
Peru, *Third Participant*
United States, *Third Participant*
Venezuela, *Third Participant*

I. Introduction

1. The European Communities appeals certain issues of law and legal interpretations developed in the Panel Report, *European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries* (the "Panel Report").¹ The Panel was established to consider a complaint by India against the European Communities regarding the conditions under which the European Communities accords tariff preferences to developing countries pursuant to Council Regulation (EC) No. 2501/2001 of 10 December 2001 "applying a scheme of generalised tariff preferences for the period from 1 January 2002 to 31 December 2004" (the "Regulation").²

¹WT/DS246/R, 1 December 2003.

²*Official Journal of the European Communities*, L Series, No. 346 (31 December 2001), p. 1 (Exhibit India-6 submitted by India to the Panel).

2. The Regulation provides for five preferential tariff "arrangements"³, namely:
- (a) general arrangements described in Article 7 of the Regulation (the "General Arrangements");
 - (b) special incentive arrangements for the protection of labour rights;
 - (c) special incentive arrangements for the protection of the environment;
 - (d) special arrangements for least-developed countries; and
 - (e) special arrangements to combat drug production and trafficking (the "Drug Arrangements").⁴

3. All the countries listed in Annex I to the Regulation are eligible to receive tariff preferences under the General Arrangements⁵, which provide, broadly, for suspension of Common Customs Tariff duties on products listed as "non-sensitive" and for reduction of Common Customs Tariff *ad valorem* duties on products listed as "sensitive".⁶ The General Arrangements are described in further detail in paragraphs 2.4 and 2.5 of the Panel Report. The four other arrangements in the Regulation provide tariff preferences *in addition* to those granted under the General Arrangements.⁷ However, only some of the country beneficiaries of the General Arrangements are also beneficiaries of the other arrangements. Specifically, preferences under the special incentive arrangements for the protection of labour rights and the special incentive arrangements for the protection of the environment are restricted to those countries that "are determined by the European Communities to comply with certain labour [or] environmental policy standards"⁸, respectively. Preferences under the special arrangements for least-developed countries are restricted to certain specified countries.⁹ Finally, preferences under the Drug Arrangements are provided only to 12 predetermined countries, namely Bolivia, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Nicaragua, Pakistan, Panama, Peru, and Venezuela.¹⁰

³Regulation, Art. 1.2.

⁴*Ibid.*

⁵Panel Report, para. 2.4.

⁶Regulation, Arts. 7.1-7.2.

⁷*Ibid.*, Arts. 8-10. For example, these tariff preferences include further reductions in the duties imposed on certain "sensitive" products.

⁸Panel Report, para. 2.3. See Regulation, Arts. 14 and 21, and Annex I (Columns E and G).

⁹Regulation, Annex I (Column H).

¹⁰*Ibid.* (Column I); Panel Report, paras. 2.3 and 2.7.

4. India is a beneficiary of the General Arrangements but not of the Drug Arrangements, or of any of the other arrangements established by the Regulation. In its request for the establishment of a panel, India challenged the Drug Arrangements as well as the special incentive arrangements for the protection of labour rights and the environment.¹¹ However, in a subsequent meeting with the Director-General regarding the composition of the Panel—and later in writing to the European Communities—India indicated its decision to limit its complaint to the Drug Arrangements, while reserving its right to bring additional complaints regarding the two "special incentive arrangements".¹² Accordingly, this dispute concerns only the Drug Arrangements.

5. The Panel summarized the effect of the Drug Arrangements as follows:

The result of the Regulation is that the tariff reductions accorded under the Drug Arrangements to the 12 beneficiary countries are greater than the tariff reductions granted under the General Arrangements to other developing countries. In respect of products that are included in the Drug Arrangements but not in the General Arrangements, the 12 beneficiary countries are granted *duty-free* access to the European Communities' market, while all other developing countries must pay the *full duties applicable under the Common Customs Tariff*. In respect of products that are included in both the Drug Arrangements and the General Arrangements and that are deemed "sensitive" under column G of Annex IV to the Regulation with the exception for products of CN codes 0306 13, 1704 10 91 and 1704 10 99, the 12 beneficiary countries are granted *duty-free* access to the European Communities' market, while all other developing countries are entitled only to *reductions in the duties applicable under the Common Customs Tariff*.¹³ (original italics)

6. India requested the Panel to find that "the Drug Arrangements set out in Article 10"¹⁴ of the Regulation are inconsistent with Article I:1 of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994") and are not justified by the Decision on Differential and More Favourable Treatment, Reciprocity, and Fuller Participation of Developing Countries (the "Enabling Clause").¹⁵ In the Panel Report, circulated to Members of the World Trade Organization (the "WTO") on 1 December 2003, the Panel concluded that:

¹¹Request for the establishment of a panel by India, WT/DS246/4, 9 December 2002, p. 2.

¹²Panel Report, para. 1.5.

¹³*Ibid.*, para. 2.8. See also, *ibid.*, para. 2.7.

¹⁴*Ibid.*, para. 3.1 (referring to India's first written submission to the Panel, para. 67).

¹⁵GATT Document L/4903, 28 November 1979, BISD 26S/203 (attached as Annex 2 to this Report).

- (a) India has the burden of demonstrating that the European Communities' Drug Arrangements are inconsistent with Article I:1 of GATT 1994;
- (b) India has demonstrated that the European Communities' Drug Arrangements are inconsistent with Article I:1 of GATT 1994;
- (c) the European Communities has the burden of demonstrating that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause; [and]
- (d) the European Communities has failed to demonstrate that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause.¹⁶

The Panel also concluded that the European Communities had "failed to demonstrate that the Drug Arrangements are justified under Article XX(b) of GATT 1994".¹⁷ Finally, the Panel concluded, pursuant to Article 3.8 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), that "because the Drug Arrangements are inconsistent with Article I:1 of GATT 1994 and not justified by Article 2(a) of the Enabling Clause or Article XX(b) of GATT 1994, the European Communities has nullified or impaired benefits accruing to India under GATT 1994."¹⁸

7. On 8 January 2004, the European Communities notified the Dispute Settlement Body of its intention to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, pursuant to paragraph 4 of Article 16 of the DSU, and filed a Notice of Appeal¹⁹ pursuant to Rule 20 of the *Working Procedures for Appellate Review* (the "*Working Procedures*").²⁰ On 19 January 2004, the European Communities filed its appellant's submission.²¹ On 30 January 2004, Pakistan notified its intention to appear at the oral hearing as a third participant.²² On 2 February 2004, India filed its appellee's submission.²³ On the same day, Costa Rica, Panama, Paraguay, and the United States each filed a third participant's submission, and Bolivia, Colombia, Ecuador, Peru, and Venezuela filed a joint third participant's submission as the Andean Community.²⁴ Also on 2 February 2004, Brazil notified its intention to make a statement at the oral

¹⁶Panel Report, para. 8.1(a)-(d).

¹⁷*Ibid.*, para. 8.1(e).

¹⁸*Ibid.*, para. 8.1(f).

¹⁹Notification of an appeal by the European Communities, WT/DS246/7, 8 January 2004 (attached as Annex 1 to this Report).

²⁰WT/AB/WP/7, 1 May 2003.

²¹Pursuant to Rule 21 of the *Working Procedures*.

²²Pursuant to Rule 24(2) of the *Working Procedures*.

²³Pursuant to Rule 22 of the *Working Procedures*.

²⁴Pursuant to Rule 24(1) of the *Working Procedures*.

hearing as a third participant, and Mauritius notified its intention to appear at the oral hearing as a third participant.²⁵ Finally, on 2 February 2004, El Salvador, Guatemala, Honduras, and Nicaragua jointly notified their intention to make a statement at the oral hearing as third participants.²⁶ On 4 February 2004, Cuba notified its intention to appear at the oral hearing as a third participant.²⁷ By letter dated 16 February 2004, Pakistan submitted a request to make a statement at the oral hearing.²⁸ No participant objected to Pakistan's request, which was authorized by the Division hearing the appeal on 18 February 2004.²⁹

8. The oral hearing in this appeal was held on 19 February 2004. The participants and third participants presented oral arguments (with the exception of Cuba and Mauritius) and responded to questions posed by the Members of the Division hearing the appeal.

II. Arguments of the Participants and Third Participants

A. Claims of Error by the European Communities – Appellant

1. The Relationship Between Article I:1 of the GATT 1994 and the Enabling Clause

9. The European Communities argues that the Panel erred in finding that the Enabling Clause is an "exception" to Article I:1 of the GATT 1994 and in assigning to the European Communities the burden of justifying the Drug Arrangements under the Enabling Clause. Furthermore, the European Communities submits, the Panel erred in finding that Article I:1 applies to measures covered by the Enabling Clause. The European Communities requests the Appellate Body to reverse the Panel's consequent finding that the Drug Arrangements are inconsistent with Article I:1 of the GATT 1994 and, because India made no claim with respect to the Enabling Clause, to refrain from assessing the Drug Arrangements under the Enabling Clause.

10. According to the European Communities, the Panel's main reason for deciding that the Enabling Clause is an exception to Article I:1 was that the Enabling Clause does not provide "positive

²⁵Pursuant to Rule 24(2) of the *Working Procedures*.

²⁶*Ibid.*

²⁷Pursuant to Rule 24(4) of the *Working Procedures*.

²⁸*Ibid.*

²⁹Pursuant to Rule 27(3)(c) of the *Working Procedures*. The Director of the Appellate Body Secretariat advised Pakistan and the other participants in the appeal of the Division's decision by letter dated 18 February 2004.

rules establishing obligations in themselves".³⁰ In the European Communities' view, however, the fact that developed countries are not legally obliged to implement schemes pursuant to the Generalized System of Preferences ("GSP") does not mean that the Enabling Clause does not impose positive obligations, or that it is an exception to Article I:1. The European Communities argues that the Panel's reasoning suggests that, if a WTO provision applies only when a WTO Member takes a particular step that it is not obliged to take, that provision cannot create a positive obligation and must be an exception. According to the European Communities, this test is not consistent with Appellate Body decisions and "would lead to manifestly absurd results".³¹ For example, the European Communities contends, this test would mean that the following provisions do not impose positive rules establishing obligations in themselves, despite contrary reasoning in previous Appellate Body decisions: Article 27.4 of the *Agreement on Subsidies and Countervailing Measures* (the "SCM Agreement"); Article 3.3 of the *Agreement on the Application of Sanitary and Phytosanitary Measures* (the "SPS Agreement"); Article 2.4 of the *Agreement on Technical Barriers to Trade*; and Article 6 of the *Agreement on Textiles and Clothing*.³² According to the European Communities, Articles VI and XIX of the GATT 1994 would also be rendered exceptions under the Panel's reasoning, contrary to well-established GATT and WTO panel practice.

11. The European Communities suggests that the Panel should have begun its analysis by examining the ordinary meaning of the word "notwithstanding" in the Enabling Clause. This ordinary meaning, in the view of the European Communities, does not compel the Panel's finding that the Enabling Clause is an "exception" to Article I:1. This is apparent from the dissenting opinion in the Panel Report and the Panel's own recognition that the definition of "notwithstanding" is not dispositive of this question. Therefore, the European Communities argues, in accordance with the basic rules of treaty interpretation in Article 31 of the *Vienna Convention on the Law of Treaties* (the "*Vienna Convention*")³³, the Panel should have proceeded to examine the relevant "content",³⁴ context, and object and purpose of the Enabling Clause in order to identify the relationship between

³⁰European Communities' appellant's submission, para. 32 (quoting Panel Report, para. 7.35, itself quoting Appellate Body Report, *US – Wool Shirts and Blouses*, p. 16, DSR 1997:1, at 337).

³¹*Ibid.*, para. 34.

³²*Ibid.*, para. 35 (referring to Appellate Body Report, *Brazil – Aircraft*, paras. 134-141; Appellate Body Report, *EC – Hormones*, paras. 97-104; Appellate Body Report, *EC – Sardines*, para. 275; and Appellate Body Report, *US – Wool Shirts and Blouses*, pp. 12-17, DSR 1997:1, at 333-338).

³³Done at Vienna, 23 May 1969, 1155 U.N.T.S. 331; 8 International Legal Materials 679.

³⁴European Communities' appellant's submission, paras. 18 and 39, and heading 2.5.1.

the Enabling Clause and Article I:1. Instead, the European Communities observes, the Panel simply "assumed"³⁵ that the Enabling Clause is an exception to Article I:1.

12. Turning to the content and context of the Enabling Clause, the European Communities submits that the Enabling Clause provides a comprehensive set of rules that positively regulate the substantive content of GSP schemes, to the exclusion of the rules in Article I:1 of the GATT 1994. Specifically, the European Communities emphasizes that the words "generalized, non-reciprocal and non-discriminatory" in footnote 3 of the Enabling Clause are distinct from and are intended to replace the most-favoured-nation ("MFN") obligation in Article I:1. The European Communities also argues that, according to the Panel's own reasoning, footnote 3 should be interpreted in the context of the Agreed Conclusions of the Special Committee on Preferences of the United Nations Conference on Trade and Development (the "Agreed Conclusions")³⁶ and the submissions by developed countries to that committee. As such, the detailed obligations created by paragraph 2(a), footnote 3, and paragraph 3(c) of the Enabling Clause go far beyond "mere 'anti-abuse' safeguards".³⁷ The European Communities contends that the Enabling Clause is unlike the chapeau of Article XX of the GATT 1994, which neither regulates the substantive content of measures adopted by Members, nor replaces the substantive rules from which Article XX derogates.

13. The European Communities relies in support of its argument on the position of the Enabling Clause within the GATT 1994 and the *Marrakesh Agreement Establishing the World Trade Organization* (the "*WTO Agreement*"). Thus, the European Communities contends that if paragraph 2(a) of the Enabling Clause were an exception to Article I:1, it would typically be found in Article I, or immediately after that Article. This is not the case, however. The Enabling Clause is a separate decision complementing Part IV of the GATT 1994, which is entitled "Trade and Development". In the view of the European Communities, Part IV of the GATT 1994 and the Enabling Clause cannot be "mere 'exception[s]'" to the GATT 1994.³⁸ Rather, the European Communities argues, they constitute a "special regime" for developing countries to address inequalities among the WTO Membership.³⁹

14. The European Communities submits that its understanding of the relationship between Article I:1 and the Enabling Clause is supported by the object and purpose of the Enabling Clause, in

³⁵European Communities' appellant's submission, para. 31.

³⁶Attached as Annex D-4 to the Panel Report.

³⁷European Communities' appellant's submission, para. 48.

³⁸*Ibid.*, para. 51.

³⁹*Ibid.*

accordance with the rules of treaty interpretation. The European Communities emphasizes that the Enabling Clause is "the most concrete, comprehensive and important application"⁴⁰ of the principle of special and differential treatment. In the view of the European Communities, special and differential treatment is "the most basic principle of the international law of development"⁴¹, and it constitutes *lex specialis* that applies to the exclusion of more general WTO rules on the same subject matter. In concluding that the Enabling Clause is an "exception" to Article I:1, the Panel chose to "disregard"⁴² this principle. Moreover, the European Communities argues, characterizing special and differential treatment as an "exception" suggests that this principle "is *discriminatory* against the developed country Members".⁴³ In fact, special and differential treatment is designed to achieve effective equality among Members. Therefore, the European Communities contends that the Panel's reasoning undermines the principle of special and differential treatment and challenges its "legitimacy".⁴⁴ The European Communities also asserts that the Panel was "oblivious"⁴⁵ to certain elements of the drafting history of the Enabling Clause, which indicate that the Contracting Parties intended to strengthen the legal status of GSP schemes in the GATT by replacing the Waiver Decision on the Generalized System of Preferences (the "1971 Waiver Decision")⁴⁶ with the Enabling Clause.

15. The European Communities further contends that special and differential treatment is critical to achieving one of the fundamental objectives of the *WTO Agreement*, as identified in its Preamble: ensuring that developing countries "secure a share in the growth in international trade commensurate with the needs of their economic development".⁴⁷ Therefore, according to the European Communities, the object and purpose of the Enabling Clause clearly distinguish it from exceptions such as those found in Article XX(a) and (b) of the GATT 1994, which generally allow Members to adopt "legitimate policy objectives"⁴⁸ that are *separate and distinct* from the objectives of the *WTO Agreement*. In the European Communities' view, the Appellate Body decision in *Brazil – Aircraft* confirms that the fact that a provision confers special and differential treatment is highly relevant in determining whether that provision constitutes an exception.

⁴⁰European Communities' appellant's submission, para. 20.

⁴¹*Ibid.*, para. 21.

⁴²*Ibid.*, para. 23.

⁴³*Ibid.*, para. 26. (original italics)

⁴⁴*Ibid.*

⁴⁵*Ibid.*, para. 25.

⁴⁶GATT Document L/3545, 25 June 1971, BISD 18S/24 (attached as Annex D-2 to the Panel Report).

⁴⁷European Communities' appellant's submission, para. 20 (quoting *WTO Agreement*, Preamble, second recital).

⁴⁸*Ibid.*, para. 52.

16. The European Communities notes the Panel's suggestion that absurd results would flow from characterizing the Enabling Clause as excluding the application of Article I:1 because it "would mean that GSP imports from different developing countries could be subject to different taxation levels in the importing country's domestic market."⁴⁹ According to the European Communities, the Panel confuses *tariff measures* covered by paragraph 2(a) with the *imported products* to which such measures apply. Finding that the Enabling Clause excludes the application of Article I:1 would mean only that Article I:1 does not apply to a *tariff measure* falling within paragraph 2(a) of the Enabling Clause. It would not mean, as the Panel suggested, that Article I:1 does not apply with respect to *imported products* covered by such a *tariff measure*.

17. The European Communities submits that, as a result of the Panel's erroneous findings that the Enabling Clause is an "exception" to Article I:1 and that the Enabling Clause does not prevent the continued application of Article I:1, the Panel found that the European Communities bears the burden of justifying the Drug Arrangements under the Enabling Clause. According to the European Communities, the Enabling Clause imposes "positive obligations"⁵⁰ and is not an exception. As such, it is India that must, in the first instance, claim that the Drug Arrangements are inconsistent with the Enabling Clause and thereby bear the burden of demonstrating that inconsistency. According to the European Communities, India made no claim under the Enabling Clause. Consequently, the European Communities requests the Appellate Body to reverse the Panel's finding that the Drug Arrangements are inconsistent with Article I:1 of the GATT 1994 and to refrain from examining the consistency of the Drug Arrangements with the Enabling Clause.

2. Whether the Drug Arrangements are Justified Under the Enabling Clause

18. The European Communities makes a "subsidiary" appeal, which would arise only if the Appellate Body were to find that the Enabling Clause is an exception to Article I:1 of the GATT 1994, or that India made a valid claim under the Enabling Clause. Specifically, the European Communities claims "subsidiarily"⁵¹ that the Panel erred in finding that the Drug Arrangements are not "justified"⁵² under paragraph 2(a) of the Enabling Clause and, therefore, requests the Appellate Body to reverse this finding.

19. According to the European Communities, this finding of the Panel was based on two erroneous legal interpretations. The first alleged error relates to the Panel's interpretation of the term

⁴⁹European Communities' appellant's submission, para. 56 (quoting Panel Report, para. 7.46).

⁵⁰*Ibid.*, para. 39.

⁵¹*Ibid.*, para. 67.

⁵²*Ibid.* (quoting Panel Report, para. 7.177).

"non-discriminatory" in footnote 3 of the Enabling Clause as requiring GSP schemes to provide "identical" preferences to "all" developing countries without differentiation, except with regard to *a priori* import limitations as permissible safeguard measures. The second error alleged by the European Communities concerns the Panel's interpretation of the term "developing countries" in paragraph 2(a) of the Enabling Clause as meaning *all* developing countries, except with regard to *a priori* limitations.

20. The European Communities asserts that the Panel's interpretation of the word "non-discriminatory" in footnote 3 of the Enabling Clause is erroneous because the phrase "generalized, non-reciprocal and non discriminatory" in footnote 3 merely refers to the description of the GSP in the 1971 Waiver Decision and, of itself, does not impose any legal obligation on preference-granting countries.⁵³ Even assuming such obligations existed, the European Communities maintains, the Panel failed to take into account the context of footnote 3 and the object and purpose of the Enabling Clause. Properly interpreted, the European Communities argues, the word "non-discriminatory" allows a preference-granting country to accord differential tariff treatment in its GSP scheme to developing countries that have different development needs according to "objective criteria", provided that tariff differentiation is an "adequate" response to these differences.⁵⁴

21. The European Communities emphasizes that the immediate context for interpreting the term "non-discriminatory" in footnote 3 includes the terms "generalized" and "non-reciprocal" in that same footnote. These three terms express "distinct requirement[s]"⁵⁵, according to the European Communities, and they must be interpreted so that each is compatible with the other two, without being rendered redundant.

22. According to the European Communities, the ordinary meaning of the word "generalized" and the negotiating history indicate that GSP schemes are not required to cover *all* developing countries. The word "generalized" in footnote 3 was intended to distinguish these preferences from "special" preferences, which were granted to selected developing countries for political, historical, or geographical reasons. The European Communities maintains that consultations in the United Nations Conference on Trade and Development ("UNCTAD") led to a compromise in the Agreed Conclusions such that developed countries would, "in general"⁵⁶, recognize as beneficiaries those countries that

⁵³European Communities' response to questioning at the oral hearing.

⁵⁴European Communities' appellant's submission, para. 4.

⁵⁵*Ibid.*, para. 80.

⁵⁶*Ibid.*, para. 87.

considered themselves as developing countries, although a developed country might decide to exclude a country *ab initio* on grounds it considered "compelling".⁵⁷

23. In contrast to the term "generalized", the European Communities argues, the word "non-discriminatory" relates to whether developed countries may grant different preferences to individual developing countries that have already been recognized as beneficiaries of a GSP scheme. The European Communities submits that the Panel's interpretation of "non-discriminatory", as requiring that identical preferences be granted to *all* developing countries, would render redundant the term "generalized".

24. Referring to the term "non-reciprocal" in footnote 3, the European Communities argues that reciprocity, in connection with inter-state relations, generally refers to an exchange of identical or similar benefits. In contrast to the word "unconditionally" found in Article I:1 of the GATT 1994, the European Communities argues, the word "non-reciprocal" was not intended to prevent developed countries from attaching all types of conditions to preferences granted under GSP schemes. Rather, in the European Communities' view, the word "non-reciprocal" only prohibits developed countries from imposing conditions of *reciprocity*. The European Communities contends that the Panel's interpretation of "non-discriminatory" precludes the imposition of *any* conditions on the granting of preferences, thereby rendering redundant the word "non-reciprocal" in footnote 3. In addition, the European Communities claims, the Panel's interpretation equates *conditional* preferences with *discriminatory* preferences. In fact, according to the European Communities, a preference is not rendered discriminatory by virtue of a condition being attached to it if the condition applies equally to, and is capable of being fulfilled by, all GSP beneficiaries "that are in the same situation".⁵⁸

25. The European Communities maintains that its interpretation of "non-discriminatory" in footnote 3 does not render redundant paragraph 2(d) of the Enabling Clause, as the Panel suggested. In the view of the European Communities, the scope of paragraph 2(a) differs from that of paragraph 2(d) in three respects. First, paragraph 2(a) applies to preferences granted by *developed* countries, whereas paragraph 2(d) includes preferences granted by *any* WTO Member. Secondly, paragraph 2(a) relates only to preferences under GSP schemes, whereas paragraph 2(d) relates to any measures imposed in favour of developing countries. Thirdly, paragraph 2(a) applies only to tariff measures, whereas paragraph 2(d) applies to any kind of "special treatment".⁵⁹ In addressing only the

⁵⁷European Communities' appellant's submission, paras. 85 and 87.

⁵⁸*Ibid.*, para. 120.

⁵⁹*Ibid.*, para. 122 (quoting Enabling Clause, para. 2(d) (attached as Annex 2 to this Report)).

last of these differences, the European Communities argues, the Panel's reasoning was "manifestly flawed".⁶⁰

26. The European Communities points out that the Panel found that paragraph 3(c) of the Enabling Clause allows developed countries to differentiate in their GSP schemes in only two ways, namely, in connection with least-developed countries and in the implementation of *a priori* limitations. According to the European Communities, the Panel arrived at this interpretation despite the absence of any such restriction in the text of paragraph 3(c) and despite the Panel's acceptance of the European Communities' argument that the "needs" described in paragraph 3(c) extend to individual or common needs of particular categories of developing countries. In fact, the European Communities argues, paragraph 3(c) lends contextual support to the European Communities' interpretation of the word "non-discriminatory" in footnote 3. The European Communities claims that the objective described in paragraph 3(c) is best achieved by allowing developed countries to design their GSP schemes so as to take into account the development needs of certain categories of developing countries.

27. The European Communities argues that the Panel's contrary interpretation of paragraph 3(c) stems from the Panel's concern that developed countries might abuse their discretion by distinguishing arbitrarily between developing countries. In the view of the European Communities, such policy concerns cannot replace the text of paragraph 3(c). Furthermore, the European Communities submits that this concern is unwarranted because the European Communities' interpretation of "non-discriminatory" would not allow a preference-granting country to distinguish between developing countries on the basis of political, historical, or geographical ties. Rather, a distinction would be allowed only if it: (i) pursued an "objective which is legitimate in the light of the objectives of the Enabling Clause" and the principle of special and differential treatment; and (ii) represented a "reasonable" and "proportionate" means of achieving that objective.⁶¹ In order to assess whether these criteria are met, panels need to analyze the relevant facts.

28. The European Communities contends that, because of the Panel's erroneous legal interpretations, the Panel made insufficient factual findings in order for the Appellate Body to complete the legal analysis regarding the consistency of the Drug Arrangements with footnote 3. Nevertheless, should the Appellate Body decide to complete this analysis, the European Communities requests the Appellate Body to find that the Drug Arrangements are consistent with the term "non-discriminatory" in footnote 3 and, therefore, with paragraph 2(a) of the Enabling Clause.

⁶⁰European Communities' appellant's submission, para. 125.

⁶¹*Ibid.*, para. 135.

29. The European Communities contends that, although tariff preferences may not be an "adequate" or "appropriate" response to other development problems, drug production and trafficking form major economic activities in the relevant countries, which activities cannot be eliminated without the provision of "alternative licit activities".⁶² Therefore, the European Communities claims that tariff preferences are an appropriate response to the drug problem, as recognized by the Members of the WTO—through the Preamble to the *Agreement on Agriculture* and the waiver for the United States' Andean Trade Preference Act⁶³—and the United Nations—through other instruments. Furthermore, the European Communities argues that the Drug Arrangements are non-discriminatory because the drug problem affects individual developing countries in different ways, and because beneficiaries under the Drug Arrangements are designated according to the impact of the drug problem in those countries.

30. The European Communities distinguishes the "object and purpose" of the Enabling Clause from that of Article I:1 of the GATT 1994. Article I:1 focuses on providing equal conditions of competition for imports of like products from WTO Members, whereas the Enabling Clause embodies special and differential treatment for developing countries and, therefore, aims to provide unequal competitive opportunities to respond to the needs of such countries. The European Communities claims that, in the light of the objectives associated with special and differential treatment, providing additional preferences to countries with particular development needs is not discriminatory in the context of the Enabling Clause. However, the Panel failed to take into account these objectives. The European Communities contends that the Panel should have interpreted the objectives described in the Preamble to the *WTO Agreement* in a harmonious manner, instead of assuming that the objective of eliminating discrimination prevails over the objective of ensuring that developing countries secure a share of international trade commensurate with their development needs.

31. The European Communities contends that the Panel relied selectively and incorrectly on certain UNCTAD texts to support its findings. According to the European Communities, some of these documents do not assist in interpreting footnote 3 of the Enabling Clause.⁶⁴ In several cases, this is because they relate not to the issue of non-discrimination, but to the exclusion of certain

⁶²European Communities' appellant's submission, paras. 144-145.

⁶³*Ibid.*, para. 148 (referring to Waiver Decision on the United States – Andean Trade Preference Act, GATT Document L/6991, 19 March 1992, BISD 39S/385; renewed 14 October 1996, WT/L/184).

⁶⁴*Ibid.*, paras. 159-160 (referring to Resolution 21(II) of the Second Session of UNCTAD, entitled "Expansion and Diversification of Exports of Manufactures and Semi-Manufactures of Developing Countries" (attached as Annex D-3 to the Panel Report) ("Resolution 21(II)")) and paras. 182-183 (referring to the Recommendation contained in Annex A.II.1 to the Final Act and Report adopted at the First Session of UNCTAD on 15 June 1964, at p. 26).

developing countries *ab initio* from GSP schemes.⁶⁵ The European Communities contends that several other documents that the Panel relied on contain merely "expectations"⁶⁶ or "aim[s]"⁶⁷ of particular parties, rather than agreed statements of "legally binding" obligations.⁶⁸ Finally, the European Communities argues, the Agreed Conclusions do not purport to be an exhaustive regulation of GSP schemes. Therefore, in the European Communities' view, the allowance under the Agreed Conclusions for differentiation in favour of least-developed countries does not mean that the Agreed Conclusions prohibit all other forms of differentiation between developing countries.

32. The European Communities submits that the practice by developed countries of seeking waivers in order to provide more favourable treatment to a limited number of developing countries—as highlighted by the Panel—does not mean that such treatment may not otherwise be provided. According to the European Communities, the waivers mentioned by the Panel all relate to the restriction of preferences *ab initio* to particular countries in a particular region. The European Communities further points out that, in seeking these waivers, the preference-granting countries did not claim that the preferences were restricted to developing countries with development needs of a specific kind.

33. The European Communities contends that the Panel's interpretation of the term "developing countries" in paragraph 2(a) of the Enabling Clause is erroneous because it is entirely dependent on the Panel's erroneous interpretation of the word "non-discriminatory". In the European Communities' view, as the word "non-discriminatory" in footnote 3 of the Enabling Clause allows Members to differentiate between developing countries with different development needs, it follows for the same reasons that paragraph 2(a) does not require Members to grant the same preferences to *all* developing countries.

34. For these reasons, the European Communities requests the Appellate Body to reverse the Panel's finding that the Drug Arrangements are inconsistent with paragraph 2(a) of the Enabling Clause and, in particular, with footnote 3 thereof.

⁶⁵European Communities' appellant's submission, paras. 162-163 (referring to the Charter of Algiers, TD/38, adopted at the Ministerial Meeting of the Group of 77 on 24 October 1967 ("Charter of Algiers")) and paras. 179-181 (referring to General Principle Eight contained in the Final Act and Report adopted at the First Session of UNCTAD on 15 June 1964, at p. 20 (Exhibit EC-20 submitted by the European Communities to the Panel) ("General Principle Eight")).

⁶⁶*Ibid.*, para. 162 (referring to Charter of Algiers).

⁶⁷*Ibid.*, para. 165 (referring to the Report of the Special Group of the Organization for Economic Co-operation and Development (OECD) on Trade with Developing Countries, TD/56, 29 January 1968 ("OECD Special Report")).

⁶⁸*Ibid.*, para. 180 (referring to General Principle Eight).

B. *Arguments of India – Appellee*

1. The Relationship Between Article I:1 of the GATT 1994 and the Enabling Clause

35. India argues that the Panel correctly found that the Enabling Clause is an "exception" to Article I:1 of the GATT 1994 and requests the Appellate Body to uphold this finding. In addition, India submits that it made a claim against the Drug Arrangements under the Enabling Clause and that, therefore, the Appellate Body should examine the consistency of the Drug Arrangements under the Enabling Clause, even if it finds that the Enabling Clause is not an exception to Article I:1.

36. India contends that the Panel's test as to what is an "exception" is consistent with previous Appellate Body decisions. According to India, the Appellate Body drew an important distinction in *US – Wool Shirts and Blouses* between "positive rules establishing obligations in themselves" and "exceptions" to those obligations.⁶⁹ India states that an exception is an "affirmative defence"⁷⁰ and, accordingly, panels examine the consistency of a challenged measure with an exception only if the Member complained against invokes the exception to justify its measure. This leaves the Member with the choice of which exceptions to invoke and prevents exceptions being turned into rules. In other words, in India's view, a Member needs to comply with a provision that is an exception only when the Member invokes that exception to justify an inconsistency with another provision.

37. Applying this reasoning to the present dispute, India characterizes paragraph 2(a) of the Enabling Clause as an "exception" to Article I:1, because it grants developed-country Members a "conditional right"⁷¹ to provide tariff preferences to developing-country Members under the conditions contained in paragraphs 2(a) and 3 of the Enabling Clause. India submits that these paragraphs impose conditions only on Members who invoke the Enabling Clause as a defence, whereas Article I:1 imposes obligations regardless of the defence invoked.

38. India argues, with reference to the *Vienna Convention*, that "subsequent practice"⁷² supports its interpretation. First, India maintains that all waivers for preferential tariff treatment for products from developing countries have permitted derogations from Article I without mentioning the Enabling

⁶⁹India's appellee's submission, para. 36 (quoting Appellate Body Report, *US – Wool Shirts and Blouses*, p. 16, DSR 1997:1, at 337).

⁷⁰*Ibid.*, para. 36.

⁷¹*Ibid.*, para. 39.

⁷²*Ibid.*, para. 42 (referring to *Vienna Convention*, Art. 31.3(b)).

Clause. Indeed, according to India, the fact that the European Communities requested a waiver⁷³ from its obligations *under Article I:1* in respect of the Drug Arrangements cannot be reconciled with the European Communities' position that the Enabling Clause excludes the application of Article I:1. Secondly, India refers to two GATT panels that examined, first, the consistency of a challenged measure under Article I:1, before proceeding to consider whether the measure was authorized under the Enabling Clause. India regards this as evidence of the "common understanding" of the Contracting Parties to the *General Agreement on Tariffs and Trade 1947* (the "GATT 1947") regarding the relationship between Article I:1 and the Enabling Clause.⁷⁴

39. India disputes the European Communities' contention that the Enabling Clause is not an exception to Article I:1 because the Enabling Clause constitutes *lex specialis*. India argues, with reference to a study by the International Law Commission and certain Appellate Body decisions⁷⁵, that the "maxim *lex specialis derogat legi generali*"⁷⁶ means not that a special rule necessarily excludes the application of a related general rule, but that the two rules apply cumulatively, and the special rule prevails over the general rule only to the extent of any conflict between the two rules. Thus, India maintains, developing-country Members have not waived their rights under Article I:1, which applies "cumulatively" with the Enabling Clause, except to the extent that these provisions are in conflict with each other.⁷⁷

40. India also contests the European Communities' reliance on the Appellate Body decisions in *Brazil – Aircraft* and *EC – Hormones*. India states that these appeals related to Article 27.2(a) of the *SCM Agreement* and Article 3.1 of the *SPS Agreement*, both of which provisions explicitly exclude other provisions. India argues that, in contrast, the Enabling Clause does not clearly exclude the application of Article I:1 of the GATT 1994. In India's view, this supports India's contention that Article I:1 and the Enabling Clause apply "concurrently".⁷⁸

⁷³Council for Trade in Goods, Request for a WTO Waiver, "New EC Special Tariff Arrangements to Combat Drug Production and Trafficking", G/C/W/328, 24 October 2001 (Exhibit India-2(b) submitted by India to the Panel).

⁷⁴India's appellee's submission, para. 43 (referring to GATT Panel Report, *US – Customs User Fee*, 1988, BISD 35S/245, at 289-290; and GATT Panel Report, *US – MFN Footwear*, 1992, BISD 39S/128, at 153).

⁷⁵*Ibid.*, paras. 76-80 (referring to International Law Commission, *Study Group on Fragmentation: Koskenniemi*, p. 5, <http://www.un.org/law/ilc/sessions/55/fragmentation_outline.pdf>; Appellate Body Report, *Argentina – Footwear (EC)*, para. 89; and Appellate Body Report, *Guatemala – Cement I*, para. 65).

⁷⁶*Ibid.*, para. 76.

⁷⁷*Ibid.*, heading II.C.1.

⁷⁸*Ibid.*, para. 51.

41. India claims that, even if the Appellate Body were to find that the Enabling Clause is not an exception to Article I:1, the Appellate Body should assess the consistency of the Drug Arrangements with the Enabling Clause because India did make a claim under the Enabling Clause. The European Communities' argument to the contrary, according to India, is "factually baseless".⁷⁹ India highlights that it originally requested the establishment of a panel "to examine whether [the Drug Arrangements] are consistent with Article I:1 ... and ... the Enabling Clause".⁸⁰ In addition, India maintains that, in its first and second written submissions to the Panel, it requested the Panel to find that the Drug Arrangements "are not justified [by] the Enabling Clause".⁸¹ Moreover, India states that the European Communities acknowledged in its first written submission to the Panel that the Enabling Clause forms part of India's claim⁸², and that the Panel confirmed India's inclusion of this claim in paragraph 7.61 of the Panel Report.

42. India submits that it does not follow from India's characterization of the Enabling Clause as an "exception"—which was a "procedural argument" regarding the allocation of the burden of proof—that India made no "substantive" claims under the Enabling Clause.⁸³ India maintains that, in response to questioning by the Panel, it "merely stated that the Enabling Clause is not a *material element* of India's *claim under Article I:1 of the GATT*".⁸⁴ Furthermore, India reiterated its request for the Panel to examine the consistency of the Drug Arrangements with the Enabling Clause at the second substantive meeting of the Panel and at the interim review stage. In addition, India maintains that the Panel would have had "competence"⁸⁵ to assess the Drug Arrangements under the Enabling Clause even if the Panel had found that the Enabling Clause is not an exception to Article I:1.⁸⁶ In India's view, requiring India to resubmit its claims under the Enabling Clause to a new panel would be contrary to the "fundamental principle of good faith"⁸⁷ and the objectives of the dispute settlement

⁷⁹India's appellee's submission, para. 52.

⁸⁰*Ibid.*, para. 54 (quoting request for the establishment of a panel by India, WT/DS246/4, 9 December 2002, p. 2). (italics added by India in its appellee's submission)

⁸¹*Ibid.*, para. 56 (quoting India's first written submission to the Panel, para. 67; and India's second written submission to the Panel, para. 164). (italics added by India in its appellee's submission)

⁸²*Ibid.*, para. 58 (referring to European Communities' first written submission to the Panel, paras. 57, 141, and 206).

⁸³*Ibid.*, para. 70.

⁸⁴*Ibid.*, para. 64. (original italics)

⁸⁵*Ibid.*, heading II.B.3.

⁸⁶*Ibid.*, paras. 70-71 (referring to Panel Report, *US – Wool Shirts and Blouses*; Appellate Body Report, *EC – Hormones*, footnote 71 to para. 109 and footnote 180 to para. 197; and DSU, Arts. 7.2 and 11).

⁸⁷*Ibid.*, para. 72 (referring to Appellate Body Report, *US – FSC*, para. 166).

system.⁸⁸ India asserts that the question of which party bears the burden of proof "does not affect the outcome of this dispute".⁸⁹

43. Finally, India emphasizes that the European Communities has not yet obtained a waiver from its obligations under Article I:1 with respect to the Drug Arrangements and that only the WTO Members can provide such a waiver.

44. For these reasons, India requests the Appellate Body to uphold the Panel's finding that the Enabling Clause is an exception to Article I:1 of the GATT 1994.

2. Whether the Drug Arrangements are Justified Under the Enabling Clause

45. India requests the Appellate Body to uphold the Panel's finding that the Drug Arrangements are not justified under the Enabling Clause. In particular, India maintains that paragraph 2(a) of the Enabling Clause does not authorize the European Communities to differentiate between developing-country Members that are beneficiaries under the European Communities' GSP scheme.

46. At the outset, India submits that the present dispute focuses not on the European Communities' initial selection of particular developing countries as beneficiaries under its GSP scheme, but on the European Communities' treatment of developing countries already identified as beneficiaries under that scheme. Therefore, according to India, the Appellate Body is not required to examine legal issues arising from the initial selection of beneficiaries under the Enabling Clause. Rather, India urges the Appellate Body to find that the term "developing countries" in footnote 3 of the Enabling Clause includes at least those countries that are beneficiaries under a given GSP scheme, and that the words "products originating in developing countries" in paragraph 2(a) refer to products originating in any of those beneficiary countries.

47. India argues that its interpretation is reinforced by the nature of the MFN principle embodied in Article I:1 as "a fundamental norm of the rules-based multilateral trading system of the WTO".⁹⁰ India points to Appellate Body decisions as support for its view that "derogations" from Article I:1 exist only where provided for explicitly.⁹¹ India emphasizes that paragraph 2(a) of the Enabling Clause does *not* specifically state that developing countries waive their rights to MFN treatment. Moreover, the object and purpose of the Enabling Clause, as well as its drafting history, indicate that

⁸⁸ India's appellee's submission, para. 74 (referring to DSU, Arts. 3.3-3.4 and 3.7).

⁸⁹ *Ibid.*, para. 73.

⁹⁰ *Ibid.*, para. 1.

⁹¹ *Ibid.*, paras. 93-94 (referring to Appellate Body Report, *Canada – Autos*, para. 84; and Appellate Body Report, *EC – Bananas III*, paras. 190-191).

the developing countries did not agree to relinquish their MFN rights as between themselves in agreeing to paragraph 2(a) of the Enabling Clause.

48. India contends that the Drug Arrangements are not "non discriminatory preferences beneficial to the developing countries" within the meaning of footnote 3 of the Enabling Clause. First, India relies on dictionary definitions to ascertain that the ordinary meaning of "non-discriminatory preferences" in footnote 3 is "preferential tariff treatment that is applied equally".⁹² Secondly, India finds "contextual guidance"⁹³ on the meaning of "non-discriminatory" in Articles I, XIII, and XVII of the GATT 1994. According to India, these provisions confirm that "non-discrimination" refers to the provision of "equal competitive opportunities" in relation to non-tariff measures and of "formally equal[] treatment" in relation to tariff measures.⁹⁴ In addition, in India's submission, the inclusion of the word "unjustifiable" before the word "discrimination" in the chapeau of Article XX of the GATT 1994 demonstrates that a Member's reasons for distinguishing between products of different origin are not relevant to whether such distinction constitutes discrimination.

49. Turning to the words "generalized" and "non-reciprocal" in footnote 3, India argues that the word "generalized" refers to the countries that should be included *ab initio* as beneficiaries under a GSP scheme, whereas the word "non-discriminatory" refers to the treatment of products originating in beneficiary countries. Even if "generalized" meant that all developing countries must be included *ab initio* as beneficiaries, in India's view, the "additional requirement"⁹⁵ imposed by the word "non-discriminatory" would still be relevant in addressing the separate question of how products from beneficiary countries should be treated. India contests the European Communities' argument that the Panel's interpretation of "non-discriminatory" renders redundant the word "non-reciprocal" in footnote 3. India suggests that reciprocity is a "principle of trade negotiations"⁹⁶, whereas "non-discriminatory" addresses the implementation of the results of such negotiations. India argues that Part IV of the GATT 1994 (entitled "Trade and Development") was added to the original GATT provisions because it is possible to comply with the principle of non-discrimination while insisting on non-reciprocity in negotiations.

⁹² India's appellee's submission, para. 106.

⁹³ *Ibid.*, para. 115.

⁹⁴ *Ibid.*, paras. 118 and 120 (referring to Appellate Body Report, *EC – Bananas III*, paras. 190-191). (See also, *ibid.*, paras. 170 and 180)

⁹⁵ *Ibid.*, para. 148.

⁹⁶ *Ibid.*, para. 153.

50. India contends that paragraph 2(a) of the Enabling Clause and Article I:1 of the GATT 1994 must be interpreted in a harmonious manner so as to give effect to both provisions.⁹⁷ With this in mind, India submits that the Enabling Clause should be interpreted to authorize only those deviations from the MFN principle that are necessary in order for GSP schemes to operate. Thus, the Enabling Clause authorizes developed-country Members to exclude other developed countries from their GSP schemes, because Members could not grant any tariff preferences under these schemes if such exclusion was not authorized. However, in India's view, the Enabling Clause does not authorize tariff preferences that differentiate between developing countries, as tariff preferences under GSP schemes can be and are granted to developing countries without differentiation of this kind. According to India, a contrary interpretation would be inconsistent with the need to interpret paragraph 2(a) and Article I:1 so as to avoid conflict between the two provisions.

51. India derives support for its interpretation from several provisions of the Enabling Clause. In particular, India reads paragraphs 2(a) and 2(d) together as identifying three categories of countries: the developed countries, the developing countries, and the least-developed countries. In India's view, under the Enabling Clause, the developed countries "relinquished" their MFN rights in respect of preferential tariff treatment in favour of developing and least-developed countries, whereas the developing countries "relinquished" their MFN rights only in respect of preferential treatment in favour of least-developed countries.⁹⁸ However, India sees nothing in the text of the Enabling Clause to indicate that developing countries have similarly relinquished their MFN rights in relation to preferential treatment accorded by developed countries to other developing countries. India suggests that the European Communities itself recognized this fact prior to this dispute.⁹⁹ India maintains that paragraph 2(d) was specifically inserted to allow differentiation of a kind that was not previously allowed under the 1971 Waiver Decision. India argues that the European Communities' current interpretation of "non-discriminatory" in footnote 3 would render paragraph 2(d) redundant, contrary to the "principle of effectiveness in treaty interpretation".¹⁰⁰

52. The opening words of paragraph 3(c) demonstrate, according to India, that paragraph 3(c) of the Enabling Clause does not provide for derogations from obligations imposed under paragraph 2(a), (b), or (d). Further, unlike paragraphs 5 and 6, paragraph 3(c) does not refer to

⁹⁷India's appellee's submission, para. 83 (referring to Appellate Body Report, *Korea – Dairy*, para. 81; Appellate Body Report, *Argentina – Footwear (EC)*, para. 81; and International Court of Justice, Preliminary Objections, *Right of Passage over Indian Territory (Portugal v. India)*, 1957, ICJ Reports, p. 142).

⁹⁸*Ibid.*, paras. 3 and 5.

⁹⁹*Ibid.*, para. 6 (referring to "User's Guide to the European Union's Scheme of Generalised Tariff Preferences" (February 2003) (Exhibit India-1 submitted by India to the Panel)).

¹⁰⁰*Ibid.*, para. 132 (referring to Appellate Body Report, *US – Gasoline*, p. 23, DSR 1996:1, at 21).

"individual" or "particular" needs of developing countries. India argues that this shows that the "needs" intended by the drafters under paragraph 3(c) are the needs of "developing countries as a whole".¹⁰¹

53. India draws support for its reading of paragraph 2(a) from the object and purpose of the Enabling Clause. According to India, the purpose includes: facilitating "mutually acceptable arrangements"¹⁰² that were "unanimous[ly] agree[d]"¹⁰³ in UNCTAD; replacing "special preferences"¹⁰⁴ granted only to some developing countries with generalized preferences that do not differentiate between developing countries; and, promoting the trade of developing countries without raising barriers to or creating undue difficulties for the trade of other Members, as confirmed in paragraph 3(a). India points to several UNCTAD texts to confirm these purposes¹⁰⁵, arguing that the European Communities offers no such support for its contrary views. India regards differentiation between developing countries under a GSP scheme as inconsistent with paragraph 3(a) because it creates difficulties for the trade of other developing countries by "divert[ing] competitive opportunities"¹⁰⁶ from one country to another. In addition, India contends that linking GSP benefits to "the situation or policies"¹⁰⁷ of beneficiaries reduces the certainty and value of such benefits.

54. India contends that the European Communities' interpretation of paragraph 3(c) would mean that developed countries "would have the obligation"¹⁰⁸ to differentiate between developing countries according to their individual needs. This would have the "absurd consequence"¹⁰⁹ that a measure eliminating tariffs on products from *all* least-developed countries, without differentiating between those countries would be open to challenge under paragraph 3(c). Moreover, India argues that it would result not only in the European Communities' scheme, but in all GSP schemes being inconsistent with the Enabling Clause because they do not differentiate between developing countries based on their *individual* development needs. India also maintains that the European Communities' suggestion that its interpretation would best fulfil the objectives of paragraph 3(c) is inconsistent with

¹⁰¹India's appellee's submission, para. 124.

¹⁰²*Ibid.*, paras. 95 and 190.

¹⁰³*Ibid.*, para. 165.

¹⁰⁴*Ibid.*, paras. 147 and 190.

¹⁰⁵*Ibid.*, paras. 158-184 (referring to Agreed Conclusions; Resolution 2(II); Resolution 24(II) of the Second Session of UNCTAD; Charter of Algiers, paras. (a) and (d); and OECD Special Report, part II).

¹⁰⁶*Ibid.*, para. 192.

¹⁰⁷*Ibid.*, para. 21.

¹⁰⁸*Ibid.*, para. 14. (original italics)

¹⁰⁹*Ibid.*, para. 15.

the rule that treaty interpretation should be based on the text and not on policy considerations that are not reflected in the text.

55. For these reasons, India requests the Appellate Body to uphold the Panel's finding that the Drug Arrangements are not justified under the Enabling Clause.

C. *Arguments of the Third Participants*

I. Andean Community

56. The governments of Bolivia, Colombia, Ecuador, Peru, and Venezuela (jointly, the "Andean Community") submit that the Panel erred in finding that the Enabling Clause is an "exception" to Article I:1 of the GATT 1994 and in finding that Article I:1 applies concurrently with the Enabling Clause. The Andean Community also contends that, contrary to the Panel's finding, the Drug Arrangements are consistent with the Enabling Clause. Accordingly, the Andean Community supports the European Communities' contention that the Drug Arrangements are "fully WTO-compatible".¹¹⁰

57. The Andean Community argues that the Enabling Clause establishes "a self-standing regime"¹¹¹, meaning that Article I:1 of the GATT 1994 does not apply to GSP schemes.¹¹² According to the Andean Community, the ordinary meaning of the word "notwithstanding" in paragraph 1 of the Enabling Clause confirms this interpretation, as do the context, and object and purpose of the Enabling Clause. In addition, the "history, ... practice and ... current role"¹¹³ of the Enabling Clause indicate that GSP schemes provide the "most concrete and relevant form"¹¹⁴ of special and differential treatment. This supports the concept of the Enabling Clause as a self-standing regime. According to the Andean Community, because measures falling within the Enabling Clause are to be judged solely under the Enabling Clause, India was required to make a claim under the Enabling Clause. As India did not do so, the Andean Community maintains, India's claim should be dismissed.

58. The Andean Community submits further that, even if the Enabling Clause is an exception to Article I:1, this characterization is not determinative of which party bears the burden of proof. The Andean Community asserts that the Panel erred in assigning the burden. According to the Andean

¹¹⁰ Andean Community's third participant's submission, para. 97.

¹¹¹ See, for example, *ibid.*, paras. 8, 12, and 27.

¹¹² *Ibid.*, para. 9 (referring to Appellate Body Report, *Brazil – Aircraft*, para. 139).

¹¹³ *Ibid.*, para. 13.

Community, under the Panel's allocation of the burden of proof, every GSP scheme would be open to challenge, with the burden falling on each preference-granting country to establish the consistency of its GSP scheme with the Enabling Clause. The Andean Community claims that the assigning of the burden of proof is "a fundamental initial decision upon which every further consideration is based", such that the Appellate Body "should reverse on this element alone".¹¹⁵

59. Regarding the consistency of the Drug Arrangements with the Enabling Clause, the Andean Community submits, first, that the Panel did not properly interpret the historical texts serving as context and preparatory work for the Enabling Clause. The Andean Community emphasizes the "aspirational tone"¹¹⁶ of these texts and argues that the Panel "mischaracterize[d]"¹¹⁷ certain texts as binding or reflecting "unanimous agreement".¹¹⁸ Secondly, turning to the interpretation of the term "non-discriminatory" in the Enabling Clause, the Andean Community contends that the Panel wrongly equated this concept with MFN treatment. The Andean Community further alleges that the Panel's allowance for *a priori* limitations under the Enabling Clause is contrary to the Panel's own interpretation of "non-discriminatory".

60. In the view of the Andean Community, "a prohibition of discrimination is a command not to treat equal situations differently, or different situations equally"¹¹⁹ and, accordingly, the word "non-discriminatory" in the Enabling Clause does not require that identical treatment be granted to all developing countries. The Andean Community suggests that differentiating between developing countries—taking into account their objectively different situations—does not constitute discrimination. The Andean Community argues that the "production and trafficking of illicit drugs have far-reaching, unparalleled and unquantifiable implications for the economic and social development"¹²⁰ of affected developing countries. By providing preferential access for "alternative products"¹²¹ and, thereby, seeking to reduce the importance of drugs as an economic activity, the European Communities responds to these countries' specific needs. The Andean Community asserts that this response is consistent with the requirements of the Enabling Clause.

¹¹⁴ *Ibid.*, para. 21.

¹¹⁵ Andean Community's third participant's submission, para. 41.

¹¹⁶ *Ibid.*, para. 50.

¹¹⁷ *Ibid.*, para. 56. (original underlining)

¹¹⁸ *Ibid.*, para. 55.

¹¹⁹ *Ibid.*, para. 64.

¹²⁰ *Ibid.*, para. 78.

¹²¹ *Ibid.*, para. 87.

2. Costa Rica

61. Costa Rica submits that the Panel erred in finding that the Drug Arrangements are not justified under the Enabling Clause. Costa Rica asserts that the Panel based this finding on erroneous interpretations of the terms "non-discriminatory" and "developing countries" contained in footnote 3 and paragraph 2(a), respectively, of the Enabling Clause. Accordingly, Costa Rica supports the European Communities' request that the Appellate Body reverse this finding.

62. Costa Rica contends that, instead of relying on the ordinary meaning of these terms of the Enabling Clause in context, the Panel relied on other instruments that "cannot be properly considered context for the interpretation of the Enabling Clause".¹²² Costa Rica maintains that this led to the Panel's incorrect finding that "non-discriminatory" treatment under footnote 3 of the Enabling Clause is synonymous with identical or unconditional treatment. Costa Rica asserts that had the Panel interpreted the Enabling Clause in accordance with Article 31 of the *Vienna Convention*—in the light of the object and purpose of the Enabling Clause and the 1971 Waiver Decision—it would have found that "the 'non-discriminatory' standard prohibits developed countries from according tariff preferences that make an unjust or prejudicial distinction between different categories of developing countries."¹²³

63. In addition, according to Costa Rica, the Panel erred in concluding that the term "developing countries" in paragraph 2(a) of the Enabling Clause means *all* developing countries. In Costa Rica's view, in interpreting this term, the Panel relied on its incorrect interpretation of the term "non-discriminatory" and failed to examine paragraph 1 of the Enabling Clause as relevant context. Moreover, Costa Rica is of the opinion that it is not appropriate to consider the *travaux préparatoires* as a supplementary means of interpretation under Article 32 of the *Vienna Convention* in interpreting paragraph 2(a). However, even if this were appropriate, the drafting history of the 1971 Waiver Decision confirms that the term "developing countries" means less than all developing countries.

3. Panama

64. Panama submits that the Panel erred in finding that the Enabling Clause is an "exception" to Article I:1 of the GATT 1994. Panama maintains that the Enabling Clause is "*per se* an autonomous rule"¹²⁴ that permits the granting of more favourable treatment to developing countries. Panama also contests the Panel's finding that the Drug Arrangements are incompatible with the Enabling Clause.

¹²²Costa Rica's third participant's submission, para. 6.

¹²³*Ibid.*, para. 15.

¹²⁴Panama's third participant's submission, para. 4.

In particular, Panama argues that the Panel erred in interpreting the term "non-discriminatory" in footnote 3 of the Enabling Clause as requiring preference-granting countries to accord identical treatment to all developing countries. Panama therefore states that it is "completely in agreement with the arguments by the European Communities".¹²⁵

65. Panama is of the view that, if the Enabling Clause were an exception to Article I of the GATT 1994, it would be included as a waiver decision in the GATT 1994.¹²⁶ Because the Enabling Clause is not so included, Panama contends, it is an "independent" and "special" rule governing the differential and more favourable treatment accorded to developing countries under the schemes set out in paragraph 2 of the Enabling Clause.¹²⁷ Panama submits that "the Enabling Clause creates a standalone mechanism that is linked to the general principle contained in GATT Article I:1"¹²⁸ and, as such, constitutes an "autonomous right"¹²⁹ of WTO Members.

66. Panama argues that the Enabling Clause is not an affirmative defence but, rather, "excludes the application of ... Article I:1".¹³⁰ As such, Panama claims, it was up to India to claim that the Drug Arrangements do not fall within the scope of paragraph 2(a) of the Enabling Clause and are inconsistent with paragraph 3(c) thereof. Because India did not do so, Panama argues, the Appellate Body should refrain from assessing the consistency of the Drug Arrangements with the Enabling Clause.

67. According to Panama, "non-discrimination" does not mean equal treatment. Panama submits that the fact that the Drug Arrangements are not extended to all developing countries does not mean that they discriminate between developing countries. In addition, Panama maintains that the obligation imposed in paragraph 3(c) of the Enabling Clause must be interpreted in order to allow some flexibility for preference-granting countries to provide preferential treatment that "effectively help[s] 'generalized' needs".¹³¹ In this respect, Panama claims, the Drug Arrangements satisfy the "requirement" in paragraph 3(c) because they respond to "specific growth needs".¹³²

¹²⁵Panama's third participant's submission, para. 1.

¹²⁶Paragraph 1(b)(iii) of the language of Annex 1A incorporating the GATT 1994 into the *WTO Agreement*.

¹²⁷Panama's third participant's submission, paras. 5-6.

¹²⁸*Ibid.*, para. 10.

¹²⁹*Ibid.*, para. 8.

¹³⁰*Ibid.*, para. 17.

¹³¹*Ibid.*, para. 23.

¹³²*Ibid.*, para. 13.

4. Paraguay

68. Paraguay contends that the Panel was correct in finding that the Enabling Clause is an "exception" to Article I:1 of the GATT 1994. In addition, Paraguay agrees with the Panel's interpretation of paragraph 2(a) of the Enabling Clause and the Panel's consequent finding that the Drug Arrangements are not justified by the Enabling Clause. Accordingly, Paraguay supports India's request that the Appellate Body uphold these findings.

69. According to Paraguay, where a Member's measure differentiates between other Members in a manner inconsistent with Article I:1 and does not fall within any specific exceptions such as the Enabling Clause or Article XX of the GATT 1994, the only way for that Member to impose its measure in accordance with its WTO obligations is to seek a waiver under Article IX of the *WTO Agreement*. Paraguay maintains that the Drug Arrangements are inconsistent with Article I:1 and that the European Communities has received no such waiver in respect of them.

70. Paraguay contests the European Communities' characterization of the Enabling Clause as a "different, parallel legal regime".¹³³ Paraguay maintains that Article I:1 forms the "primary basis" for WTO trade and that exceptions to Article I:1 must be founded on "properly established legal rules".¹³⁴ In Paraguay's view, the Enabling Clause is an exception to Article I:1 and is a part of the GATT 1994, and the GSP recognized in the Enabling Clause is "a permanent mechanism of the rules-based multilateral trading system".¹³⁵

71. Paraguay emphasizes that developing countries did not renounce their right to MFN treatment under Article I:1 of the GATT 1994 in agreeing to the Enabling Clause. According to Paraguay, the Enabling Clause was adopted to replace the "special preferences"¹³⁶ provided by developed countries to certain developing countries, with a generalized system under which all developing countries would benefit. Paraguay argues that the only distinction that the WTO draws within the category of developing countries is in recognizing the category of least-developed countries, as explicitly stated in paragraph 2(d) of the Enabling Clause. As such, in Paraguay's view, the "condition"¹³⁷ of non-discrimination in footnote 3 means that benefits granted to some developing countries must be granted

¹³³Paraguay's third participant's submission, para. 13.

¹³⁴*Ibid.*, para. 12.

¹³⁵*Ibid.*, para. 11.

¹³⁶*Ibid.*, para. 14.

¹³⁷*Ibid.*, para. 27.

to all such countries. Therefore, Paraguay submits that tariff preferences pursuant to the Enabling Clause must apply to all developing countries.

5. United States

72. The United States contends that the Panel misconceived the relationship between the Enabling Clause and Article I:1 of the GATT 1994. The United States also submits that the Panel erred in concluding that the term "non-discriminatory" in footnote 3 of the Enabling Clause requires preference-granting countries to accord "identical" treatment to all beneficiaries and that, consequently, paragraph 2(a) covers only identical preferences extended to *all* developing countries. Accordingly, the United States supports the European Communities' request that the Appellate Body reverse the Panel's legal interpretation of the terms "non-discriminatory" in footnote 3 and "developing countries" in paragraph 2(a) and, consequently, reverse the Panel's finding that the Enabling Clause is an "exception" to Article I:1.

73. Beginning with the relationship between Article I:1 and the Enabling Clause, the United States claims that the Panel failed to consider the entire text of the Enabling Clause and the context and object and purpose of the Enabling Clause and of the GATT 1994. The United States argues that the Panel "misconstru[ed]" the statement of the Appellate Body in *US – Wool Shirts and Blouses* and applied this statement "as a mechanical 'test'" without due regard to the term "notwithstanding" in the Enabling Clause.¹³⁸ The United States observes that the Panel examined the ordinary meaning of "notwithstanding" in paragraph 1 of the Enabling Clause only after the Panel had concluded that the Enabling Clause is an "exception". In addition, in the view of the United States, the reasoning underlying the Panel's conclusion that the Enabling Clause is an exception "would result in ... inconsistencies and absurd results"¹³⁹ because several WTO obligations apply only if a Member chooses to take the action addressed in the relevant provision.

74. The United States submits that the Enabling Clause is part of the overall balance of rights and obligations in the covered agreements and, as such, is a "separate provision authorizing the types of treatment provided therein", "in spite of" the MFN obligation in Article I:1.¹⁴⁰ In other words, the United States maintains that, contrary to the finding of the Panel, the Enabling Clause *is* a "positive rule establishing obligations in itself".¹⁴¹ The United States emphasizes that several aspects of the Enabling Clause are unrelated to Article I:1 and that the Enabling Clause is incorporated into the

¹³⁸United States' third participant's submission, paras. 2-3.

¹³⁹*Ibid.*, para. 5.

¹⁴⁰*Ibid.*, paras. 3 and 10.

¹⁴¹*Ibid.*, para. 4.

GATT 1994. The United States also argues that, unlike Article XX of the GATT 1994, the Enabling Clause "encourages"¹⁴² developed-country Members to grant preferences to developing-country Members. In the view of the United States, "[p]lacing the burden on developed countries to defend actions they take to benefit developing countries ... would create a *disincentive* for developed countries" to take such action.¹⁴³

75. Turning to footnote 3 of the Enabling Clause, the United States contests the Panel's "assumption"¹⁴⁴ that the term "non-discriminatory" in footnote 3 imposes obligations on preference-granting countries. In the view of the United States, "[t]his footnote is simply a cross-reference to where the Generalized System of Preferences is described."¹⁴⁵ Because the Panel began its analysis "from a false premise", the United States suggests that the Panel's finding as to footnote 3 "should be rejected on that basis alone".¹⁴⁶ In any case, the United States contends, the Panel erroneously arrived at a "one size fits all"¹⁴⁷ obligation to grant "identical" tariff preferences to "all" developing countries. Furthermore, according to the United States, the fact that the Panel understood the Enabling Clause to allow *a priori* limitations demonstrates that the term "non-discriminatory" does not preclude all conditions. The United States asserts that the Panel focused not on the text, but on a policy concern—the prevention of "abuse"¹⁴⁸ by preference-granting countries. In the United States' view, the Panel's focus on this policy concern is inconsistent with Article 3.2 of the DSU and led to an incorrect interpretation of "non-discriminatory".

76. With respect to paragraph 3(c) of the Enabling Clause, the United States argues that the Panel wrongly interpreted this provision as imposing an obligation not to provide differentiated GSP benefits. In doing so, the United States submits, the Panel failed to recognize that the term "generalized" in footnote 3 ensures that the responses of preference-granting countries to the needs of developing countries do not result in tariff advantages accorded primarily to select countries.

77. Finally, the United States contends that the Panel's interpretation of "developing countries" in paragraph 2(a) as referring to *all* developing countries is "completely dependent"¹⁴⁹ on its erroneous interpretation of "non-discriminatory". Moreover, the United States argues, the Enabling Clause

¹⁴²United States' third participant's submission, para. 8. (original italics)

¹⁴³*Ibid.*, para. 9. (original italics)

¹⁴⁴*Ibid.*, para. 11.

¹⁴⁵*Ibid.*

¹⁴⁶*Ibid.*

¹⁴⁷*Ibid.*, para. 22.

¹⁴⁸*Ibid.*, para. 20 (quoting Panel Report, para. 7.158).

¹⁴⁹*Ibid.*, para. 23.

refers only to "developing countries" or "the developing countries", and not to "*all* developing countries".¹⁵⁰

III. Issues Raised in This Appeal

78. The following issues are raised in this appeal:

- (a) Whether the Panel erred in concluding that the "special arrangements to combat drug production and trafficking" (the "Drug Arrangements"), which are part of Council Regulation (EC) No. 2501/2001 (the "Regulation")¹⁵¹, are inconsistent with Article I:1 of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994")¹⁵², based on the Panel's findings that:
 - (i) the Decision on Differential and More Favourable Treatment, Reciprocity, and Fuller Participation of Developing Countries (the "Enabling Clause")¹⁵³ is an "exception"¹⁵⁴ to Article I:1 of the GATT 1994;
 - (ii) the Enabling Clause "does not exclude the applicability"¹⁵⁵ of Article I:1 of the GATT 1994; and
 - (iii) the European Communities bears the burden of invoking the Enabling Clause and proving that the Drug Arrangements are consistent with that Clause¹⁵⁶, and
- (b) Whether the Panel erred in concluding that the European Communities failed to prove that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause¹⁵⁷, based on the Panel's findings that:

¹⁵⁰United States' third participant's submission, para. 24. (original italics)

¹⁵¹Council Regulation (EC) No. 2501/2001 of 10 December 2001 applying a scheme of generalised tariff preferences for the period from 1 January 2002 to 31 December 2004, *Official Journal of the European Communities*, L Series, No. 346 (31 December 2001), p. 1 (Exhibit India-6 submitted by India to the Panel).

¹⁵²Panel Report, paras. 7.60 and 8.1(b).

¹⁵³GATT Document L/4903, 28 November 1979, BISD 26S/203 (attached as Annex 2 to this Report).

¹⁵⁴Panel Report, para. 7.53.

¹⁵⁵*Ibid.*

¹⁵⁶*Ibid.*

¹⁵⁷*Ibid.*, para. 8.1(d).

- (i) the term "non-discriminatory" in footnote 3 to paragraph 2(a) of the Enabling Clause requires that, pursuant to schemes under the Generalized System of Preferences ("GSP"), "identical tariff preferences"¹⁵⁸ be provided to all developing countries without differentiation, except as regards the implementation of *a priori* limitations; and
- (ii) the term "developing countries" in paragraph 2(a) of the Enabling Clause means "all"¹⁵⁹ developing countries, except as regards the implementation of *a priori* limitations.

IV. The Relationship Between Article I:1 of the GATT 1994 and the Enabling Clause

79. We begin our analysis of the European Communities' appeal by examining its claim that the Panel improperly characterized the relationship between Article I:1 of the GATT 1994 and the Enabling Clause, and thus improperly allocated the burden of proof in this dispute.

A. *The Panel's Analysis and the Arguments on Appeal*

80. The Panel observed that the participants disagree on whether the Enabling Clause constitutes a "positive rule setting out obligations", or an "exception" authorizing derogation from one or more such positive rules.¹⁶⁰ Based on its understanding of the Appellate Body's decision in *US – Wool Shirts and Blouses*, the Panel determined that the Enabling Clause, in and of itself, does not establish legal obligations but, instead, contains requirements that are "only subsidiary obligations, dependent on the decision of the Member to take [particular] measures".¹⁶¹ The Panel further concluded that the legal function of the Enabling Clause is to permit Members to derogate from Article I:1 "so as to enable developed countries, *inter alia*, to provide GSP to developing countries".¹⁶² As a result, the Panel found that the Enabling Clause is "in the nature of an exception" to Article I:1.¹⁶³

81. The Panel noted that the GATT 1994 includes several provisions in the nature of exceptions that serve to justify a measure's inconsistency with Article I:1, including Articles XX, XXI, and XXIV, and the Enabling Clause. According to the Panel, these exceptions reflect "legitimate

¹⁵⁸Panel Report, para. 7.161.

¹⁵⁹*Ibid.*, para. 7.176.

¹⁶⁰*Ibid.*, para. 7.32.

¹⁶¹*Ibid.*, para. 7.37.

¹⁶²*Ibid.*, para. 7.38.

¹⁶³*Ibid.*, para. 7.39.

objectives" that may be pursued by Members.¹⁶⁴ The Panel reasoned that, because a complaining party may not be able to discern the objectives of a given measure, particularly as they may not be apparent from the text of the measure itself, it is "sufficient" for a complaining party to demonstrate an inconsistency with Article I:1, without also establishing "violations" of any of the possible exception provisions.¹⁶⁵

82. With respect to the present dispute, the Panel found that India could make its case against the European Communities solely by establishing the inconsistency of the Drug Arrangements with Article I:1.¹⁶⁶ Having done so, according to the Panel, it would then be incumbent upon the European Communities to invoke the Enabling Clause as a defence and to demonstrate the consistency of the Drug Arrangements with the requirements contained in that Clause.¹⁶⁷

83. The Panel also examined whether Article I:1 applies to a measure covered by the Enabling Clause. It looked first to the ordinary meaning of the term "notwithstanding", as used in paragraph 1 of the Enabling Clause, and concluded on that basis that the Enabling Clause takes precedence over Article I "to the extent of conflict between the two provisions".¹⁶⁸ Nevertheless, the Panel declined to assume the exclusion of the applicability of a "basic GATT obligation" such as Article I:1 in the absence of a textual indication of Members' intent to that effect.¹⁶⁹ Thus, it also referred to World Trade Organization ("WTO") jurisprudence relating to other exception provisions, and concluded that the relationship between these exceptions and the obligations from which derogation is permitted is "one where both categories of provisions apply concurrently to the same measure, but where, in the case of conflict between these two categories of provisions, [the exception] prevails".¹⁷⁰ Accordingly, the Panel concluded, on the basis of both the ordinary meaning of the text of the provision and WTO case law, that Article I:1 applies to measures covered by the Enabling Clause and that the Enabling Clause prevails over Article I:1 "to the extent of the conflict between [them]".¹⁷¹

¹⁶⁴Panel Report, para. 7.40.

¹⁶⁵*Ibid.*

¹⁶⁶*Ibid.*

¹⁶⁷*Ibid.*, para. 7.42.

¹⁶⁸*Ibid.*, para. 7.44. Paragraph 1 of the Enabling Clause provides:

Notwithstanding the provisions of Article I of the General Agreement, contracting parties may accord differential and more favourable treatment to developing countries, without according such treatment to other contracting parties. (footnote omitted)

¹⁶⁹Panel Report, para. 7.44.

¹⁷⁰*Ibid.*, para. 7.45.

¹⁷¹*Ibid.*

84. Finally, the Panel referred to the European Communities' reliance on the Appellate Body's decisions in *Brazil – Aircraft* and *EC – Hormones* and distinguished those cases from the present dispute. The Panel stated that the relationship between the provisions at issue in those cases was "different" from the relationship it had found between Article I:1 and the Enabling Clause.¹⁷² In particular, the Panel determined that, in the two earlier disputes, one provision "clearly exclude[d]" the application of the other.¹⁷³ In contrast, the Panel had already found that the Enabling Clause does not exclude the applicability of Article I:1. In these circumstances, the Panel suggested that the Enabling Clause constitutes an "affirmative defence", in relation to which the responding party bears the burden of proof if that party invokes the Enabling Clause to justify its challenged measure.¹⁷⁴

85. On appeal, the European Communities challenges the Panel's finding that the Enabling Clause is an "exception"¹⁷⁵ to Article I:1 of the GATT 1994 and that, therefore, the European Communities must invoke the Enabling Clause as an "affirmative defence"¹⁷⁶ to India's claim that the Drug Arrangements are inconsistent with Article I:1. The European Communities submits that the Enabling Clause is part of a "special regime for developing countries"¹⁷⁷, which "encourages"¹⁷⁸, *inter alia*, the granting of tariff preferences by developed-country Members to developing countries. As a result, the Enabling Clause exists "side-by-side and on an equal level" with Article I:1, and applies to the *exclusion* thereof, rather than as an exception thereto.¹⁷⁹ The European Communities argues, therefore, that India is required to bring a claim under the Enabling Clause if it considers that the European Communities' GSP scheme has nullified or impaired India's rights.¹⁸⁰ The European Communities requests us to refrain from examining the consistency of the Drug Arrangements with the requirements of the Enabling Clause because, according to the European Communities and as

¹⁷²Panel Report, paras. 7.48-7.50.

¹⁷³*Ibid.*, para. 7.48. (See also, *ibid.*, paras. 7.47-7.50) The Panel was referring to Articles 3.1(a) and 27.2(b) of the *Agreement on Subsidies and Countervailing Measures* (the "SCM Agreement"), as interpreted in Appellate Body Report, *Brazil – Aircraft*, and Articles 3.1 and 3.3 of the *Agreement on the Application of Sanitary and Phytosanitary Measures* (the "SPS Agreement"), as interpreted in Appellate Body Report, *EC – Hormones*.

¹⁷⁴Panel Report, para. 7.49.

¹⁷⁵*Ibid.*, para. 7.39.

¹⁷⁶*Ibid.*, para. 7.42.

¹⁷⁷European Communities' appellant's submission, para. 51.

¹⁷⁸*Ibid.*, para. 53.

¹⁷⁹*Ibid.*, para. 22.

¹⁸⁰*Ibid.*, para. 15(2).

allegedly acknowledged by India before the Panel, India did not bring a claim under the Enabling Clause.¹⁸¹

86. India, by contrast, supports the Panel's understanding of the relationship between Article I:1 and the Enabling Clause. India argues that paragraph 2(a) of the Enabling Clause qualifies as an "exception" because the conditions therein must be complied with only by Members adopting a measure pursuant to the authorization granted by that provision. This differs from the most-favoured nation ("MFN") obligation in Article I:1.¹⁸² Moreover, according to India, we are not precluded from addressing the consistency of the Drug Arrangements with the Enabling Clause because, contrary to the assertion of the European Communities, India did make a claim under that Clause before the Panel.¹⁸³ India submits that denying the Panel the "competence"¹⁸⁴ to evaluate this claim, even if the Enabling Clause is not regarded as an exception, would be inconsistent with the objectives of WTO dispute settlement, "namely to secure a 'prompt' and 'positive solution to a dispute', and 'achieve a satisfactory settlement of the matter' in accordance with rights and obligations under the covered agreements."¹⁸⁵ According to India, this is particularly so because the European Communities had been on notice throughout the Panel proceedings of India's position that the Drug Arrangements are not justified by the Enabling Clause.¹⁸⁶

B. *Relevance of the Relationship Between Article I:1 of the GATT 1994 and the Enabling Clause for the Allocation of the Burden of Proof*

87. We begin our analysis of the relationship between Article I:1 of the GATT 1994 and the Enabling Clause, and the attendant implications for the allocation of the burden of proof in this dispute, by recalling the observation of the Appellate Body in *US – Wool Shirts and Blouses*:

[I]t is a generally-accepted canon of evidence in civil law, common law and, in fact, most jurisdictions, that the burden of proof rests upon the party, whether complaining or defending, who asserts the affirmative of a particular claim or defence.¹⁸⁷

¹⁸¹European Communities' appellant's submission, paras. 3, 13(2), and 66.

¹⁸²India's appellee's submission, paras. 36 and 39.

¹⁸³*Ibid.*, paras. 54-57.

¹⁸⁴*Ibid.*, para. 71 and heading II.B.3.

¹⁸⁵*Ibid.*, para. 74 (quoting DSU, Arts. 3.3, 3.4, and 3.7), (footnotes omitted).

¹⁸⁶*Ibid.*, para. 73.

¹⁸⁷Appellate Body Report, *US – Wool Shirts and Blouses*, p. 14, DSR 1997:1, at 335.

It is thus for the *complaining* party to raise a claim with respect to a particular obligation and to *prove* that the responding party is acting inconsistently with that obligation. It is for the *responding* party, if it so chooses, to raise a defence in response to an allegation of inconsistency and to *prove* that its challenged measure satisfies the conditions of that defence. Therefore, the question before us is whether India must raise a "claim" and prove that the Drug Arrangements are inconsistent with the Enabling Clause, or whether the European Communities must raise and prove, in "defence", that the Drug Arrangements are consistent with the Enabling Clause, in order to justify the alleged inconsistency of the Drug Arrangements with Article I:1.¹⁸⁸

88. We recall that the Appellate Body has addressed the allocation of the burden of proof in similar situations. In cases where one provision permits, in certain circumstances, behaviour that would otherwise be inconsistent with an obligation in another provision, and one of the two provisions refers to the other provision, the Appellate Body has found that the complaining party bears the burden of establishing that a challenged measure is inconsistent with the provision permitting particular behaviour *only* where one of the provisions suggests that the obligation is not applicable to the said measure.¹⁸⁹ Otherwise, the permissive provision has been characterized as an exception, or defence, and the onus of invoking it and proving the consistency of the measure with its requirements has been placed on the responding party.¹⁹⁰ However, this distinction may not always be evident or readily applicable.

C. *Characterization of the Enabling Clause*

I. Text of Article I:1 and the Enabling Clause

89. In considering whether the Enabling Clause is an exception to Article I:1 of the GATT 1994, we look, first, to the text of the provisions at issue. Article I:1, which embodies the MFN principle, provides:

¹⁸⁸We are not concerned here with the situation where a complaining party brings a challenge solely under the provisions of the Enabling Clause, that is, without also claiming an inconsistency with Article I of the GATT 1994.

¹⁸⁹See Appellate Body Report, *EC – Hormones*, para. 104; Appellate Body Report, *Brazil – Aircraft*, paras. 139-141; and Appellate Body Report, *EC – Sardines*, para. 275.

¹⁹⁰See Appellate Body Report, *US – FSC (Article 21.5 – EC)*, paras. 131-133; and Appellate Body Report, *US – Wool Shirts and Blouses*, p.16, DSR 1997:1, at 337.

Article I

General Most-Favoured-Nation Treatment

1. With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation or imposed on the international transfer of payments for imports or exports, and with respect to the method of levying such duties and charges, and with respect to all rules and formalities in connection with importation and exportation, and with respect to all matters referred to in paragraphs 2 and 4 of Article III,* any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties.

Article I:1 plainly imposes upon WTO Members the obligation to treat "like products ... equally, irrespective of their origin".¹⁹¹

90. We turn now to the Enabling Clause, which has become an integral part of the GATT 1994.¹⁹² Paragraph 1 of the Enabling Clause, which applies to all measures authorized by that Clause, provides:

Notwithstanding the provisions of Article I of the General Agreement, contracting parties may accord differential and more favourable treatment to developing countries, without according such treatment to other contracting parties. (footnote omitted)

The ordinary meaning of the term "notwithstanding" is, as the Panel noted¹⁹³, "[i]n spite of, without regard to or prevention by".¹⁹⁴ By using the word "notwithstanding", paragraph 1 of the Enabling

¹⁹¹Appellate Body Report, *EC – Bananas III*, para. 190.

¹⁹²In response to questioning at the oral hearing, the participants and third participants agreed that the Enabling Clause is one of the "other decisions of the CONTRACTING PARTIES" within the meaning of paragraph 1(b)(iv) of the language of Annex 1A incorporating the GATT 1994 into the *WTO Agreement*. That provision stipulates that:

1. The General Agreement on Tariffs and Trade 1994 ("GATT 1994") shall consist of:

(b) the provisions of the legal instruments set forth below that have entered into force under the GATT 1947 before the date of entry into force of the WTO Agreement:

(iv) other decisions of the CONTRACTING PARTIES to GATT 1947[.]

¹⁹³See Panel Report, para. 7.44.

¹⁹⁴*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 2, p. 1948.

Clause permits Members to provide "differential and more favourable treatment" to developing countries "in spite of" the MFN obligation of Article I:1. Such treatment would otherwise be inconsistent with Article I:1 because that treatment is not extended to all Members of the WTO "immediately and unconditionally".¹⁹⁵ Paragraph 1 thus excepts Members from complying with the obligation contained in Article I:1 for the purpose of providing differential and more favourable treatment to developing countries, provided that such treatment is in accordance with the conditions set out in the Enabling Clause. As such, the Enabling Clause operates as an "exception" to Article I:1.

2. Object and Purpose of the WTO Agreement and the Enabling Clause

91. The European Communities' contention that the Enabling Clause is *not* in the nature of an exception appears to be founded on the European Communities' understanding of the object and purpose of the *Marrakesh Agreement Establishing the World Trade Organization* (the "WTO Agreement") and the Enabling Clause. We, too, look to the object and purpose of the *WTO Agreement* and the Enabling Clause to clarify whether the Enabling Clause was intended to operate as an exception to Article I:1.

92. The Preamble to the *WTO Agreement* provides that Members recognize:

... that there is need for *positive efforts* designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development[.]¹⁹⁶ (emphasis added)

The Waiver Decision on the Generalized System of Preferences (the "1971 Waiver Decision")¹⁹⁷, which provided the initial authorization under the GATT for developed countries' GSP schemes and is explicitly referred to in footnote 3 of the Enabling Clause¹⁹⁸, offers relevant guidance in discerning the object and purpose of the Enabling Clause. In the Preamble to the 1971 Waiver Decision, the Contracting Parties recognized:

¹⁹⁵GATT 1994, Art. I:1.

¹⁹⁶Second recital. We note that Article XXXVI:3 of the GATT 1994 similarly provides:

There is need for positive efforts designed to ensure that less-developed contracting parties secure a share in the growth in international trade commensurate with the needs of their economic development.

¹⁹⁷GATT Document L/3545, 25 June 1971, BISD 18S/24 (attached as Annex D-2 to the Panel Report).

¹⁹⁸Footnote 3 of the Enabling Clause states:

As described in the Decision of the CONTRACTING PARTIES of 25 June 1971, relating to the establishment of "generalized, non-reciprocal and non-discriminatory preferences beneficial to the developing countries" (BISD 18S/24).

... that a principal aim of the CONTRACTING PARTIES is promotion of the trade and export earnings of developing countries for the furtherance of their economic development;

[and recognized] further that individual and joint action is essential to further the development of the economies of developing countries[.]¹⁹⁹

We understand, therefore, that the Enabling Clause is among the "positive efforts" called for in the Preamble to the *WTO Agreement* to be taken by developed-country Members to enhance the "economic development" of developing-country Members.²⁰⁰

93. According to the European Communities, the Enabling Clause, as the "most concrete, comprehensive and important application of the principle of Special and Differential Treatment", serves "to achieve one of the fundamental objectives of the WTO Agreement".²⁰¹ In the view of the European Communities, provisions that are exceptions permit Members to adopt measures to pursue objectives that are "not ... among the WTO Agreement's own objectives"²⁰²; the Enabling Clause thus does not fall under the category of exceptions. Pointing to this alleged difference between the role of measures falling under the Enabling Clause and that of measures falling under exception provisions such as Article XX, the European Communities contends that the *WTO Agreement* does not "merely tolerate" measures under the Enabling Clause, but rather "encourages" developed-country Members to adopt such measures.²⁰³ According to the European Communities, to require preference-granting countries to invoke the Enabling Clause in order to justify or defend their GSP schemes cannot be reconciled with the intention of WTO Members to encourage these schemes.

94. We note, however, as did the Panel²⁰⁴, that WTO objectives may well be pursued through measures taken under provisions characterized as exceptions. The Preamble to the *WTO Agreement* identifies certain objectives that may be pursued by Members through measures that would have to be

¹⁹⁹First and second recitals. Similarly, Article XXXVI:1(d) of the GATT 1994 provides:

[I]ndividual and joint action is essential to further the development of the economies of less-developed contracting parties and to bring about a rapid advance in the standards of living in these countries[.]

²⁰⁰We discuss further the role of the Enabling Clause in the context of the covered agreements, *infra*, paras. 106-109.

²⁰¹European Communities' appellant's submission, para. 20.

²⁰²*Ibid.*, para. 52.

²⁰³*Ibid.*, para. 53.

²⁰⁴See Panel Report, para. 7.52.

justified under the "General Exceptions" of Article XX. For instance, one such objective is reflected in the recognition by Members that the expansion of trade must be accompanied by:

... the optimal use of the world's resources in accordance with the objective of sustainable development, [with Members] seeking both to protect and preserve the environment and to enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development[.]²⁰⁵

95. As the Appellate Body observed in *US – Shrimp*, WTO Members retained Article XX(g) from the *General Agreement on Tariffs and Trade 1947* (the "GATT 1947") without alteration after the conclusion of the Uruguay Round, being "fully aware of the importance and legitimacy of environmental protection as a goal of national and international policy".²⁰⁶ Article XX(g) of the GATT 1994 permits Members, subject to certain conditions, to take measures "relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption". It is well-established that Article XX(g) is an *exception* in relation to which the responding party bears the burden of proof.²⁰⁷ Thus, by authorizing in Article XX(g) measures for environmental conservation, an important objective referred to in the Preamble to the *WTO Agreement*, Members implicitly recognized that the implementation of such measures would not be discouraged simply because Article XX(g) constitutes a defence to otherwise WTO-inconsistent measures. Likewise, characterizing the Enabling Clause as an exception, in our view, does not undermine the importance of the Enabling Clause within the overall framework of the covered agreements and as a "positive effort" to enhance economic development of developing-country Members. Nor does it "discourage[]"²⁰⁸ developed countries from adopting measures in favour of developing countries under the Enabling Clause.

96. The European Communities acknowledges that requiring Members to pursue environmental measures through Article XX(g), an exception provision, may be logical because "the WTO Agreement is not an environmental agreement and ... it contains no positive regulation of environmental matters."²⁰⁹ Because the *WTO Agreement* "regulate[s] positively the use of trade

²⁰⁵*WTO Agreement*, Preamble, first recital.

²⁰⁶Appellate Body Report, *US – Shrimp*, para. 129.

²⁰⁷*Ibid.*, para. 157; Appellate Body Report, *US – Wool Shirts and Blouses*, pp. 15-16, DSR 1997-1, at 337 (referring to GATT Panel Report, *Canada – FIRA*, para. 5.20; GATT Panel Report, *US – Section 337*, para. 5.27; GATT Panel Report, *US – Malt Beverages*, paras. 5.43 and 5.52; and Panel Report, *US – Gasoline*, para. 6.20).

²⁰⁸United States' third participant's submission, para. 9.

²⁰⁹European Communities' appellant's submission, para. 54.

measures"²¹⁰, however, and the Enabling Clause "promotes" the use of trade measures to further the development of developing countries, the European Communities argues that Members should not be required to prove the consistency of their measures with the Enabling Clause.

97. We do not consider it relevant, for the purposes of determining whether a provision is or is not in the nature of an exception, that the provision governs "trade measures" rather than measures of a primarily "non-trade" nature. Indeed, in a previous appeal, the Appellate Body found that the proviso to Article XVIII:11 of the GATT 1994—a provision authorizing quantitative restrictions when taken in response to balance-of-payments difficulties—is a defence to be invoked by the responding party.²¹¹ The fact that a provision regulates the use of "trade measures", therefore, does not compel a finding that it is for the complaining party to establish inconsistency with that provision, rather than for the defending party to rely on it as a defence.

98. In sum, in our view, the characterization of the Enabling Clause as an exception in no way diminishes the right of Members to provide or to receive "differential and more favourable treatment". The status and relative importance of a given provision does not depend on whether it is characterized, for the purpose of allocating the burden of proof, as a claim to be proven by the complaining party, or as a defence to be established by the responding party. Whatever its characterization, a provision of the covered agreements must be interpreted in accordance with the "customary rules of interpretation of public international law", as required by Article 3.2 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU").²¹² Members' rights under the Enabling Clause are not curtailed by requiring preference-granting countries to establish in dispute settlement the consistency of their preferential measures with the conditions of the Enabling Clause. Nor does characterizing the Enabling Clause as an exception

²¹⁰European Communities' appellant's submission, para. 54.

²¹¹Appellate Body Report, *India – Quantitative Restrictions*, paras. 134-136. We also note that GATT panels determined Article XI:2(c) of the GATT 1947 to constitute an "exception", even though that provision addresses "trade measures", namely quantitative restrictions. (See GATT Panel Report, *Japan – Agricultural Products I*, para. 5.1.3.7; GATT Panel Report, *EEC – Dessert Apples*, para. 12.3; and GATT Panel Report, *Canada – Ice Cream and Yoghurt*, para. 59)

²¹²In this regard, we recall the Appellate Body's statement in *EC – Hormones* that:
... merely characterizing a treaty provision as an "exception" does not by itself justify a "stricter" or "narrower" interpretation of that provision than would be warranted by examination of the ordinary meaning of the actual treaty words, viewed in context and in the light of the treaty's object and purpose, or, in other words, by applying the normal rules of treaty interpretation.

(Appellate Body Report, para. 104)

detract from its critical role in encouraging the granting of special and differential treatment to developing-country Members of the WTO.

99. In the light of the above, we *uphold* the Panel's findings, in paragraph 7.53 of the Panel Report, that the Enabling Clause is an "exception" to Article I:1 of the GATT 1994.

100. We examine now the European Communities' appeal regarding the Panel's finding that the Enabling Clause "does not exclude the applicability" of Article I:1 of the GATT 1994.²¹³ The European Communities argues that the Enabling Clause exists "side-by-side and on an equal level" with Article I:1, and thus applies to the exclusion of that provision.²¹⁴ In our view, the European Communities misconstrues the relationship between the two provisions.

101. It is well settled that the MFN principle embodied in Article I:1 is a "cornerstone of the GATT" and "one of the pillars of the WTO trading system"²¹⁵, which has consistently served as a key basis and impetus for concessions in trade negotiations. However, we recognize that Members are entitled to adopt measures providing "differential and more favourable treatment" under the Enabling Clause. Therefore, challenges to such measures, brought under Article I:1, cannot succeed where such measures are in accordance with the terms of the Enabling Clause. In our view, this is so because the text of paragraph 1 of the Enabling Clause ensures that, to the extent that there is a conflict between measures under the Enabling Clause and the MFN obligation in Article I:1, the Enabling Clause, as the more specific rule, prevails over Article I:1. In order to determine whether such a conflict exists, however, a dispute settlement panel should, as a first step, examine the consistency of a challenged measure with Article I:1, as the general rule. If the measure is considered at this stage to be inconsistent with Article I:1, the panel should then examine, as a second step, whether the measure is nevertheless justified by the Enabling Clause. It is only at this latter stage that a final determination of consistency with the Enabling Clause or inconsistency with Article I:1 can be made.

²¹³Panel Report, para. 7.53.

²¹⁴European Communities' appellant's submission, para. 22.

²¹⁵Appellate Body Report, *Canada – Autos*, para. 69. See also, Appellate Body Report, *US – Section 211 Appropriations Act*, para. 297, which reads:

Like the national treatment obligation, the obligation to provide most-favoured-nation treatment has long been one of the cornerstones of the world trading system. For more than fifty years, the obligation to provide most-favoured-nation treatment in Article I of the GATT 1994 has been both central and essential to assuring the success of a global rules-based system for trade in goods.

102. In other words, the Enabling Clause "does not exclude the applicability"²¹⁶ of Article I:1 in the sense that, as a matter of procedure (or "order of examination", as the Panel stated²¹⁷), the challenged measure is submitted successively to the test of compatibility with the two provisions. But, as a matter of final determination—or *application* rather than *applicability*—it is clear that only one provision applies at a time. This is what the Panel itself found when, after stating that "as an exception provision, the Enabling Clause applies concurrently with Article I:1", it added "and *takes precedence* to the extent of the conflict between the two provisions."²¹⁸

103. It is with this understanding, therefore, that we *uphold* the Panel's finding, in paragraph 7.53 of the Panel Report, that the Enabling Clause "does not exclude the applicability" of Article I:1 of the GATT 1994.

D. *Burden of Proof*

104. We now examine the implications of the relationship between Article I:1 of the GATT 1994 and the Enabling Clause for the allocation of the burden of proof in this dispute. As a general rule, the burden of proof for an "exception" falls on the respondent, that is, as the Appellate Body stated in *US – Wool Shirts and Blouses*, on the party "assert[ing] the affirmative of a particular ... defence".²¹⁹ From this allocation of the burden of proof, it is normally for the respondent, first, to *raise* the defence and, second, to *prove* that the challenged measure meets the requirements of the defence provision.

105. We are therefore of the view that the European Communities must *prove* that the Drug Arrangements satisfy the conditions set out in the Enabling Clause. Consistent with the principle of *jura novit curia*²²⁰, it is not the responsibility of the European Communities to provide us with the

²¹⁶Panel Report, para. 7.53.

²¹⁷*Ibid.*, para. 7.45.

²¹⁸*Ibid.* (emphasis added)

²¹⁹Appellate Body Report, p. 14, DSR 1997:1, at 335. (See also, Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 133; and Appellate Body Report, *India – Quantitative Restrictions*, para. 136)

²²⁰The principle of *jura novit curia* has been articulated by the International Court of Justice as follows:

It being the duty of the Court itself to ascertain and apply the relevant law in the given circumstances of the case, the burden of establishing or proving rules of international law cannot be imposed upon any of the parties, for the law lies within the judicial knowledge of the Court.

(International Court of Justice, Merits, *Case Concerning Military and Paramilitary Activities in and against Nicaragua (Nicaragua v. United States of America)*, 1986 ICJ Reports, p. 14, para. 29 (quoting International Court of Justice, Merits, *Fisheries Jurisdiction Case (United Kingdom of Great Britain and Northern Ireland v. Iceland)*, 1974 ICJ Reports, p. 9, para. 17))

legal interpretation to be given to a particular provision in the Enabling Clause²²¹; instead, the burden of the European Communities is to adduce sufficient evidence to substantiate its assertion that the Drug Arrangements comply with the requirements of the Enabling Clause.

1. Responsibility for Raising the Enabling Clause

106. With respect to the legal responsibility for *raising* a defence as an issue in a dispute settlement proceeding, however, we regard the particular circumstances of this case as dictating a special approach, given the fundamental role of the Enabling Clause in the WTO system as well as its contents. The Enabling Clause authorizes developed-country Members to grant enhanced market access to products from developing countries beyond that granted to products from developed countries. Enhanced market access is intended to provide developing countries with increasing returns from their growing exports, which returns are critical for those countries' economic development. The Enabling Clause thus plays a vital role in promoting trade as a means of stimulating economic growth and development. In this respect, the Enabling Clause is not a typical "exception", or "defence", in the style of Article XX of the GATT 1994, or of other exception provisions identified by the Appellate Body in previous cases.

107. A brief review of the history of the Enabling Clause confirms its special status in the covered agreements. When the GATT 1947 entered into force, the Contracting Parties stated that one of its objectives was to "rais[e] standards of living".²²² However, this objective was to be achieved in countries at all stages of economic development through the *universally-applied* commitments embodied in the GATT provisions. In 1965, the Contracting Parties added Articles XXXVI, XXXVII, and XXXVIII to form Part IV of the GATT 1947, entitled "Trade and Development".²²³ Article XXXVI expressly recognized the "need for positive efforts" and "individual and joint action" so that developing countries would be able to share in the growth in international trade and further their economic development.²²⁴ Some of these "positive efforts" resulted in the Agreed Conclusions

²²¹Compare Appellate Body Report, *EC – Hormones*, para. 156, which states:

[N]othing in the DSU limits the faculty of a panel freely to use arguments submitted by any of the parties -- or to develop its own legal reasoning -- to support its own findings and conclusions on the matter under its consideration. A panel might well be unable to carry out an objective assessment of the matter, as mandated by Article 11 of the DSU, if in its reasoning it had to restrict itself solely to arguments presented by the parties to the dispute.

²²²GATT 1947, Preamble, first recital.

²²³*Protocol Amending the General Agreement on Tariffs and Trade to Introduce a Part IV on Trade and Development*, BISD 13S/2 (1965).

²²⁴GATT 1947, Arts. XXXVI:3 and XXXVII:1(d).

of the United Nations Conference on Trade and Development ("UNCTAD") Special Committee on Preferences (the "Agreed Conclusions")²²⁵, which recognized that preferential tariff treatment accorded under a generalized scheme of preferences was key for developing countries "(a) to increase their export earnings; (b) to promote their industrialization; and (c) to accelerate their rates of economic growth."²²⁶ The Agreed Conclusions also made clear that the achievement of these objectives through the adoption of preferences by developed countries required a GATT waiver, in particular, with respect to the MFN obligation in Article I.1.²²⁷ Accordingly, the Contracting Parties adopted the 1971 Waiver Decision in order to waive the obligations of Article I of the GATT 1947 and thereby authorize the granting of tariff preferences to developing countries for a period of ten years.²²⁸

108. In 1979, the Enabling Clause expanded the authorization provided by the 1971 Waiver Decision to cover additional preferential measures and made the authorization a permanent feature of the GATT. In his report at the conclusion of the Tokyo Round of negotiations, the then-Director General observed:

The Enabling Clause meets a fundamental concern of developing countries by introducing differential and more favourable treatment as an integral part of the GATT system, no longer requiring waivers from the GATT. It also provides the perspective against which the participation of developing countries in the trading system may be seen.²²⁹

Members reaffirmed the significance of the Enabling Clause in 1994 with the incorporation of the Enabling Clause into the GATT 1994.²³⁰ The relationship between trade and development, and in particular the role of the Enabling Clause, remain prominent on the agenda of the WTO, as recognized by the Doha Ministerial Conference in 2001.²³¹

109. We thus understand that, between the entry into force of the GATT and the adoption of the Enabling Clause, the Contracting Parties determined that the MFN obligation failed to secure

²²⁵Attached as Annex D-4 to the Panel Report.

²²⁶Agreed Conclusions, para. I.2 (Panel Report, p. D-8).

²²⁷*Ibid.*, paras. IX.1 and IX.2(c) (Panel Report, pp. D-13–D-14).

²²⁸1971 Waiver Decision, para. (a) (Panel Report, p. D-4).

²²⁹European Communities' appellant's submission, para. 25 (quoting Report by the Director-General of GATT, in GATT, *The Tokyo Round of Multilateral Trade Negotiations* (1979), Vol. I, p. 99).

²³⁰Para. 1(b)(iv) of the language of Annex 1A to the *WTO Agreement* incorporating the GATT 1994 into the *WTO Agreement*.

²³¹Ministerial Decision of 14 November 2001, *Implementation-related Issues and Concerns*, WT/MIN(01)/17, paras. 12.1-12.2.

adequate market access for developing countries so as to stimulate their economic development. Overcoming this required recognition by the multilateral trading system that certain obligations, applied to all Contracting Parties, could impede rather than facilitate the objective of ensuring that developing countries secure a share in the growth of world trade. This recognition came through an authorization for GSP schemes in the 1971 Waiver Decision and then in the broader authorization for preferential treatment for developing countries in the Enabling Clause.²³²

110. In our view, the special status of the Enabling Clause in the WTO system has particular implications for WTO dispute settlement. As we have explained, paragraph 1 of the Enabling Clause enhances market access for developing countries as a means of improving their economic development by authorizing preferential treatment for those countries, "notwithstanding" the obligations of Article I. It is evident that a Member cannot implement a measure authorized by the Enabling Clause without according an "advantage" to a developing country's products over those of a developed country. It follows, therefore, that every measure undertaken pursuant to the Enabling Clause would necessarily be inconsistent with Article I, if assessed on that basis alone, but it would be exempted from compliance with Article I because it meets the requirements of the Enabling Clause. Under these circumstances, we are of the view that a complaining party challenging a measure taken pursuant to the Enabling Clause must allege more than mere inconsistency with Article I:1 of the GATT 1994, for to do only that would not convey the "legal basis of the complaint sufficient to present the problem clearly".²³³ In other words, it is insufficient in WTO dispute settlement for a complainant to allege inconsistency with Article I:1 of the GATT 1994 if the complainant seeks also to argue that the measure is not justified under the Enabling Clause. This is especially so if the challenged measure, like that at issue here, is plainly taken pursuant to the Enabling Clause, as we discuss *infra*.²³⁴

111. Furthermore, the history and objective of the Enabling Clause lead us to agree with the European Communities²³⁵ that Members are *encouraged* to deviate from Article I in the pursuit of "differential and more favourable treatment" for developing countries. This deviation, however, is encouraged only to the extent that it complies with the series of requirements set out in the Enabling

²³²We recognize that an exemption for developing countries from certain GATT obligations also resulted from the 1954-1955 Review Session, where the Contracting Parties amended the GATT by adding Article XVIII for the benefit of developing countries facing balance-of-payments difficulties or seeking to nurture an infant industry. (See Reports Relating to the Review of the Agreement: Quantitative Restrictions, GATT Document L/332/Rev.1 and Addenda, adopted 2, 4 and 5 March 1955, BISD, 3S/170, paras. 3, 35-36, 44, and 52)

²³³DSU, Art. 6.2. See also, Appellate Body Report, *Korea – Dairy*, paras. 120, 124, and 127.

²³⁴*Infra*, paras. 116-117.

²³⁵European Communities' appellant's submission, para. 53.

Clause, requirements that we find to be more extensive than more typical defences such as those found in Article XX.

112. Paragraph 2 of the Enabling Clause identifies the four types of measures to which the authorization of paragraph 1 applies:

- (a) Preferential tariff treatment accorded by developed contracting parties to products originating in developing countries in accordance with the Generalized System of Preferences;³
- (b) Differential and more favourable treatment with respect to the provisions of the General Agreement concerning non-tariff measures governed by the provisions of instruments multilaterally negotiated under the auspices of the GATT;
- (c) Regional or global arrangements entered into amongst less-developed contracting parties for the mutual reduction or elimination of tariffs and, in accordance with criteria or conditions which may be prescribed by the CONTRACTING PARTIES, for the mutual reduction or elimination of non-tariff measures, on products imported from one another
- (d) Special treatment of the least developed among the developing countries in the context of any general or specific measures in favour of developing countries.

³ As described in the Decision of the CONTRACTING PARTIES of 25 June 1971, relating to the establishment of "generalized, non-reciprocal and non-discriminatory preferences beneficial to the developing countries" (BISD 18S/24).

Measures that a Member claims are exempt from a finding of inconsistency with Article I by virtue of the Enabling Clause must fit within these sub-paragraphs, of which the most relevant for this case is paragraph 2(a), which provides for GSP schemes. As we discuss in greater detail *infra*²³⁶, this provision requires the preferential treatment to be "in accordance with" the GSP and further defines this obligation through each of the terms "generalized, non-reciprocal and non-discriminatory". Paragraphs 2(b)-(d) impose different obligations to be satisfied by a Member taking a measure pursuant to those provisions. Paragraph 3 identifies three conditions that must also be satisfied by any measure under the Enabling Clause. Paragraph 4 sets forth procedural conditions for the introduction, modification, or withdrawal of a preferential measure for developing countries.

²³⁶*Infra*, paras. 142-174.

Paragraphs 5 through 9 include obligations that are not necessarily related to measures providing "differential and more favourable treatment".²³⁷

113. In the light of the extensive requirements set forth in the Enabling Clause, we are of the view that, when a complaining party considers that a preference scheme of another Member does not meet one or more of those requirements, the specific provisions of the Enabling Clause with which the scheme allegedly falls afoul, form critical components of the "legal basis of the complaint"²³⁸ and, therefore, of the "matter" in dispute.²³⁹ Accordingly, a complaining party cannot, in good faith, ignore those provisions and must, in its request for the establishment of a panel, identify them and thereby "notify" the parties and third parties of the nature of [its] case".²⁴⁰ For the failure of such a complaining party to raise the relevant provisions of the Enabling Clause would place an unwarranted burden on the responding party. This due process consideration applies equally to the elaboration of a complaining party's case in its written submissions, which must "explicitly" articulate a claim so that the panel and all parties to a dispute "understand that a specific claim has been made, [are] aware of its dimensions, and have an adequate opportunity to address and respond to it".²⁴¹

114. Exposing preference schemes to open-ended challenges would be inconsistent, in our view, with the intention of Members, as reflected in the Enabling Clause, to "encourage"²⁴² the adoption of preferential treatment for developing countries and to provide a practical means of doing so within the legal framework of the covered agreements. Accordingly, although a responding party must defend the consistency of its preference scheme with the conditions of the Enabling Clause and must prove such consistency, a *complaining* party has to define the parameters within which the *responding* party must make that defence.

²³⁷See Enabling Clause (attached as Annex 2 to this Report).

²³⁸DSU, Art. 6.2, which provides:

The request for the establishment of a panel shall be made in writing. It shall indicate whether consultations were held, identify the specific measures at issue and provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly. In case the applicant requests the establishment of a panel with other than standard terms of reference, the written request shall include the proposed text of special terms of reference.

²³⁹Appellate Body Report, *US – Carbon Steel*, para. 125 (referring to Appellate Body Report, *Guatemala – Cement I*, paras. 69-76).

²⁴⁰*Ibid.*, para. 126 (referring to Appellate Body Report, *Brazil – Desiccated Coconut*, p. 22, DSR 1997:1, at 186; and Appellate Body Report, *EC – Bananas III*, para. 142).

²⁴¹Appellate Body Report, *Chile – Price Band System*, para. 164.

²⁴²European Communities' appellant's submission, para. 53.

115. The responsibility of the complaining party in such an instance, however, should not be overstated. It is merely to *identify* those provisions of the Enabling Clause with which the scheme is allegedly inconsistent, without bearing the burden of *establishing* the facts necessary to support such inconsistency. That burden, as we concluded above²⁴³, remains on the responding party invoking the Enabling Clause as a defence.

116. We observe, moreover, that the measure challenged in this dispute is unmistakably a preferential tariff scheme, granted by a developed-country Member in favour of developing countries, and proclaiming to be in accordance with the GSP. The Drug Arrangements are found in Council Regulation (EC) No. 2501/2001, the title of which indicates the Regulation to be "applying a scheme of generalised tariff preferences for the period from 1 January 2002 to 31 December 2004". The first recital in the Preamble to the Regulation provides:

Since 1971, the Community has granted trade preferences to developing countries, in the framework of its scheme of generalised tariff preferences.

In its original proposal for the Regulation, the European Commission explained:

In 1994, the Commission adopted some guidelines on the *role of the GSP* for the ten-year period 1995 to 2004. A new regulation is required in order to implement *those guidelines* for the remainder of the period, i.e. the years 2002 to 2004. This memorandum is meant to explain the proposal for that new regulation.²⁴⁴ (footnote omitted; emphasis added)

In its amended proposal, adding Pakistan to the list of beneficiaries under the Drug Arrangements, the European Commission further stated:

Since the *GSP drug regime* was extended to the countries of the Andean Community and to those of the Central American Common Market, it provided an important incentive to allow for the substitution of illicit crops, enhance exports in order to create jobs not linked to drug production and trafficking and foster diversification.

²⁴³*Supra*, para. 105.

²⁴⁴Explanatory Memorandum to the Proposal for a Council Regulation applying a scheme of generalised tariff preferences for the period 1 January 2002 to 31 December 2004, para. 1 (attached to Amended Proposal for a Council Regulation applying a scheme of generalised tariff preferences for the period 1 January 2002 to 31 December 2004, 2001/0131 (ACC), at p. 3) (Exhibit India-7 submitted by India to the Panel).

The problems which Pakistan is facing today, are similar. The *GSP drug regime* is therefore likely to stabilise its economic and social structures and thus consolidate the institutions that uphold the rule of law.²⁴⁵ (emphasis added)

117. It is therefore clear, on the face of the Regulation and from official, publicly-available explanatory documentation, that the Drug Arrangements challenged by India in this dispute are part of a preferential tariff scheme implemented by the European Communities pursuant to the authorization in paragraph 2(a) of the Enabling Clause. As such, India would have been well aware that the Drug Arrangements must comply with the requirements of the Enabling Clause, and that the European Communities was likely to invoke the Enabling Clause in response to a challenge of inconsistency with Article I:1. Indeed, India admitted as much before the Panel.²⁴⁶ India also must have believed that at least certain of those requirements were not being met and that, as a consequence, the inconsistency of the Drug Arrangements with Article I could not be justified. Accordingly, India, as the complaining party, should reasonably have articulated its claims of inconsistency with specific provisions of the Enabling Clause at the outset of this dispute as part of its responsibility to "engage in [dispute settlement] procedures in good faith in an effort to resolve the dispute".²⁴⁷

118. In sum, although the burden of *justifying* the Drug Arrangements under the Enabling Clause falls on the European Communities, India was required to do more than simply allege inconsistency with Article I. India's claim of inconsistency with Article I with respect to the measure challenged here is inextricably linked with its argument that the Drug Arrangements do not satisfy the conditions in the Enabling Clause and that, therefore, they cannot be justified as a derogation from Article I. In the light of the above considerations, we are of the view that India was required to (i) identify, in its

²⁴⁵Explanatory Memorandum to the Amended Proposal for a Council Regulation applying a scheme of generalised tariff preferences for the period 1 January 2002 to 31 December 2004, 2001/0131 (ACC), p. 2, fourth and fifth recitals (Exhibit India-7 submitted by India to the Panel).

²⁴⁶See, for example, India's first written submission to the Panel, para. 44, which states: "[S]ince the Drug Arrangements are part of the EC's GSP scheme, it may reasonably be assumed that the EC will invoke the Enabling Clause as a defence."

²⁴⁷DSU, Art. 3.10. See also, Appellate Body Report, *US – FSC*, para. 166, which reads: Article 3.10 of the DSU commits Members of the WTO, if a dispute arises, to engage in dispute settlement procedures "in good faith in an effort to resolve the dispute". This is another specific manifestation of the principle of good faith which, we have pointed out, is at once a general principle of law and a principle of general international law. This pervasive principle requires both complaining and responding Members to comply with the requirements of the DSU (and related requirements in other covered agreements) in good faith. By good faith compliance, complaining Members accord to the responding Members the full measure of protection and opportunity to defend, contemplated by the letter and spirit of the procedural rules. (footnote omitted)

request for the establishment of a panel, which obligations in the Enabling Clause the Drug Arrangements are alleged to have contravened, and (ii) make written submissions in support of this allegation. The requirement to make such an argument, however, does not mean that India must prove inconsistency with a provision of the Enabling Clause, because the ultimate burden of establishing the consistency of the Drug Arrangements with the Enabling Clause lies with the European Communities.²⁴⁸

2. Whether India Raised the Enabling Clause Before the Panel

119. We turn now to examine whether, in fact, India fulfilled these requirements and thereby sufficiently identified the scope of its claim before the Panel. In its request for consultations, India claimed that the Drug Arrangements and the special incentive arrangements for the protection of labour rights and the environment "nullify or impair the benefits accruing to India under the most-favoured-nation provisions of Article I:1 of the GATT 1994 and paragraphs 2(a), 3(a) and 3(c) of the Enabling Clause."²⁴⁹ In its request for the establishment of a panel, India asked that a panel examine whether the aforementioned arrangements of the European Communities' GSP scheme "are consistent with Article I:1 of the GATT 1994 and the requirements set out in paragraphs 2(a), 3(a) and 3(c) of the Enabling Clause".²⁵⁰ The Panel's terms of reference, therefore, included India's allegations that certain aspects of the European Communities' GSP scheme were not "consistent" with, or did not "meet the requirements set out in", paragraphs 2(a), 3(a), and 3(c) of the Enabling Clause.²⁵¹

²⁴⁸Compare Appellate Body Report, *US – Certain EC Products*, para. 114, which states:

On the basis of our review of the European Communities' submissions and statements to the Panel, we conclude that the European Communities *did not specifically claim* before the Panel that, by adopting the 3 March Measure, the United States acted inconsistently with Article 23.2(a) of the DSU. As the European Communities did not make a specific claim of inconsistency with Article 23.2(a), it *did not adduce any evidence or arguments* to demonstrate that the United States made a "determination as to the effect that a violation has occurred" in breach of Article 23.2(a) of the DSU. And, as the European Communities did not adduce any evidence or arguments in support of a claim of violation of Article 23.2(a) of the DSU, the European Communities could not have established, and *did not establish, a prima facie case* of violation of Article 23.2(a) of the DSU. (footnotes omitted; emphasis added)

²⁴⁹Request for consultations by India, WT/DS246/1, 12 March 2002, p. 1.

²⁵⁰Request for the establishment of a panel by India, WT/DS246/4, 9 December 2002, p. 2. In addition to the Drug Arrangements and the special incentives for the protection of labour rights and the environment, India also challenged the WTO-consistency of "any implementing rules and regulations, ... any amendments to any of the foregoing, and ... their application". (*Ibid.*)

²⁵¹Request for the establishment of a panel by India, WT/DS246/4, 9 December 2002, pp. 1-2. The Panel's terms of reference incorporated these allegations by reference to document WT/DS246/4. (Constitution of the panel established at the request of India, WT/DS246/5, 6 March 2003, para. 2)

120. In its written submissions before the Panel, India clearly invoked paragraph 2(a) of the Enabling Clause as the basis for its allegation that the Drug Arrangements are not "justified" by the Enabling Clause.²⁵² For example, in its first written submission before the Panel, India stated:

The tariff preferences under the Drug Arrangements are beneficial to some developing countries and detrimental to others and consequently do not comply with paragraph 2(a) of the Enabling Clause.²⁵³

121. India's second written submission before the Panel included a sub-heading entitled, "The EC has failed to demonstrate that under the Drug Arrangements it accords tariff treatment that is 'non-discriminatory' within the meaning of paragraph 2(a) of the Enabling Clause".²⁵⁴ Under this sub-heading, India argued:

[P]aragraph 2(a) of the Enabling Clause was meant to ensure that benefits under the GSP are extended to *all* developing countries, as opposed to some developing countries. Paragraph 2(a) of the Enabling Clause does not envisage selectivity. Instead, it requires that preferential tariff treatment is accorded to all developing countries.²⁵⁵ (original italics)

India further argued that, even if the European Communities' interpretation of paragraph 2(a) were correct, the Drug Arrangements would not be "non-discriminatory", as required by footnote 3 to paragraph 2(a).²⁵⁶

122. We find that India acted in good faith, in its written submissions before the Panel, explaining why, in its view, the Drug Arrangements fail to meet certain requirements of the Enabling Clause, namely, those present in paragraph 2(a). Such an explanation, in our view, was sufficient to place the European Communities on notice as to the reasons underlying India's allegation that the Drug Arrangements are not justified by the relevant provision of the Enabling Clause. With such notice, India's first written submission to the Panel, heading IV.C. and para. 67; India's second written submission to the Panel, heading III.B. and para. 164. By the time of its first written submission to the Panel, India had indicated to the European Communities and to the Panel that this dispute was limited to the WTO-consistency of the Drug Arrangements, but that India reserved its right to challenge the special incentives for the protection of labour rights and the environment in a future dispute settlement proceeding. (See *supra*, para. 4; and Panel Report, para. 1.5) Both participants confirmed, in response to questioning at the oral hearing, that the measure at issue in this dispute was limited to the Drug Arrangements.

²⁵³India's first written submission to the Panel, para. 62.

²⁵⁴India's second written submission to the Panel, heading III.B.3.

²⁵⁵*Ibid.*, para. 95.

²⁵⁶*Ibid.*, paras. 119-128.

the European Communities could be expected to defend its challenged measure under the Enabling Clause, in relation to which the European Communities ultimately bears the burden of justification.

123. In allocating the burden of proof, therefore, we conclude that India was required to raise the Enabling Clause in making its claim of inconsistency with Article I.1. Once India had identified, in its panel request and through argumentation in its written submissions, the relevant obligations of the Enabling Clause that it claims were not satisfied by the Drug Arrangements, the European Communities was then required to prove that the Drug Arrangements met those obligations, having chosen to rely on the Enabling Clause as a defence.

124. Finally, we observe that the European Communities' appeal of the Panel's conclusion that the Drug Arrangements are inconsistent with Article I.1 of the GATT 1994 is "based on" the European Communities' claim that the Panel erroneously found that (i) the Enabling Clause is an "exception" to Article I.1; (ii) the Enabling Clause "does not exclude the applicability" of Article I.1; and (iii) the European Communities had the burden of proving the consistency of the Drug Arrangements with that Clause.²⁵⁷ As we have not reversed any of these findings of the Panel²⁵⁸, we do not need to review further and we *do not rule* on the Panel's conclusion that the Drug Arrangements are inconsistent with Article I.1 of the GATT 1994.²⁵⁹

125. For these reasons, we *modify* the Panel's finding, in paragraph 7.53 of the Panel Report, that "the European Communities bears the burden of invoking the Enabling Clause and justifying its Drug Arrangements under that provision." We *find* that it was incumbent upon India to *raise* the Enabling Clause in making its claim of inconsistency with Article I.1 of the GATT 1994, but that the

²⁵⁷In its Notice of Appeal, the European Communities' reference to Article I.1 was limited to its decision to:

... seek[] review of the Panel's legal conclusion that [the Drug Arrangements] are inconsistent with Article I.1 ... This conclusion is based on the following erroneous legal findings:

- that the Enabling Clause is an "exception" to Article I.1 of the GATT;
- that the Enabling Clause does not exclude the applicability of Article I.1 of the GATT;
- that the EC had the burden of proving that the Drug Arrangements were consistent with the Enabling Clause.

(Notification of an appeal by the European Communities, WT/DS246/7, 8 January 2004, p.1 (attached as Annex 1 to this Report))

²⁵⁸*Supra*, paras. 99, 103, and 123.

²⁵⁹Panel Report, paras. 7.60 and 8.1(b). The European Communities confirmed, in response to questioning at the oral hearing, that it is not appealing the Panel's conclusion, in paragraph 7.60 of the Panel Report, that the tariff advantages under the Drug Arrangements are inconsistent with Article I.1 because they are not accorded "unconditionally" to the like products originating in all other WTO Members.

European Communities bore the burden of *proving* that the Drug Arrangements satisfy the conditions of the Enabling Clause, in order to justify those Arrangements under that Clause. We *find*, further, that India sufficiently raised paragraph 2(a) of the Enabling Clause in making its claim of inconsistency with Article I:1 before the Panel. We turn now to examine whether the European Communities met its burden of justifying the Drug Arrangements under that provision.

V. Whether the Drug Arrangements are Justified Under the Enabling Clause

126. The European Communities "appeals subsidiarily" the Panel's finding that the Drug Arrangements are not justified under paragraph 2(a), should we "conclude that the Enabling Clause is an exception to GATT Article I:1, or that India made a valid claim under the Enabling Clause".²⁶⁰ Having found that the Enabling Clause is in the nature of an exception to Article I:1 of the GATT 1994, we proceed to examine the European Communities' appeal as it relates to paragraph 2(a) of the Enabling Clause.

127. The European Communities challenges three of the Panel's findings, namely that:

- (a) "the term 'non-discriminatory' in footnote 3 [to paragraph 2(a) of the Enabling Clause] requires that identical tariff preferences under GSP schemes be provided to all developing countries without differentiation, except for the implementation of a priori limitations"²⁶¹;
- (b) "the term 'developing countries' in paragraph 2(a) [of the Enabling Clause] should be interpreted to mean *all* developing countries, with the exception that where developed countries are implementing a priori limitations, 'developing countries' may mean *less than all* developing countries"²⁶²; and, ultimately, that
- (c) the European Communities failed "to demonstrate that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause".²⁶³

²⁶⁰European Communities' appellant's submission, para. 67.

²⁶¹Panel Report, paras. 7.161 and 7.176.

²⁶²*Ibid.*, para. 7.174. (original italics; footnote omitted)

²⁶³*Ibid.*, para. 8.1(d).

128. Before addressing these specific issues, we will identify the precise scope of the appeal before us. In doing so, we note that both the European Communities and India agree that, in addressing paragraph 2(a) of the Enabling Clause, the Panel implicitly made findings on issues that were not before it. Thus, India submits that "[t]he issue before the Panel was not whether the EC could exclude from its GSP scheme countries claiming developing country status."²⁶⁴ In India's view, that issue did not arise "because India and all the countries enjoying tariff preferences under the Drug Arrangements are beneficiaries under the EC's GSP scheme."²⁶⁵ Also not before the Panel, according to India, was "whether the EC's mechanisms for the graduation of developing countries meet the requirements of the Enabling Clause."²⁶⁶ India emphasizes that it "did not submit any claims on these issues to the Panel because they are not relevant to the resolution of this dispute."²⁶⁷ In other words, according to India, the legal issues raised in this dispute "relate exclusively"²⁶⁸ to the treatment of those countries that a preference-granting country has included in its GSP scheme as beneficiaries. The European Communities echoes India's concern that the Panel read obligations into the Enabling Clause "in respect of issues which had not been raised by any of the parties and which [the Panel] did not have to address in order to resolve the dispute".²⁶⁹

129. Against this background, we understand India's claim before the Panel to have been limited to the consistency of the Drug Arrangements with the term "non-discriminatory" in footnote 3 to paragraph 2(a) of the Enabling Clause.²⁷⁰ In particular, India's challenge to the Drug Arrangements is based on its submission that the term "non-discriminatory" prevents preference-granting countries from according preferential tariff treatment to any beneficiary of their GSP schemes without granting identical preferential tariff treatment to all other beneficiaries. Therefore, in this Report, we do not rule on whether the Enabling Clause permits *ab initio* exclusions from GSP schemes of countries claiming developing country status, or the partial or total withdrawal of GSP benefits from certain developing countries under certain conditions.

²⁶⁴India's appellee's submission, para. 101.

²⁶⁵*Ibid.*

²⁶⁶India's opening statement at the oral hearing. By "graduation", we understand India to refer to the withdrawal of preferential tariff treatment with respect to specific products or designated developing countries on grounds of the degree of their development.

²⁶⁷India's opening statement at the oral hearing.

²⁶⁸India's appellee's submission, para. 103.

²⁶⁹European Communities' appellant's submission, para. 7.

²⁷⁰See *supra*, paras. 120-122.

130. We note, moreover, that the European Communities has *not* appealed the Panel's interpretation of paragraph 3(c) of the Enabling Clause.²⁷¹ Instead, the European Communities has invoked that provision solely as "contextual support" for its interpretation of "non-discriminatory" in footnote 3.²⁷² We also note that the Panel made no findings in this case as to whether the Drug Arrangements are inconsistent with paragraph 3(a) or 3(c) of the Enabling Clause. Our mandate, pursuant to Article 17.6 of the DSU, is limited to "issues of law covered in the panel report and legal interpretations developed by the panel". Therefore, in this appeal, we are not required to, and we shall not address, the issue of whether the Drug Arrangements are consistent with paragraphs 3(a) and 3(c) of the Enabling Clause. This does not prevent us, of course, from examining those paragraphs as context for our interpretation of "non-discriminatory" in footnote 3.

131. With these considerations in mind, we turn to address the meaning of the term "non-discriminatory" in footnote 3. In doing so, we consider it useful to begin our analysis by setting out briefly the relevant findings of the Panel.

A. *Panel Findings*

132. The Panel stated at the outset that "[t]he main issue disputed by the parties is whether the Drug Arrangements are consistent with paragraph 2(a) of the Enabling Clause, particularly the requirement of 'non-discriminatory' in footnote 3 to this subparagraph." ²⁷³ Paragraph 2(a) reads:

2. The provisions of paragraph 1 apply to the following:

- (a) Preferential tariff treatment accorded by developed contracting parties to products originating in developing countries in accordance with the Generalized System of Preferences,³

³ As described in the Decision of the CONTRACTING PARTIES of 25 June 1971, relating to the establishment of "generalized, non-reciprocal and non discriminatory preferences beneficial to the developing countries" (BISD 18S/24). (footnote 2 omitted)

²⁷¹The European Communities refers to the Panel's finding, in paragraph 7.99 of the Panel Report, that paragraph 3(c) requires preference-granting countries to "provide product coverage and tariff cuts at levels in general no less than those offered and accepted in the Agreed Conclusions." The European Communities explains that "[s]ince this issue was not raised by India and is not directly relevant to the issues in dispute, ... the EC has not deemed [it necessary] to appeal it." (European Communities' appellant's submission, footnote 40 to para. 47)

²⁷²European Communities' appellant's submission, para. 126.

²⁷³Panel Report, para. 7.65.

133. The Panel went on to examine, not the language of those provisions, but the meaning of paragraph 3(c) of the Enabling Clause, which reads:

- 3. Any differential and more favourable treatment provided under this clause:

...

- (c) shall in the case of such treatment accorded by developed contracting parties to developing countries be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries.

The Panel explained that "[i]t is only possible to give a full meaning to paragraph 2(a) and footnote 3 after determining whether paragraph 3(c) allows differentiation among developing countries in 'respond[ing] positively to the development, financial and trade needs of developing countries'." ²⁷⁴

134. Having found that the text of paragraph 3(c) "does not reveal whether the 'needs of developing countries' refers to the needs of *all* developing countries or to the needs of *individual* developing countries" ²⁷⁵, the Panel proceeded to examine "the drafting history in UNCTAD ... to identify the intention of the drafters on issues relating to the GSP arrangements." ²⁷⁶ The Panel concluded that paragraph 3(c) allows for differentiation among beneficiaries for the purposes of granting preferential treatment to least-developed countries and setting *a priori* import limitations for products originating in particularly competitive developing countries. The Panel asserted that "[n]o other differentiation among developing countries is permitted by paragraph 3(c)." ²⁷⁷

135. Having made these findings based on its review of what it considered the "context" and "preparatory work" ²⁷⁸ of paragraph 3(c) of the Enabling Clause, the Panel turned to examine paragraph 2(a) and footnote 3 thereto. The Panel observed that the word "discriminate ... can have either a *neutral* meaning of making a distinction or a *negative* meaning carrying the connotation of a distinction that is unjust or prejudicial." ²⁷⁹ In order to determine the appropriate meaning of the

²⁷⁴Panel Report, para. 7.65 (quoting Enabling Clause, para. 3(c) (attached as Annex 2 to this Report)). In a footnote, the Panel explained further that "[t]he European Communities argue[d] that 'if the term 'non-discriminatory' was interpreted as prohibiting any difference in treatment between developing countries, developed countries would be effectively precluded from responding positively to those needs, thus rendering [to] a nullity the requirement set forth in paragraph 3(c)'" (*Ibid.*, footnote 291 to para. 7.65 (quoting European Communities' first written submission to the Panel, para. 71))

²⁷⁵*Ibid.*, para. 7.78. (original italics)

²⁷⁶*Ibid.*, para. 7.80.

²⁷⁷*Ibid.*, para. 7.116.

²⁷⁸*Ibid.*, para. 7.88.

²⁷⁹*Ibid.*, para. 7.126. (original italics)

term "non-discriminatory" as used in footnote 3, the Panel turned to the context of that term. According to the Panel, this context includes paragraphs 2(a), 2(d), and 3(c) of the Enabling Clause, with the "most relevant elements of context" being Resolution 21(II) of the Second Session of UNCTAD ("Resolution 21(II)")²⁸⁰ and the Agreed Conclusions.²⁸¹ Based on its review of these documents, the Panel found that:

... the clear intention of the negotiators was to provide GSP equally to all developing countries and to eliminate all differentiation in preferential treatment to developing countries, with the exception of the implementation of a priori limitations in GSP schemes.²⁸²

136. The Panel concluded:

... that the requirement of non-discrimination, as a general principle formally set out in Resolution 21(II) and later carried over into the 1971 Waiver Decision and then into the Enabling Clause, obliges preference-giving countries to provide the GSP benefits to *all* developing countries without differentiation, except for the implementation of a priori limitations in GSP schemes.²⁸³ (original italics)

137. The Panel found further support for its conclusion in its previous analysis of paragraph 3(c)²⁸⁴ and in paragraph 2(d) of the Enabling Clause, which provides:

2. The provisions of paragraph 1 apply to the following:

(d) Special treatment of the least developed among the developing countries in the context of any general or specific measures in favour of developing countries. (footnote omitted)

The Panel stated that the term "non-discriminatory" cannot be interpreted "to permit preferential treatment to less than all developing countries without an explicit authorization".²⁸⁵ According to the Panel, "[s]uch explicit authorization is only provided for the benefit of the least-developed countries

²⁸⁰Resolution 21(II) of the Second Session of UNCTAD, entitled "Expansion and Diversification of Exports of Manufactures and Semi-Manufactures of Developing Countries" (attached as Annex D-3 to the Panel Report).

²⁸¹Panel Report, para. 7.128.

²⁸²*Ibid.*, para. 7.144.

²⁸³*Ibid.*

²⁸⁴*Ibid.*, paras. 7.148-7.149.

²⁸⁵*Ibid.*, para. 7.151.

in paragraph 2(d) of the Enabling Clause and for the implementation of a priori limitations, as set out in the Agreed Conclusions." ²⁸⁶

138. Turning to the "object and purpose" of the Enabling Clause, the Panel considered that "the objective of promoting the trade of developing countries and that of promoting trade liberalization generally"²⁸⁷ are relevant for the interpretation of the term "non-discriminatory". The Panel determined, however, that the latter "contributes more to guiding the interpretation of 'non-discriminatory', given its function of preventing abuse in providing GSP." ²⁸⁸

139. The Panel found further support for its interpretation in an examination of the "overall practice" of preference-granting countries²⁸⁹, which, according to the Panel, "suggests that there was a common understanding of 'equal' treatment to all developing countries except for a priori measures, and that it was on this basis that the 1971 Waiver Decision was adopted." ²⁹⁰

140. Based on its analysis described above, the Panel found that:

... the term "non-discriminatory" in footnote 3 requires that *identical* tariff preferences under GSP schemes be provided to *all* developing countries without differentiation, except for the implementation of a priori limitations.²⁹¹ (emphasis added)

141. Regarding the measure at issue in this dispute, the Panel found that:

... the European Communities' Drug Arrangements, as a GSP scheme, do not provide identical tariff preferences to *all* developing countries and that the differentiation is neither for the purpose of special treatment to the least-developed countries, nor in the context of the implementation of a priori measures. Such differentiation is inconsistent with paragraph 2(a), particularly the term "non-discriminatory" in footnote 3[.]²⁹² (original italics)

Consequently, the Panel also found that "the European Communities has failed to demonstrate that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause".²⁹³

²⁸⁶Panel Report, para. 7.151.

²⁸⁷*Ibid.*, para. 7.158.

²⁸⁸*Ibid.*

²⁸⁹*Ibid.*, para. 7.159.

²⁹⁰*Ibid.*

²⁹¹*Ibid.*, para. 7.161.

²⁹²*Ibid.*, para. 7.177.

²⁹³*Ibid.*, para. 8.1(d).

B. *Interpretation of the Term "Non-Discriminatory" in Footnote 3 to Paragraph 2(a) of the Enabling Clause*

142. We proceed to interpret the term "non-discriminatory" as it appears in footnote 3 to paragraph 2(a) of the Enabling Clause.

143. We recall first that the Enabling Clause has become a part of the GATT 1994.²⁹⁴ Paragraph 1 of the Enabling Clause authorizes WTO Members to provide "differential and more favourable treatment to developing countries, without according such treatment to other WTO Members". As explained above, such differential treatment is permitted "notwithstanding" the provisions of Article I of the GATT 1994. Paragraph 2(a) and footnote 3 thereto clarify that paragraph 1 applies to "[p]referential tariff treatment accorded by developed contracting parties to products originating in developing countries in accordance with the Generalized System of Preferences"²⁹⁵, "[a]s described in the [1971 Waiver Decision], relating to the establishment of 'generalized, non-reciprocal and non-discriminatory preferences beneficial to the developing countries'".²⁹⁶

144. The Preamble to the 1971 Waiver Decision in turn refers to "preferential tariff treatment" in the following terms:

Recalling that at the Second UNCTAD, unanimous agreement was reached in favour of the early establishment of a mutually acceptable system of generalized, non-reciprocal and non-discriminatory preferences beneficial to the developing countries in order to increase the export earnings, to promote the industrialization, and to accelerate the rates of economic growth of these countries;

Considering that mutually acceptable arrangements have been drawn up in the UNCTAD concerning the establishment of generalized, non-discriminatory, non-reciprocal preferential tariff treatment in the markets of developed countries for products originating in developing countries.[²⁹⁷ (original italics; underlining added)

145. Paragraph 2(a) of the Enabling Clause provides, therefore, that, to be justified under that provision, preferential tariff treatment must be "in accordance" with the GSP "as described" in the *Preamble* to the 1971 Waiver Decision. "Accordance" being defined in the dictionary as

²⁹⁴See *supra*, footnote 192.

²⁹⁵Enabling Clause, para. 2(a) (attached as Annex 2 to this Report).

²⁹⁶*Ibid.*; footnote 3 to para. 2(a).

²⁹⁷1971 Waiver Decision, third and fourth recitals.

"conformity"²⁹⁸, only preferential tariff treatment that is in conformity with the description "generalized, non-reciprocal and non-discriminatory" treatment can be justified under paragraph 2(a).

146. In the light of the above, we do not agree with European Communities' assertion²⁹⁹ that the Panel's interpretation of the word "non-discriminatory" in footnote 3 of the Enabling Clause is erroneous because the phrase "generalized, non-reciprocal and non-discriminatory" in footnote 3 merely refers to the description of the GSP in the 1971 Waiver Decision and, of itself, does not impose any legal obligation on preference-granting countries. Nor do we agree with the United States that the Panel erred in "assum[ing]" that the term "non-discriminatory" in footnote 3 imposes obligations on preference-granting countries, and that, instead, footnote 3 "is simply a cross-reference to where the Generalized System of Preferences is described."³⁰⁰

147. We find support for our interpretation in the French version of paragraph 2(a) of the Enabling Clause, requiring that the tariff preferences be accorded "*conformément au Système généralisé de préférences*". The term "in accordance" is thus "*conformément*" in the French version. In addition, the phrase "[a]s described in [the 1971 Waiver Decision]" in footnote 3 is stated as "*[l]el qu'il est défini dans la décision des PARTIES CONTRACTANTES en date du 25 juin 1971*". Similarly, the Spanish version uses the terms "*conformidad*" and "*[l]al como lo define la Decisión de las PARTES CONTRATANTES de 25 de junio de 1971*". In our view, the stronger, more obligatory language in both the French and Spanish texts—that is, using "as defined in" rather than "as described in"—lends support to our view that only preferential tariff treatment that is "generalized, non-reciprocal and non-discriminatory" is covered under paragraph 2(a) of the Enabling Clause.³⁰¹

148. Having found that the qualification of the GSP as "generalized, non-reciprocal and non-discriminatory" imposes obligations that must be fulfilled for preferential tariff treatment to be justified under paragraph 2(a), we turn to address the Panel's finding that:

²⁹⁸*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 1, p. 15.

²⁹⁹European Communities' response to questioning at the oral hearing.

³⁰⁰United States' third participant's submission, para. 11.

³⁰¹We further note the existence of a 1999 WTO waiver allowing *developing* countries to grant special preferences to *least-developed* countries. (Waiver Decision on Preferential Tariff Treatment for Least-Developed Countries, WT/L/304, 15 June 1999 (the "1999 LDC Waiver")) That waiver applies only to "preferential tariff treatment ... provided on a generalized, non-reciprocal and non-discriminatory basis". (*Ibid.*, para. 2) As such, for tariff preferences to be justified thereunder, there is a *requirement* that the treatment be accorded on a "generalized, non-reciprocal and non-discriminatory basis" (emphasis added) We see no reason why *developed* countries would be permitted to provide preferential tariff treatment to developing countries under the Enabling Clause other than on a "non-discriminatory basis", when there is clearly a requirement for *developing* countries to provide such treatment to least-developed countries on a "non-discriminatory basis" under the 1999 LDC Waiver.

... the term "non-discriminatory" in footnote 3 requires that *identical* tariff preferences under GSP schemes be provided to *all* developing countries without differentiation, except for the implementation of a priori limitations.³⁰² (emphasis added)

149. The European Communities maintains that "non-discrimination" is not synonymous with formally equal treatment³⁰³ and that "[t]reating differently situations which are objectively different is not discriminatory."³⁰⁴ The European Communities asserts that "[t]he objective of the Enabling Clause is different from that of Article I:1 of the GATT."³⁰⁵ In its view, the latter is concerned with "providing equal conditions of competition for imports of like products originating in all Members", whereas "the Enabling Clause is a form of Special and Differential Treatment for developing countries, which seeks the opposite result: to create unequal competitive opportunities in order to respond to the special needs of developing countries."³⁰⁶ The European Communities derives contextual support from paragraph 3(c), which states that the treatment provided under the Enabling Clause "shall ... be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries." The European Communities concludes that the term "non-discriminatory" in footnote 3 "does not prevent the preference-giving countries from differentiating between developing countries which have different development needs, where tariff differentiation constitutes an adequate response to such differences."³⁰⁷

150. India, in contrast, asserts that "non-discrimination in respect of tariff measures refers to formally equal[] treatment"³⁰⁸ and that paragraph 2(a) of the Enabling Clause requires that "preferential tariff treatment [be] applied equally" among developing countries.³⁰⁹ In support of its argument, India submits that an interpretation of paragraph 2(a) of the Enabling Clause that authorizes developed countries to provide "discriminatory tariff treatment *in favour of the developing countries* but not *between the developing countries* gives full effect to both Article I of the GATT and paragraph 2(a) of the Enabling Clause and minimises the conflict between them."³¹⁰ India emphasizes that, by consenting to the adoption of the Enabling Clause, developing countries did not

³⁰²Panel Report, para. 7.161.

³⁰³European Communities' appellant's submission, para. 71.

³⁰⁴*Ibid.*

³⁰⁵*Ibid.*, para. 152.

³⁰⁶*Ibid.*

³⁰⁷*Ibid.*, para. 188.

³⁰⁸India's appellee's submission, para. 120.

³⁰⁹*Ibid.*, para. 106.

³¹⁰*Ibid.*, para. 92. (original italics)

"relinquish[] their MFN rights [under Article I of the GATT 1994] as between themselves, thus permitting developed countries to discriminate between them."³¹¹

151. We examine now the ordinary meaning of the term "non-discriminatory" in footnote 3 to paragraph 2(a) of the Enabling Clause. As we observed, footnote 3 requires that GSP schemes under the Enabling Clause be "generalized, non-reciprocal and non discriminatory". Before the Panel, the participants offered competing definitions of the word "discriminate". India suggested that this word means "to make or constitute a difference in or between; distinguish" and 'to make a distinction in the treatment of different categories of peoples or things.'³¹² The European Communities, however, understood this word to mean "to make a distinction in the treatment of different categories of people or things, esp. *unjustly or prejudicially* against people on grounds of race, colour, sex, social status, age, etc."³¹³

152. Both definitions can be considered as reflecting ordinary meanings of the term "discriminate"³¹⁴ and essentially exhaust the relevant ordinary meanings. The principal distinction between these definitions, as the Panel noted, is that India's conveys a "*neutral*" meaning of making a distinction", whereas the European Communities' conveys a "*negative*" meaning carrying the connotation of a distinction that is unjust or prejudicial."³¹⁵ Accordingly, the ordinary meanings of "discriminate" point in conflicting directions with respect to the propriety of according differential treatment. Under India's reading, any differential treatment of GSP beneficiaries would be prohibited, because such treatment necessarily makes a distinction between beneficiaries. In contrast, under the European Communities' reading, differential treatment of GSP beneficiaries would not be prohibited *per se*. Rather, distinctions would be impermissible only where the basis for such distinctions was improper. Given these divergent meanings, we do not regard the term "non-discriminatory", on its own, as determinative of the permissibility of a preference-granting country according different tariff preferences to different beneficiaries of its GSP scheme.

153. Nevertheless, at this stage of our analysis, we are able to discern some of the content of the "non-discrimination" obligation based on the ordinary meanings of that term. Whether the drawing of

³¹¹India's appellee's submission, para. 104.

³¹²Panel Report, para. 7.126 (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 1, p. 689).

³¹³*Ibid.* (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 1, p. 689). (italics added by the Panel)

³¹⁴See *Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 1, p. 697.

³¹⁵Panel Report, para. 7.126. (original italics)

distinctions is *per se* discriminatory, or whether it is discriminatory only if done on an improper basis, the ordinary meanings of "discriminate" converge in one important respect: they both suggest that distinguishing among similarly-situated beneficiaries is discriminatory. For example, India suggests that all beneficiaries of a particular Member's GSP scheme are similarly-situated, implicitly arguing that any differential treatment of such beneficiaries constitutes discrimination. The European Communities, however, appears to regard GSP beneficiaries as similarly-situated when they have "similar development needs".³¹⁶ Although the European Communities acknowledges that differentiating between similarly-situated GSP beneficiaries would be inconsistent with footnote 3 of the Enabling Clause, it submits that there is no inconsistency in differentiating between GSP beneficiaries with "different development needs".³¹⁷ Thus, based on the ordinary meanings of "discriminate", India and the European Communities effectively appear to agree that, pursuant to the term "non-discriminatory" in footnote 3, similarly-situated GSP beneficiaries should not be treated differently.³¹⁸ The participants disagree only as to the basis for determining whether beneficiaries are similarly-situated.

154. Paragraph 2(a), on its face, does not explicitly authorize or prohibit the granting of different tariff preferences to different GSP beneficiaries. It is clear from the ordinary meanings of "non-discriminatory", however, that preference-granting countries must make available identical tariff preferences to all similarly-situated beneficiaries.

155. We continue our interpretive analysis by turning to the immediate context of the term "non-discriminatory". We note first that footnote 3 to paragraph 2(a) stipulates that, in addition to being "non-discriminatory", tariff preferences provided under GSP schemes must be "generalized".

³¹⁶European Communities' appellant's submission, para. 175. (See also, *ibid.*, para. 186)

³¹⁷*Ibid.*, para. 188.

³¹⁸We note that the contrasting definitions proffered by the participants, as well as the convergence of those definitions on the fact that similarly-situated entities should not be treated differently, find reflection in the use of the term "discrimination" in general international law. In this respect, we note, as an example, the definitions of "discrimination" provided by the European Communities, in footnotes 56 and 57 of its appellant's submission:

56 ... Mere differences of treatment do not necessarily constitute discrimination ... discrimination may in general be said to arise where those who are in all material respects the same are treated differently, or where those who are in material respects different are treated in the same way.

(quoting R. Jennings and A. Watts (eds.), *Oppenheim's International Law*, 9th ed. (Longman, 1992), Vol. I, p. 378)

57 ... Discrimination occurs when in a legal system an inequality is introduced in the enjoyment of a certain right, or in a duty, while there is no sufficient connection between the inequality upon which the legal inequality is based, and the right or the duty in which this inequality is made.

(quoting E. W. Vierdag, *The Concept of Discrimination in International Law*, (Martinus Nijhoff, 1973), p. 61)

According to the ordinary meaning of that term, tariff preferences provided under GSP schemes must be "generalized" in the sense that they "apply more generally; [or] become extended in application".³¹⁹ However, this ordinary meaning alone may not reflect the entire significance of the word "generalized" in the context of footnote 3 of the Enabling Clause, particularly because that word resulted from lengthy negotiations leading to the GSP. In this regard, we note the Panel's finding that, by requiring tariff preferences under the GSP to be "generalized", developed and developing countries together sought to eliminate existing "special" preferences that were granted only to certain designated developing countries.³²⁰ Similarly, in response to our questioning at the oral hearing, the participants agreed that one of the objectives of the 1971 Waiver Decision and the Enabling Clause was to eliminate the fragmented system of special preferences³²¹ that were, in general, based on historical and political ties between developed countries and their former colonies.

156. It does not necessarily follow, however, that "non-discriminatory" should be interpreted to require that preference-granting countries provide "identical" tariff preferences under GSP schemes to "all" developing countries. In concluding otherwise, the Panel assumed that allowing tariff preferences such as the Drug Arrangements would necessarily "result [in] the collapse of the whole GSP system and a return back to special preferences favouring selected developing countries".³²² To us, this conclusion is unwarranted. We observe that the term "generalized" requires that the GSP schemes of preference-granting countries remain generally applicable.³²³ Moreover, unlike the Panel, we believe that the Enabling Clause sets out sufficient conditions on the granting of preferences to protect against such an outcome. As we discuss below³²⁴, provisions such as paragraphs 3(a) and

³¹⁹*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 1, p. 1082.

³²⁰Panel Report, paras. 7.135-7.137. The Panel also observed that statements by developed and developing countries indicated the aim of providing GSP schemes with a broad scope, encompassing the granting of preferences by *all* developed countries to *all* developing countries. (*Ibid.*, paras. 7.131-7.132)

³²¹See also European Communities' appellant's submission, para. 175.

³²²Panel Report, para. 7.102.

³²³The European Communities argues in this respect that the GATT Contracting Parties and the WTO Members have granted a number of waivers, as mentioned in the Panel Report, for tariff preferences that are "confined *ab initio* and permanently to a limited number of developing countries located in a certain geographical region". (European Communities' appellant's submission, paras. 184-185 (referring to Panel Report, para. 7.160)) See also, Panel Report, footnote 31 to para. 4.32 (referring to Waiver Decision on the Caribbean Basin Economic Recovery Act, GATT Document L/5779, 15 February 1985; BISD 31S/20, renewed 15 November 1995, WT/L/104; Waiver Decision on CARIBCAN, GATT Document L/6102, 28 November 1986, BISD 33S/97, renewed 14 October 1996, WT/L/185; Waiver Decision on the United States – Andean Trade Preference Act, GATT Document L/6991, 19 March 1992, BISD 39S/385, renewed 14 October 1996, WT/L/184; Waiver Decision on The Fourth ACP-EEC Convention of Lomé, GATT Document L/7604, 9 December 1994, BISD 41S/26, renewed 14 October 1996, WT/L/186; and Waiver Decision on European Communities – The ACP-EC Partnership Agreement, WT/MIN (01)/15, 14 November 2001.

³²⁴*Infra*, paras. 157-168.

3(c) of the Enabling Clause impose specific conditions on the granting of different tariff preferences among GSP beneficiaries.

157. As further context for the term "non-discriminatory" in footnote 3, we turn next to paragraph 3(c) of the Enabling Clause, which specifies that "differential and more favourable treatment" provided under the Enabling Clause:

... shall in the case of such treatment accorded by developed contracting parties to developing countries be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries.

158. At the outset, we note that the use of the word "shall" in paragraph 3(c) suggests that paragraph 3(c) sets out an obligation for developed-country Members in providing preferential treatment under a GSP scheme to "respond positively" to the "needs of developing countries".³²⁵ Having said this, we turn to consider whether the "development, financial and trade needs of developing countries" to which preference-granting countries are required to respond when granting preferences must be understood to cover the "needs" of developing countries *collectively*.

159. The Panel found that "the only appropriate way [under paragraph 3(c) of the Enabling Clause] of responding to the differing development needs of developing countries is for preference-giving countries to ensure that their [GSP] schemes have sufficient breadth of product coverage and depth of tariff cuts to respond positively to those differing needs."³²⁶ In reaching this conclusion, the Panel appears to have placed a great deal of significance on the fact that paragraph 3(c) does not refer to needs of "*individual*" developing countries.³²⁷ The Panel thus understood that paragraph 3(c) does not permit the granting of preferential tariff treatment exclusively to a sub-category of developing countries on the basis of needs that are common to or shared by only those developing countries. We see no basis for such a conclusion in the text of paragraph 3(c). Paragraph 3(c) refers generally to "the development, financial and trade needs of developing countries". The absence of an explicit requirement in the text of paragraph 3(c)³²⁸ to respond to the needs of "all" developing countries, or

³²⁵We note that the European Communities agreed before the Panel that paragraph 3(c) of the Enabling Clause sets forth a "requirement". (European Communities' first written submission to the Panel, paras. 7.1 and 1.49)

³²⁶Panel Report, para. 7.149. (See also, *ibid.*, paras. 7.95-7.97 and 7.105)

³²⁷*Ibid.*, para. 7.78.

³²⁸The United States refers to Article 3.2 of the DSU to support its argument that "panels are barred from reading legal obligations into the Enabling Clause that are not found in the text." (United States' third participant's submission, para. 13)

to the needs of "each and every"³²⁹ developing country, suggests to us that, in fact, that provision imposes no such obligation.³³⁰

160. Furthermore, as we understand it, the participants in this case agree that developing countries may have "development, financial and trade needs" that are subject to change and that certain development needs may be common to only a certain number of developing countries.³³¹ We see no reason to disagree. Indeed, paragraph 3(c) contemplates that "differential and more favourable treatment"³³² accorded by developed to developing countries may need to be "modified" in order to "respond positively" to the needs of developing countries. Paragraph 7 of the Enabling Clause supports this view by recording the expectation of "less-developed contracting parties" that their capacity to make contributions or concessions under the GATT will "improve with the progressive development of their economies and improvement in their trade situation". Moreover, the very purpose of the special and differential treatment permitted under the Enabling Clause is to foster economic development of developing countries. It is simply unrealistic to assume that such development will be in lockstep for all developing countries at once, now and for the future.

161. In addition, the Preamble to the *WTO Agreement*, which informs all the covered agreements including the GATT 1994 (and, hence, the Enabling Clause), explicitly recognizes the "need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development".³³³ The word "commensurate" in this phrase appears to leave open the possibility that developing countries may have different needs according to their levels of development and particular circumstances. The Preamble to the *WTO Agreement* further recognizes

³²⁹Panel Report, para. 7.105. (italics omitted)

³³⁰In this respect, we agree with the European Communities that paragraph 3(c) should "be interpreted in a manner which, while preserving its relevance, is both workable for developed countries and consistent with the requirements that the preferences be *non-discriminatory*." (European Communities' appellant's submission, para. 138 (original italics))

³³¹The European Communities emphasized before the Panel that the "development, financial and trade needs of developing countries" referred to in paragraph 3(c) of the Enabling Clause "[o]bviously ... may vary between different categories of developing countries, as well as over time" (European Communities' first written submission to the Panel, para. 71) That "needs of developing countries" may change over time was also acknowledged by India in response to our questioning at the oral hearing. In addition, we understand India not to disagree that developing countries may have different individual needs, given that it argues that paragraph 3(c) should be interpreted as requiring "GSP schemes [to] respond to the needs of developing countries as a whole and not their individual needs." (India's appellee's submission, para. 124)

³³²Enabling Clause, para. 1 (attached as Annex 2 to this Report).

³³³*WTO Agreement*, Preamble, second recital.

that Members' "respective needs and concerns at different levels of economic development"³³⁴ may vary according to the different stages of development of different Members.

162. In sum, we read paragraph 3(c) as authorizing preference-granting countries to "respond positively" to "needs" that are *not* necessarily common or shared by all developing countries. Responding to the "needs of developing countries" may thus entail treating different developing-country beneficiaries differently.

163. However, paragraph 3(c) does not authorize *any* kind of response to *any* claimed need of developing countries. First, we observe that the types of needs to which a response is envisaged are limited to "development, financial and trade needs". In our view, a "need" cannot be characterized as one of the specified "needs of developing countries" in the sense of paragraph 3(c) based merely on an assertion to that effect by, for instance, a preference-granting country or a beneficiary country. Rather, when a claim of inconsistency with paragraph 3(c) is made, the existence of a "development, financial [or] trade need" must be assessed according to an *objective* standard. Broad-based recognition of a particular need, set out in the *WTO Agreement* or in multilateral instruments adopted by international organizations, could serve as such a standard.³³⁵

164. Secondly, paragraph 3(c) mandates that the response provided to the needs of developing countries be "positive". "Positive" is defined as "consisting in or characterized by constructive action or attitudes".³³⁶ This suggests that the response of a preference-granting country must be taken with a view to *improving* the development, financial or trade situation of a beneficiary country, based on the particular need at issue. As such, in our view, the expectation that developed countries will "respond positively" to the "needs of developing countries" suggests that a sufficient nexus should exist between, on the one hand, the preferential treatment provided under the respective measure authorized by paragraph 2, and, on the other hand, the likelihood of alleviating the relevant "development, financial [or] trade need". In the context of a GSP scheme, the particular need at issue must, by its nature, be such that it can be effectively addressed through tariff preferences. Therefore, only if a preference-granting country acts in the "positive" manner suggested, in "respon[se]" to a

³³⁴*WTO Agreement*, Preamble, first recital.

³³⁵The European Communities argues that tariff preferences are an appropriate response to the drug problem. In support of its argument, the European Communities refers to the Preamble to the *Agreement on Agriculture* and the waiver for the United States' Andean Trade Preference Act. In addition, the European Communities finds support in several international conventions and resolutions that have recognized drug production and drug trafficking as entailing particular problems for developing countries. (See Panel Report, paras. 4.71-4.74; and European Communities' appellant's submission, paras. 144-149)

³³⁶*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 2, p. 2293.

widely-recognized "development, financial [or] trade need", can such action satisfy the requirements of paragraph 3(c).

165. Accordingly, we are of the view that, by requiring developed countries to "respond positively" to the "needs of developing countries", which are varied and not homogeneous, paragraph 3(c) indicates that a GSP scheme may be "non-discriminatory" even if "identical" tariff treatment is not accorded to "all" GSP beneficiaries. Moreover, paragraph 3(c) suggests that tariff preferences under GSP schemes may be "non-discriminatory" when the relevant tariff preferences are addressed to a particular "development, financial [or] trade need" and are made available to all beneficiaries that share that need.

166. India submits that developing countries should not be presumed to have waived their MFN rights under Article I:1 of the GATT 1994 *vis-à-vis* other developing countries³³⁷, and we make no such presumption. In fact, we note that the Enabling Clause *specifically* allows developed countries to provide differential and more favourable treatment to developing countries "notwithstanding" the provisions of Article I.³³⁸ With this in mind, and given that paragraph 3(c) of the Enabling Clause contemplates, in certain circumstances, differentiation among GSP beneficiaries, we cannot agree with India that the right to MFN treatment can be invoked by a GSP beneficiary *vis-à-vis* other GSP beneficiaries in the context of GSP schemes that meet the conditions set out in the Enabling Clause.

167. Finally, we note that, pursuant to paragraph 3(a) of the Enabling Clause, any "differential and more favourable treatment ... shall be designed to facilitate and promote the trade of developing countries and not to raise barriers to or create undue difficulties for the trade of any other contracting parties." This requirement applies, *a fortiori*, to any preferential treatment granted to one GSP beneficiary that is not granted to another.³³⁹ Thus, although paragraph 2(a) does not prohibit *per se* the granting of different tariff preferences to different GSP beneficiaries³⁴⁰, and paragraph 3(c) even contemplates such differentiation under certain circumstances³⁴¹, paragraph 3(a) requires that any positive response of a preference-granting country to the varying needs of developing countries not impose unjustifiable burdens on other Members.

³³⁷India's appellee's submission, para. 94.

³³⁸Compare para. 1 of the Enabling Clause ("Notwithstanding the provisions of Article I") with para. (a) of the 1971 Waiver Decision ("the provisions of Article I shall be waived ... to the extent necessary").

³³⁹We note in this respect that the language contained in paragraph 3(a) of the Enabling Clause is reflected in waivers referred to in *supra*, footnote 323.

³⁴⁰*Supra*, paras. 153-154.

³⁴¹*Supra*, paras. 162-165.

168. Having examined the context of paragraph 2(a), we turn next to examine the object and purpose of the *WTO Agreement*. We note first that paragraph 7 of the Enabling Clause provides that "[t]he concessions and contributions made and the obligations assumed by developed and less-developed contracting parties under the provisions of the [GATT 1994] should promote the basic objectives of the [GATT 1994], including those embodied in the Preamble". As we have observed, the Preamble to the *WTO Agreement* provides that there is "need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development".³⁴² Similarly, the Preamble to the 1971 Waiver Decision provides that "a principal aim of the CONTRACTING PARTIES is promotion of the trade and export earnings of developing countries for the furtherance of their economic development".³⁴³ These objectives are also reflected in paragraph 3(c) of the Enabling Clause, which states that the treatment provided under the Enabling Clause "shall ... be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries".

169. Although enhanced market access will contribute to responding to the needs of developing countries *collectively*, we have also recognized that the needs of developing countries may vary over time. We are of the view that the objective of improving developing countries' "share in the growth in international trade", and their "trade and export earnings", can be fulfilled by promoting preferential policies aimed at those interests that developing countries have in common, *as well as* at those interests shared by sub-categories of developing countries based on their particular needs. An interpretation of "non-discriminatory" that does not require the granting of "identical tariff preferences"³⁴⁴ allows not only for GSP schemes providing preferential market access to all beneficiaries, but also the possibility of additional preferences for developing countries with particular needs, provided that such additional preferences are not inconsistent with other provisions of the Enabling Clause, including the requirements that such preferences be "generalized" and "non-reciprocal". We therefore consider such an interpretation to be consistent with the object and purpose of the *WTO Agreement* and the Enabling Clause.

170. The Panel took the view, however, that the objective of "elimination of discriminatory treatment in international commerce"³⁴⁵, found in the Preamble to the GATT 1994, "contributes more

³⁴²*WTO Agreement*, Preamble, second recital.

³⁴³1971 Waiver Decision, Preamble, first recital.

³⁴⁴Panel Report, para. 7.161.

³⁴⁵*Ibid.*, para. 7.157 (quoting GATT 1994, Preamble, second recital).

to guiding the interpretation of 'non-discriminatory'"³⁴⁶ than does the objective of ensuring that developing countries "secure ... a share in the growth in international trade commensurate with their development needs."³⁴⁷ We fail to see on what basis the Panel drew this conclusion.

171. We next examine the relevance of paragraph 2(d) of the Enabling Clause³⁴⁸ for the interpretation of "non-discriminatory" in footnote 3. The Panel characterized paragraph 2(d) as an "exception" to paragraph 2(a)³⁴⁹ and relied on paragraph 2(d) to support its view that paragraph 2(a) requires "formally identical treatment".³⁵⁰ In the Panel's view, if developed-country Members were entitled under paragraph 2(a) to differentiate between developing-country Members, then they would have been entitled under that paragraph alone to differentiate between developing and least-developed countries. Accordingly, "there would have been no need to include paragraph 2(d) in the Enabling Clause."³⁵¹

172. We do not agree with the Panel that paragraph 2(d) is an "exception" to paragraph 2(a), or that it is rendered redundant if paragraph 2(a) is interpreted as allowing developed countries to differentiate in their GSP schemes between developing countries. To begin with, we note that the terms of paragraph 2 do not expressly indicate that each of the four sub-paragraphs thereunder is mutually exclusive, or that any one is an exception to any other. Moreover, in our view, it is clear from several provisions of the Enabling Clause that the drafters wished to emphasize that least-developed countries form an identifiable sub-category of developing countries with "special economic difficulties and ... particular development, financial and trade needs".³⁵² When a developed-country Member grants tariff preferences in favour of developing countries under paragraph 2(a), as we have already found³⁵³, footnote 3 imposes a requirement that such preferences be "non-discriminatory". In the absence of paragraph 2(d), a Member granting preferential tariff treatment only to least-developed countries would therefore need to establish, under paragraph 2(a), that this preferential treatment did not "discriminate" against other developing countries contrary to footnote 3. The inclusion of paragraph 2(d), however, makes clear that developed countries may accord preferential treatment to

³⁴⁶Panel Report, paras. 7.157-7.158.

³⁴⁷*Ibid.*, para. 7.155 (referring to *WTO Agreement*, Preamble, second recital).

³⁴⁸Paragraph 2(d) deals with special treatment of least-developed countries "in the context of any general or specific measures in favour of developing countries".

³⁴⁹Panel Report, para. 7.147.

³⁵⁰*Ibid.*, para. 7.145.

³⁵¹*Ibid.*, para. 7.145.

³⁵²Enabling Clause, para. 6 (attached as Annex 2 to this Report). Similarly, paragraph 8 of the Enabling Clause refers to the "special economic situation and [the] development, financial and trade needs" of least-developed countries.

³⁵³*Supra*, paras. 145-148.

least-developed countries distinct from the preferences granted to other developing countries under paragraph 2(a). Thus, pursuant to paragraph 2(d), preference-granting countries need not establish that differentiating between developing and least-developed countries is "non-discriminatory". This demonstrates that paragraph 2(d) does have an effect that is different and independent from that of paragraph 2(a), even if the term "non-discriminatory" does not require the granting of "identical tariff preferences"³⁵⁴ to all GSP beneficiaries.

173. Having examined the text and context of footnote 3 to paragraph 2(a) of the Enabling Clause, and the object and purpose of the *WTO Agreement* and the Enabling Clause, we conclude that the term "non-discriminatory" in footnote 3 does not prohibit developed-country Members from granting different tariffs to products originating in different GSP beneficiaries, provided that such differential tariff treatment meets the remaining conditions in the Enabling Clause. In granting such differential tariff treatment, however, preference-granting countries are required, by virtue of the term "non-discriminatory", to ensure that identical treatment is available to all similarly-situated GSP beneficiaries, that is, to all GSP beneficiaries that have the "development, financial and trade needs" to which the treatment in question is intended to respond.

174. For all of these reasons, we *reverse* the Panel's finding, in paragraphs 7.161 and 7.176 of the Panel Report, that "the term 'non-discriminatory' in footnote 3 [to paragraph 2(a) of the Enabling Clause] requires that identical tariff preferences under GSP schemes be provided to all developing countries without differentiation, except for the implementation of a priori limitations."³⁵⁵

C. *The Words "Developing Countries" in Paragraph 2(a) of the Enabling Clause*

175. In addition to the Panel's interpretation of the term "non-discriminatory" in footnote 3 of the Enabling Clause, the European Communities appeals the Panel's finding that "the term 'developing countries' in paragraph 2(a) should be interpreted to mean *all* developing countries, [except as regards] *a priori* limitations".³⁵⁶ The Panel's interpretation of paragraph 2(a) is premised on its findings that (i) footnote 3 permits the granting of different tariff preferences to different GSP beneficiaries *only* for the purpose of *a priori* limitations³⁵⁷, and (ii) paragraph 3(c) permits the granting of different tariff preferences to different GSP beneficiaries *only* for the purposes of

³⁵⁴Panel Report, para. 7.161.

³⁵⁵Given our interpretation, which permits differentiation among GSP beneficiaries, it is not necessary for us to rule on whether *a priori* limitations are permitted under the Enabling Clause. (See also, *supra*, paras. 128-129)

³⁵⁶Panel Report, para. 7.174. (original italics) See also, European Communities' appellant's submission, para. 67.

³⁵⁷Panel Report, para. 7.170.

a priori limitations and preferential treatment in favour of least-developed countries.³⁵⁸ We have concluded, contrary to the Panel, that footnote 3 and paragraph 3(c) do *not* preclude the granting of differential tariffs to different sub-categories of GSP beneficiaries, subject to compliance with the remaining conditions of the Enabling Clause. We find, therefore, that the term "developing countries" in paragraph 2(a) should not be read to mean "all" developing countries and, accordingly, that paragraph 2(a) does not prohibit preference-granting countries from according different tariff preferences to different sub-categories of GSP beneficiaries.

176. Accordingly, we also *reverse* the Panel's finding, in paragraph 7.174 of the Panel Report, that "the term 'developing countries' in paragraph 2(a) [of the Enabling Clause] should be interpreted to mean *all* developing countries, with the exception that where developed countries are implementing a priori limitations, 'developing countries' may mean *less than all* developing countries."

D. *Consistency of the Drug Arrangements with the Enabling Clause*

177. We turn next to examine the consistency of the Drug Arrangements with the Enabling Clause.

178. We recall that, with respect to the Enabling Clause, the only challenge by India before the Panel related to paragraph 2(a) and, in particular, footnote 3 thereto.³⁵⁹ In response, the European Communities argued that it found contextual support for its interpretation of paragraph 2(a) in the requirement, contained in paragraph 3(c), to respond positively to the needs of developing countries.³⁶⁰ In rejecting the European Communities' interpretation of paragraph 2(a), the Panel did not determine whether the Drug Arrangements satisfy the conditions set out in paragraph 3(c), but, rather, limited its discussion of paragraph 3(c) to the relevance of that provision as context for its interpretation of paragraph 2(a). Thus, the Panel made a finding of inconsistency only with respect to paragraph 2(a) of the Enabling Clause.³⁶¹ The European Communities appeals this finding of inconsistency with paragraph 2(a).

179. Although paragraph 3(c) informs the interpretation of the term "non-discriminatory" in footnote 3 to paragraph 2(a), as detailed above³⁶², paragraph 3(c) imposes requirements that are

³⁵⁸Panel Report, para. 7.171.

³⁵⁹*Supra*, paras. 120-122.

³⁶⁰See Panel Report, para. 7.123; European Communities' first written submission to the Panel, paras. 70-71 and 149; and European Communities' second written submission to the Panel, paras. 48-52.

³⁶¹Panel Report, para. 8.1(d).

³⁶²*Supra*, paras. 157-162.

according to which a beneficiary could be *removed* specifically from the Drug Arrangements on the basis that it is no longer "similarly affected by the drug problem". Indeed, Article 25.3 expressly states that the evaluation of the effects of the Drug Arrangements described in Articles 25.1(b) and 25.2 "will be without prejudice to the continuation of the [Drug Arrangements] until 2004, and their possible extension thereafter." This implies that, even if the European Commission found that the Drug Arrangements were having no effect whatsoever on a beneficiary's "efforts in combating drug production and trafficking",³⁷⁴ or that a beneficiary was no longer suffering from the drug problem, beneficiary status would continue.³⁷⁵ Therefore, even if the Regulation allowed for the list of beneficiaries under the Drug Arrangements to be modified, the Regulation itself gives no indication as to how the beneficiaries under the Drug Arrangements were chosen or what kind of considerations would or could be used to determine the effect of the "drug problem" on a particular country. In addition, we note that the Regulation does not, for instance, provide any indication as to how the European Communities would assess whether the Drug Arrangements provide an "adequate and proportionate response"³⁷⁶ to the needs of developing countries suffering from the drug problem.

184. It is true that a country may be removed as a beneficiary under Annex I, either altogether or in respect of certain product sectors, for reasons that are not specific to the Drug Arrangements. Thus, Article 3 of the Regulation provides for the removal of a country from Annex I (and hence, from the General Arrangements and any other arrangements under which it is a beneficiary) if particular circumstances are met indicating that the country has reached a certain level of development. Article 12 provides for the removal of a country as a beneficiary under the General Arrangements and the Drug Arrangements with respect to a product sector where the country's level of development and competition has reached a certain threshold with respect to that sector. Neither Article 3 nor Article 12 appears to relate in any way to the degree to which the country is suffering from the "drug problem". Finally, Title V to the Regulation contains certain "Temporary Withdrawal and Safeguard Provisions" that are common to all the preferential arrangements under the Regulation. Although one reason for which the arrangements may be temporarily withdrawn is "shortcomings in customs controls on export or transit of drugs (illicit substances or precursors), or failure to comply with international conventions on money laundering",³⁷⁷ this reason applies equally to the General Arrangements, the Drug Arrangements, and the other special incentive arrangements. Moreover, as

³⁷⁴Regulation, Art. 25.1(b).

³⁷⁵In response to questioning at the oral hearing, the European Communities confirmed that, although the sixth recital to the Preamble of the Regulation provides that the Drug Arrangements "should be closely monitored", the list of beneficiaries will be unaffected by the monitoring described in Articles 25.1 and 25.2 of the Regulation.

³⁷⁶European Communities' appellant's submission, para. 133.

³⁷⁷Regulation, Art. 26.1(d).

the Panel appeared to recognize, this condition is not connected to the question of whether the beneficiary is a "seriously drug-affected country".³⁷⁸

185. We note, moreover, that the Drug Arrangements will be in effect until 31 December 2004.³⁷⁹ Until that time, other developing countries that are "similarly affected by the drug problem" can be included as beneficiaries under the Drug Arrangements only through an amendment to the Regulation. The European Communities confirmed this understanding in response to questioning at the oral hearing.

186. Against this background, we fail to see how the Drug Arrangements can be distinguished from other schemes that the European Communities describes as "confined *ab initio* and permanently to a limited number of developing countries".³⁸⁰ As we understand it, the European Communities' position is that such schemes would be discriminatory, whereas the Drug Arrangements are not because "all developing countries are potentially beneficiaries" thereof.³⁸¹ In seeking a waiver from its obligations under Article I:1 of the GATT 1994 to implement the Drug Arrangements, the European Communities explicitly acknowledged, however, that "[b]ecause the special arrangements are *only available* to imports originating in [the 12 beneficiaries of the Drug Arrangements], a waiver ... appears necessary".³⁸² This statement appears to undermine the European Communities' argument that "all developing countries are potentially beneficiaries of the Drug Arrangements" and, therefore, that the Drug Arrangements are "non-discriminatory".³⁸³

187. We recall our conclusion that the term "non-discriminatory" in footnote 3 of the Enabling Clause requires that identical tariff treatment be available to all similarly-situated GSP beneficiaries. We find that the measure at issue fails to meet this requirement for the following reasons. First, as the European Communities itself acknowledges, according to benefits under the Drug Arrangements to countries other than the 12 identified beneficiaries would require an amendment to the Regulation.

³⁷⁸Panel Report, para. 7.216.

³⁷⁹Regulation, Arts. 1.1 and 41.2. We understand that the Regulation has been extended to 31 December 2005. (Council Regulation (EC) No. 2211/2003 of 15 December 2003 amending Regulation (EC) No. 2501/2001 applying a scheme of generalised tariff preferences for the period from 1 January 2002 to 31 December 2004 and extending it to 31 December 2005, *Official Journal of the European Union*, L Series, No. 332 (19 December 2003), p. 1)

³⁸⁰European Communities' appellant's submission, para. 185.

³⁸¹*Ibid.*, para. 186.

³⁸²Council for Trade in Goods, Request for a WTO Waiver, *New EC Special Tariff Arrangements to Combat Drug Production and Trafficking*, G/C/W/328, 24 October 2001, p. 2. (emphasis added)

³⁸³European Communities' appellant's submission, para. 186.

Such a "closed list" of beneficiaries cannot ensure that the preferences under the Drug Arrangements are available to all GSP beneficiaries suffering from illicit drug production and trafficking.

188. Secondly, the Regulation contains no criteria or standards to provide a basis for distinguishing beneficiaries under the Drug Arrangements from other GSP beneficiaries. Nor did the European Communities point to any such criteria or standards anywhere else, despite the Panel's request to do so.³⁸⁴ As such, the European Communities cannot justify the Regulation under paragraph 2(a), because it does not provide a basis for establishing whether or not a developing country qualifies for preferences under the Drug Arrangements. Thus, although the European Communities claims that the Drug Arrangements are available to all developing countries that are "similarly affected by the drug problem"³⁸⁵, because the Regulation does not define the criteria or standards that a developing country must meet to qualify for preferences under the Drug Arrangements, there is no basis to determine whether those criteria or standards are discriminatory or not.

189. For all these reasons, we find that the European Communities has failed to prove that the Drug Arrangements meet the requirement in footnote 3 that they be "non-discriminatory". Accordingly, we *uphold*, for different reasons, the Panel's conclusion, in paragraph 8.1(d) of the Panel Report, that the European Communities "failed to demonstrate that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause".

VI. Findings and Conclusions

190. For the reasons set out in this Report, the Appellate Body:

- (a) upholds the Panel's finding, in paragraph 7.53 of the Panel Report, that the Enabling Clause is an "exception" to Article I:1 of the GATT 1994;
- (b) upholds the Panel's finding, in paragraph 7.53 of the Panel Report, that the Enabling Clause "does not exclude the applicability" of Article I:1 of the GATT 1994;
- (c) modifies the Panel's finding, in paragraph 7.53 of the Panel Report, that the European Communities "bears the burden of invoking the Enabling Clause and justifying its Drug Arrangements" under that Clause, by finding that it was incumbent upon India to *raise* the Enabling Clause in making its claim of inconsistency with Article I:1 of the GATT 1994, but that the European Communities bore the burden of *proving* that

the Drug Arrangements satisfy the conditions of the Enabling Clause, in order to justify those Arrangements under that Clause; and finds, further, that India sufficiently raised paragraph 2(a) of the Enabling Clause in making its claim of inconsistency with Article I:1 before the Panel;

- (d) need not rule on the Panel's conclusion, in paragraphs 7.60 and 8.1(b) of the Panel Report, that the Drug Arrangements are inconsistent with Article I:1 of the GATT 1994;
- (e) reverses the Panel's finding, in paragraphs 7.161 and 7.176 of the Panel Report, that "the term 'non-discriminatory' in footnote 3 [to paragraph 2(a) of the Enabling Clause] requires that identical tariff preferences under GSP schemes be provided to all developing countries without differentiation, except for the implementation of a priori limitations";
- (f) reverses the Panel's finding, in paragraph 7.174 of the Panel Report, that "the term 'developing countries' in paragraph 2(a) [of the Enabling Clause] should be interpreted to mean *all* developing countries, with the exception that where developed countries are implementing a priori limitations, 'developing countries' may mean *less than all* developing countries"; and
- (g) upholds, for different reasons, the Panel's conclusion, in paragraph 8.1(d) of the Panel Report, that the European Communities "failed to demonstrate that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause".

191. The Appellate Body therefore recommends that the Dispute Settlement Body request the European Communities to bring Council Regulation (EC) No. 2501/2001, found in this Report, and in the Panel Report as modified by this Report, to be inconsistent with Article I:1 of the GATT 1994 and not justified under paragraph 2(a) of the Enabling Clause, into conformity with its obligations under the GATT 1994.

³⁸⁴See *supra*, footnote 372.

³⁸⁵European Communities' appellant's submission, para. 186.

Signed in the original at Geneva this 18th day of March 2004 by:

ANNEX 1

**WORLD TRADE
ORGANIZATION**

WT/DS246/7
8 January 2004

(04-0070)

Original: English

**EUROPEAN COMMUNITIES – CONDITIONS FOR THE GRANTING OF
TARIFF PREFERENCES TO DEVELOPING COUNTRIES**

Georges Abi-Saab
Presiding Member

Notification of an Appeal by the European Communities under paragraph 4 of Article 16 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU")

The following notification, dated 8 January 2004, from the Permanent Delegation of the European Commission, is being circulated to Members.

Luiz Olavo Baptista
Member

Giorgio Sacerdoti
Member

Pursuant to Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 20 of the Working Procedures for Appellate Review, the European Communities hereby notifies its decision to appeal to the Appellate Body certain issues of law covered in the report of the panel established in response to the request from India in the dispute *European Communities – Conditions for the Granting of Tariff Preferences to Developing Countries* (WT/DS246R).

The European Communities seeks review of the Panel's legal conclusion that the Special Arrangements to Combat Drug Production and Trafficking provided in Council Regulation (EC) No. 2501/2001 (the "Drug Arrangements") are inconsistent with Article I:1 of the *General Agreement on Tariff and Trade 1994* (the "GATT"). This conclusion is based on the following erroneous legal findings:

- that the Enabling Clause is an "exception" to Article I:1 of the GATT;
- that the Enabling Clause does not exclude the applicability of Article I:1 of the GATT;
- that the EC had the burden of proving that the Drug Arrangements were consistent with the Enabling Clause.

The above legal conclusion, and the related legal findings and interpretations are set out in paragraphs 7.31 to 7.60 and 8.1 (b) and (c) of the Panel report.

India did not make any claims under the Enabling Clause and, therefore, the Appellate Body should refrain from examining the consistency of the Drug Arrangements with the Enabling Clause. However, if the Appellate Body were to uphold the Panel's conclusion that the Drug Arrangements are inconsistent with Article I:1 of the GATT, or if the Appellate Body were to decide that India made a valid claim under the Enabling Clause, the European Communities appeals subsidiarily the Panel's

legal conclusion that the European Communities "failed to demonstrate that the Drug Arrangements are justified under paragraph 2(a) of the Enabling Clause". That conclusion is based on the following erroneous legal findings:

- that "the term "non-discriminatory" in footnote 3 to Paragraph 2(a) requires that identical tariff preferences under GSP schemes be provided to all developing countries without differentiation, except for the implementation of a priori limitations"; and
 - that the term "developing countries" in Paragraph 2(a) means all developing countries.
- This legal conclusion and the related legal findings and interpretations are set out in paragraphs 7.61-7.177 and 8.1(d) of the Panel report.

Finally the EC seeks review of the Panel's legal conclusion that the European Communities has nullified or impaired benefits accrued to India under GATT 1994, which is set out in paragraph 8.1(f) of the Panel report

ANNEX 2

DIFFERENTIAL AND MORE FAVOURABLE TREATMENT RECIPROCIITY AND FULLER PARTICIPATION OF DEVELOPING COUNTRIES

*Decision of 28 November 1979
(L/4903)*

Following negotiations within the framework of the Multilateral Trade Negotiations, the CONTRACTING PARTIES *decide* as follows:

1. Notwithstanding the provisions of Article I of the General Agreement, contracting parties may accord differential and more favourable treatment to developing countries¹, without according such treatment to other contracting parties.
2. The provisions of paragraph 1 apply to the following:²
 - (a) Preferential tariff treatment accorded by developed contracting parties to products originating in developing countries in accordance with the Generalized System of Preferences,³
 - (b) Differential and more favourable treatment with respect to the provisions of the General Agreement concerning non-tariff measures governed by the provisions of instruments multilaterally negotiated under the auspices of the GATT;
 - (c) Regional or global arrangements entered into amongst less-developed contracting parties for the mutual reduction or elimination of tariffs and, in accordance with criteria or conditions which may be prescribed by the CONTRACTING PARTIES, for the mutual reduction or elimination of non-tariff measures, on products imported from one another
 - (d) Special treatment of the least developed among the developing countries in the context of any general or specific measures in favour of developing countries.
3. Any differential and more favourable treatment provided under this clause:
 - (a) shall be designed to facilitate and promote the trade of developing countries and not to raise barriers to or create undue difficulties for the trade of any other contracting parties;
 - (b) shall not constitute an impediment to the reduction or elimination of tariffs and other restrictions to trade on a most-favoured-nation basis;

¹ The words "developing countries" as used in this text are to be understood to refer also to developing territories.

² It would remain open for the CONTRACTING PARTIES to consider on an *ad hoc* basis under the GATT provisions for joint action any proposals for differential and more favourable treatment not falling within the scope of this paragraph.

³ As described in the Decision of the CONTRACTING PARTIES of 25 June 1971, relating to the establishment of "generalized, non-reciprocal and non discriminatory preferences beneficial to the developing countries" (BISD 18S/24).

(c) shall in the case of such treatment accorded by developed contracting parties to developing countries be designed and, if necessary, modified, to respond positively to the development, financial and trade needs of developing countries.

4. Any contracting party taking action to introduce an arrangement pursuant to paragraphs 1, 2 and 3 above or subsequently taking action to introduce modification or withdrawal of the differential and more favourable treatment so provided shall:⁴

(a) notify the CONTRACTING PARTIES and furnish them with all the information they may deem appropriate relating to such action;

(b) afford adequate opportunity for prompt consultations at the request of any interested contracting party with respect to any difficulty or matter that may arise. The CONTRACTING PARTIES shall, if requested to do so by such contracting party, consult with all contracting parties concerned with respect to the matter with a view to reaching solutions satisfactory to all such contracting parties.

5. The developed countries do not expect reciprocity for commitments made by them in trade negotiations to reduce or remove tariffs and other barriers to the trade of developing countries, i.e., the developed countries do not expect the developing countries, in the course of trade negotiations, to make contributions which are inconsistent with their individual development, financial and trade needs. Developed contracting parties shall therefore not seek, neither shall less-developed contracting parties be required to make, concessions that are inconsistent with the latter's development, financial and trade needs.

6. Having regard to the special economic difficulties and the particular development, financial and trade needs of the least-developed countries, the developed countries shall exercise the utmost restraint in seeking any concessions or contributions for commitments made by them to reduce or remove tariffs and other barriers to the trade of such countries, and the least-developed countries shall not be expected to make concessions or contributions that are inconsistent with the recognition of their particular situation and problems.

7. The concessions and contributions made and the obligations assumed by developed and less-developed contracting parties under the provisions of the General Agreement should promote the basic objectives of the Agreement, including those embodied in the Preamble and in Article XXXVI. Less-developed contracting parties expect that their capacity to make contributions or negotiated concessions or take other mutually agreed action under the provisions and procedures of the General Agreement would improve with the progressive development of their economies and improvement in their trade situation and they would accordingly expect to participate more fully in the framework of rights and obligations under the General Agreement.

8. Particular account shall be taken of the serious difficulty of the least-developed countries in making concessions and contributions in view of their special economic situation and their development, financial and trade needs.

9. The contracting parties will collaborate in arrangements for review of the operation of these provisions, bearing in mind the need for individual and joint efforts by contracting parties to meet the development needs of developing countries and the objectives of the General Agreement.

⁴ Nothing in these provisions shall affect the rights of contracting parties under the General Agreement.

World Trade Organization

United States – Subsidies on Upland Cotton

Report of the Appellate Body, 3 March 2005

(05-0884)

Original: English

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UNITED STATES – SUBSIDIES ON UPLAND COTTON

AB-2004-5

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US – Gasoline	Appellate Body Report, <i>United States – Standards for Reformulated and Conventional Gasoline</i> , WT/DS2/AB/R, adopted 20 May 1996, DSR 1996:1, 3
US – Hot-Rolled Steel	Appellate Body Report, <i>United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan</i> , WT/DS184/AB/R, adopted 23 August 2001, DSR 2001:X, 4697
US – Lamb	Appellate Body Report, <i>United States – Safeguard Measures on Imports of Fresh, Chilled or Frozen Lamb Meat from New Zealand and Australia</i> , WT/DS177/AB/R, WT/DS178/AB/R, adopted 16 May 2001, DSR 2001:IX, 4051
US – Lead and Bismuth II	Appellate Body Report, <i>United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom</i> , WT/DS138/AB/R, adopted 7 June 2000, DSR 2000:Y, 2595
US – Line Pipe	Appellate Body Report, <i>United States – Definitive Safeguard Measures on Imports of Circular-Welded Carbon Quality Line Pipe from Korea</i> , WT/DS202/AB/R, adopted 8 March 2002
US – Section 211 Appropriations Act	Appellate Body Report, <i>United States – Section 211 Omnibus Appropriations Act of 1998</i> , WT/DS176/AB/R, adopted 1 February 2002, DSR 2002:II, 589
US – Shrimp (Article 21.5 – Malaysia)	Appellate Body Report, <i>United States – Import Prohibition of Certain Shrimp and Shrimp Products – Recourse to Article 21.5 of the DSU by Malaysia</i> , WT/DS58/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6481
US – Softwood Lumber IV	Appellate Body Report, <i>United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada</i> , WT/DS257/AB/R, adopted 17 February 2004
US – Steel Safeguards	Appellate Body Report, <i>United States – Definitive Safeguard Measures on Imports of Certain Steel Products</i> , WT/DS248/AB/R, WT/DS249/AB/R, WT/DS251/AB/R, WT/DS252/AB/R, WT/DS253/AB/R, WT/DS254/AB/R, WT/DS258/AB/R, WT/DS259/AB/R, adopted 10 December 2003

US – Wheat Gluten	Appellate Body Report, <i>United States – Definitive Safeguard Measures on Imports of Wheat Gluten from the European Communities</i> , WT/DS166/AB/R, adopted 19 January 2001, DSR 2001:II, 717
US – Wool Shirts and Blouses	Appellate Body Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/AB/R and Corr.1, adopted 23 May 1997, DSR 1997:1, 323
US – Wool Shirts and Blouses	Panel Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/R, adopted 23 May 1997, as upheld by the Appellate Body Report, WT/DS33/AB/R, DSR 1997:1, 343

WORLD TRADE ORGANIZATION
APPELLATE BODY

TABLE OF ABBREVIATIONS USED IN THIS REPORT

Abbreviation	Description
AMS	Aggregate Measurement of Support
<i>Anti-Dumping Agreement</i>	<i>Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994</i>
CCC	Commodity Credit Corporation
CCP payments	counter-cyclical payments
DP payments	direct payments
DSB	Dispute Settlement Body
DSU	<i>Understanding on Rules and Procedures Governing the Settlement of Disputes</i>
ETI Act	FSC Repeal and Extraterritorial Income Exclusion Act of 2000, Public Law 106-519
FAIR Act of 1996	Federal Agriculture Improvement and Reform Act of 1996, Public Law 104-127
FSRI Act of 2002	Farm Security and Rural Investment Act of 2002, Public Law 107-171
GATT 1994	<i>General Agreement on Tariffs and Trade 1994</i>
GSM 102	General Sales Manager 102
GSM 103	General Sales Manager 103
MLA payments	market loss assistance payments
peace clause	Article 13 of the <i>Agreement on Agriculture</i>
Panel Report	Panel Report, <i>United States – Subsidies on Upland Cotton</i> ("US – Upland Cotton"), WT/DS267/R, and Corr.1, 8 September 2004
PFC payments	production flexibility contract payments
price-contingent subsidies	Marketing loan program payments, Step 2 payments, market loss assistance payments, and counter-cyclical payments
SCGP	Supplier Credit Guarantee Program
<i>SCM Agreement</i>	<i>Agreement on Subsidies and Countervailing Measures</i>
Step 2 payments	User marketing (Step 2) payments
USDA	United States Department of Agriculture
<i>Vienna Convention</i>	<i>Vienna Convention on the Law of Treaties</i> , done at Vienna, 23 May 1969, 1155 U.N.T.S. 331; 8 International Legal Materials 679
<i>Working Procedures</i>	<i>Working Procedures for Appellate Review</i>
WTO	World Trade Organization
<i>WTO Agreement</i>	<i>Marrakesh Agreement Establishing the World Trade Organization</i>

United States – Subsidies on Upland Cotton

United States, *Appellant/Appellee*
Brazil, *Appellanti/Appellee*

AB-2004-5

Present:

Janow, Presiding Member
Baptista, Member
Ganesan, Member

Argentina, *Third Participant*
Australia, *Third Participant*
Benin, *Third Participant*
Canada, *Third Participant*
Chad, *Third Participant*
China, *Third Participant*
European Communities, *Third Participant*
India, *Third Participant*
New Zealand, *Third Participant*
Pakistan, *Third Participant*
Paraguay, *Third Participant*
Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu, *Third Participant*
Venezuela, *Third Participant*

I. Introduction

1. The United States and Brazil each appeals certain issues of law and legal interpretations developed in the Panel Report, *United States – Subsidies on Upland Cotton* (the "Panel Report").¹ The Panel was established on 18 March 2003 to consider claims by Brazil regarding various United States measures² that Brazil alleged constituted actionable subsidies within the meaning of Part III of the *Agreement on Subsidies and Countervailing Measures* (the "*SCM Agreement*"), prohibited subsidies within the meaning of Part II of the *SCM Agreement*, export subsidies within the scope of the *Agreement on Agriculture*, and/or subsidies actionable under Article XVI of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994"). Brazil also alleged that certain of these measures were inconsistent with Article III:4 of the GATT 1994. The United States argued that some

¹WT/DS267/R, 8 September 2004.

²Brazil made claims in respect of marketing loan program payments, user marketing (Step 2) payments, production flexibility contract payments, market loss assistance payments, direct payments, counter-cyclical payments, crop insurance payments, cottonseed payments, export credit guarantees and the FSC Repeal and Extraterritorial Income Exclusion Act of 2000 (Public Law 106-519) (the "ETI Act of 2000"). Brazil also made claims regarding legislation and regulations underlying certain of these programs. All of these measures are described more fully in paragraphs 7.200 to 7.250 of the Panel Report and are discussed further in the relevant sections of this Report.

of the measures were domestic support measures that were exempt from certain actions by virtue of paragraphs (a) and (b) of Article 13 of the *Agreement on Agriculture*.

2. The Panel Report was circulated to Members of the World Trade Organization (the "WTO") on 8 September 2004. In paragraph 7.194 of its Report, the Panel made the following findings with respect to whether certain measures fell within its terms of reference:

The Panel rules that the following measures, as addressed in document WT/DS267/7, are within its terms of reference:

- (i) export credit guarantees to facilitate the export of United States upland cotton, and other eligible agricultural commodities;
- (ii) production flexibility contract payments and market loss assistance payments³

3. The Panel also ruled, in paragraph 7.196 of its Report, that:

... in its request for consultations in document WT/DS267/1, Brazil provided a statement of available evidence with respect to export credit guarantees under the GSM 102, GSM 103 and SCGP programmes relating to upland cotton and eligible agricultural commodities other than upland cotton, as required by Article 4.2 of the *SCM Agreement*.

4. With respect to the substantive issues raised by the parties, the Panel set out the following conclusions in paragraph 8.1 of its Report:

- (a) Article 13 of the *Agreement on Agriculture* is not in the nature of an affirmative defence;
- (b) PFC payments⁴, DP payments⁵, and the legislative and regulatory provisions which establish and maintain the DP programme, do not satisfy the condition in paragraph (a) of Article 13 of the *Agreement on Agriculture*;

³The Panel also ruled that production flexibility contract payments, market loss assistance payments, direct payments and counter-cyclical payments to upland cotton producers with respect to non-upland cotton base acres; cottonseed payments under both Public Law 106-224 and Public Law 107-25 (for the 2000 crop); storage payments and interest subsidies that implement the marketing loan program; and payments under programs and provisions within the Panel's terms of reference made after the date on which the Panel was established, were all within its terms of reference. (See Panel Report, para. 7.194(iii)-(vi)). The Panel also ruled that certain other measures fell outside of its terms of reference: see Panel Report, para. 7.195

⁴Production flexibility contract payments. Production flexibility contract payments are described by the Panel in paras. 7.212 ff of the Panel Report and are discussed further *infra*, para. 251.

⁵Direct payments. Direct payments are described by the Panel in paras. 7.218 ff of the Panel Report and are discussed further *infra*, para. 312.

(c) United States domestic support measures considered in Section VII:D of this report⁶ grant support to a specific commodity in excess of that decided during the 1992 marketing year and, therefore, do not satisfy the conditions in paragraph (b) of Article 13 of the *Agreement on Agriculture* and, therefore, are not exempt from actions based on paragraph 1 of Article XVI of the *GATT 1994* or Articles 5 and 6 of the *SCM Agreement*;

(d) concerning United States export credit guarantees under the GSM 102⁷, GSM 103⁸ and SCGP⁹ export credit guarantee programmes:

(i) in respect of exports of upland cotton and other unscheduled agricultural products supported under the programmes, and in respect of one scheduled product (rice):

- United States export credit guarantees under the GSM 102, GSM 103 and SCGP export credit guarantee programmes are export subsidies applied in a manner which results in circumvention of United States' export subsidy commitments, within the meaning of Article 10.1 of the *Agreement on Agriculture* and they are therefore inconsistent with Article 8 of the *Agreement on Agriculture*;

- as they do not conform fully to the provisions of Part V of the Agreement on Agriculture, they do not satisfy the condition in paragraph (c) of Article 13 of the *Agreement on Agriculture* and, therefore, are not exempt from actions based on Article XVI of the *GATT 1994* or Articles 3, 5 and 6 of the *SCM Agreement*;

⁶In Section VII:D of the Panel Report, the Panel considered the following measures for purposes of calculating support during the implementation period in which Article 13 of the *Agreement on Agriculture* applies: marketing loan program payments, user marketing (Step 2) payments to domestic users (and not to exporters), production flexibility contract payments, market loss assistance payments, direct payments, counter-cyclical payments, crop insurance payments, and cottonseed payments for the 1999, 2000, and 2002 crops of cottonseed. (Panel Report, para. 7.537 and footnote 695 thereto)

⁷General Sales Manager 102 ("GSM 102"). The United States' export credit guarantee programs, including the GSM 102 program, are described by the Panel in paras. 7.236 ff of the Panel Report and are discussed further *infra*, paras. 586-587.

⁸General Sales Manager 103 ("GSM 103"). The United States' export credit guarantee programs, including the GSM 103 program, are described by the Panel in paras. 7.236 ff of the Panel Report and are discussed further *infra*, paras. 586 and 588.

⁹Supplier Credit Guarantee Program ("SCGP"). The United States' export credit guarantee programs, including the SCGP program, are described by the Panel in paras. 7.236 ff of the Panel Report and are discussed further *infra*, paras. 586 and 589.

- United States export credit guarantees under the GSM 102, GSM 103 and SCGP export credit guarantee programmes are provided by the United States government at premium rates which are inadequate to cover long-term operating costs and losses of the programmes within the meaning of item (j) of the Illustrative List of Export Subsidies in Annex I of the *SCM Agreement*, and therefore constitute *per se* export subsidies prohibited by Articles 3.1(a) and 3.2 of the *SCM Agreement*.

(ii) however, in respect of exports of unscheduled agricultural products not supported under the programmes and other scheduled agricultural products:

- the United States has established that export credit guarantees under the GSM 102, GSM 103 and SCGP export credit guarantee programmes have not been applied in [a] manner which either results in, or which threatens to lead to, circumvention of United States export subsidy commitments within the meaning of Article 10.1 and that they therefore are not inconsistent with Article 8 of the *Agreement on Agriculture*;

- in these circumstances, and as Brazil has also not made a prima facie case before this Panel that the programmes do not conform fully to the provisions of Part V of the *Agreement on Agriculture*, this Panel must treat them as if they are exempt from actions based on Article XVI of the *GATT 1994* and Article 3 of the *SCM Agreement* in this dispute.

(e) concerning section 1207(a) of the FSRI Act of 2002¹⁰ providing for user marketing (Step 2) payments to exporters of upland cotton:

(i) section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to exporters of upland cotton is an export subsidy, listed in Article 9.1(a) of the *Agreement on Agriculture*, provided in respect of upland cotton, an unscheduled product. It is, therefore, inconsistent with the United States' obligations under Articles 3.3 and 8 of the *Agreement on Agriculture*;

(ii) as it does not conform fully to the provisions of Part V of the *Agreement on Agriculture*, it does not satisfy the condition in paragraph (c) of Article 13 of the *Agreement on Agriculture* and, therefore, is not exempt from actions based on Article XVI of the *GATT 1994* or Articles 3, 5 and 6 of the *SCM Agreement*;

(iii) section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to exporters of upland cotton is an export subsidy prohibited by Articles 3.1(a) and 3.2 of the *SCM Agreement*.

(f) concerning section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to domestic users of upland cotton: it is an import substitution subsidy prohibited by Articles 3.1(b) and 3.2 of the *SCM Agreement*;

(g) concerning serious prejudice to the interests of Brazil:

(i) the effect of the mandatory price-contingent United States subsidy measures – marketing loan programme payments, user marketing (Step 2) payments, MLA payments¹¹ and CCP payments¹² -- is significant price suppression in the same world market within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*;

(ii) however, Brazil has not established that:

- the effect of PFC payments, DP payments and crop insurance payments is significant price suppression in the same world market within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*; or

¹¹Market loss assistance payments. Market loss assistance payments are described by the Panel in paras. 7.216 ff of the Panel Report and are discussed further *infra*, para. 2.51 and footnote 368.

¹²Counter-cyclical payments. Counter-cyclical payments are described by the Panel in paras. 7.223 ff of the Panel Report and are discussed further *infra*, footnote 370.

¹⁰Farm Security and Rural Investment Act of 2002 (the "FSRI Act of 2002"); Public Law 107-171.

- the effect of the United States subsidy measures listed in paragraph 7.1107 of Section VII:G of this report¹³ is an increase in the United States' world market share within the meaning of Article 6.3(d) of the *SCM Agreement* constituting serious prejudice within the meaning of Article 5(c) of the *SCM Agreement*.

- (h) concerning the ETI Act of 2000:
 - (i) Brazil has not made a prima facie case before this Panel that the ETI Act of 2000 and alleged export subsidies provided thereunder are inconsistent with Articles 10.1 and 8 of the *Agreement on Agriculture* in respect of upland cotton;
 - (ii) with respect to the condition in Article 13(c)(ii) of the *Agreement on Agriculture*, as Brazil has also not made a prima facie case before this Panel that they do not conform fully to the provisions of Part V of the *Agreement on Agriculture* in respect of upland cotton, this Panel must treat them as if they are exempt from actions based on Article XVI of the *GATT 1994* and Article 3 of the *SCM Agreement* in this dispute. (footnotes omitted)

5. Based on these conclusions, the Panel recommended that the United States bring the measures listed in paragraphs 8.1(d)(i) and 8.1(e) of the Panel Report into conformity with the *Agreement on Agriculture*¹⁴, and withdraw the prohibited subsidies listed in paragraphs 8.1(d)(i), 8.1(e) and 8.1(f) of the Panel Report without delay and, at the latest, within six months of the date of adoption of the Panel Report by the Dispute Settlement Body (the "DSB") or 1 July 2005 (whichever is earlier).¹⁵ With respect to the "mandatory price-contingent United States subsidy measures" addressed in paragraph 8.1(g)(i) of the Panel Report, the Panel noted that, pursuant to Article 7.8 of the *SCM Agreement*, "upon adoption of [the Panel Report] the United States is under an obligation to take appropriate steps to remove the adverse effects or ... withdraw the subsidy."¹⁶

¹³The Panel listed the following measures in paragraph 7.1107 of its Report: "(i) user marketing (Step 2) payments to domestic users and exporters; (ii) marketing loan programme payments; (iii) production flexibility contract payments; (iv) market loss assistance payments; (v) direct payments; (vi) counter-cyclical payments; (vii) crop insurance payments; (viii) cottonseed payments for the 2000 crop; and (ix) legislative and regulatory provisions currently providing for the payment of measures in (i), (ii), (v), (vi) and (vii) above".

¹⁴Panel Report, para. 8.3(a).

¹⁵*Ibid.*, paras. 8.3(b) and 8.3(c).

¹⁶*Ibid.*, para. 8.3(d).

6. On 18 October 2004, the United States notified the DSB of its intention to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, pursuant to paragraph 4 of Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), and filed a Notice of Appeal¹⁷ pursuant to Rule 20 of the *Working Procedures for Appellate Review* (the "*Working Procedures*").¹⁸ On 28 October 2004, the United States filed its appellant's submission.¹⁹ On 2 November 2004, Brazil filed an other appellant's submission.²⁰ On 16 November 2004, Brazil and the United States each filed an appellee's submission.²¹

7. On 16 November 2004, Argentina, Australia, Canada, China, the European Communities, and New Zealand each filed a third participant's submission, and Benin and Chad filed a joint third participants' submission.²² India, Pakistan, Paraguay, Venezuela, and the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu notified the Appellate Body of their intention to appear at the oral hearing.²³

8. After consultation with the Appellate Body Secretariat, Brazil and the United States noted, in letters filed on 10 December 2004, that it would not be possible for the Appellate Body to circulate its Report in this appeal within the 90-day time limit referred to in Article 17.5 of the DSU. Brazil and the United States agreed that additional time was needed for several reasons: the issues arising in this

¹⁷WT/DS267/17, 18 October 2004, attached as Annex 1 to this Report.

¹⁸WT/AB/WP/4, 1 May 2003. Revised *Working Procedures* were circulated by the Appellate Body during the course of these proceedings (WT/AB/WP/5, 4 January 2005). These revised *Working Procedures*, however, apply only to appeals initiated after 1 January 2005 and therefore did not apply to this appeal.

¹⁹Pursuant to Rule 21(1) of the *Working Procedures*. In a letter dated 1 November 2004, Brazil, without requesting action by the Appellate Body, drew attention to the failure by the United States to submit its appellant's submission in a timely fashion. Brazil observed that the United States' appellant's submission was submitted on 28 October 2004 after the deadline of 5:00 p.m. that had been established by the Division in the *Working Schedule* issued pursuant to Rule 26 of the *Working Procedures*.

²⁰Pursuant to Rule 23(1) of the *Working Procedures*.

²¹Pursuant to Rules 22 and 23(3) of the *Working Procedures*, respectively.

²²Pursuant to Rule 24(1) of the *Working Procedures*.

²³Pursuant to Rule 24 of the *Working Procedures*. The notifications were received on the following dates: India, 16 November 2004; Pakistan, 17 November 2004; Paraguay, 17 November 2004; Venezuela, 17 November 2004; and the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu, 18 November 2004.

appeal were particularly numerous and complex compared to prior appeals, which increased the burden on the Appellate Body and WTO translation services; WTO translation services were unavailable during the WTO holiday period; and the Appellate Body was likely to be considering two or three other appeals during the same period. Brazil and the United States accordingly confirmed that they would deem the Appellate Body Report in this proceeding, issued no later than 3 March 2005, to be an Appellate Body Report circulated pursuant to Article 17.5 of the DSU.²⁴

9. The oral hearing in this appeal was held on 13-15 December 2004. The participants and third participants presented oral arguments (with the exception of Pakistan, Paraguay, and Venezuela) and responded to questions posed by the Members of the Division hearing the appeal.

II. Arguments of the Participants and the Third Participants

A. *Claims of Error by the United States – Appellant*

1. Domestic Support

(a) Terms of Reference – Expired Measures

10. The United States contends that the Panel was wrong to reject its argument that payments under the expired production flexibility contract and market loss assistance programs were outside the Panel's terms of reference. The United States asks the Appellate Body to reverse the Panel's finding because these measures had expired before Brazil requested consultations.

11. Article 4.2 of the DSU provides that consultations are to cover "any representations made by another Member concerning measures affecting the operation of any covered agreement taken within the territory of the former".²⁵ The United States submits that measures that have expired before a request for consultations cannot be measures that are "affecting the operation of any covered agreement" at the time the request is made; consequently, they cannot be measures within the scope of the "dispute" referred to in Article 4.7, with respect to which a complaining Member can request the establishment of a panel. It was common ground that the legislation authorizing production flexibility contract payments and market loss assistance payments expired before Brazil's consultation and panel requests. They thus cannot have been within the scope of consultations under Article 4.2.

²⁴On 16 December 2004, the Appellate Body notified the Chair of the DSB that the expected date of circulation of its Report was 3 March 2005. (WT/DS267/18, 20 December 2004)

²⁵United States' appellant's submission, para. 501. (emphasis added by the United States)

12. In response to the Panel's concern that the United States' position would mean that subsidy payments made in the past might never be the subject of challenge in WTO dispute settlement, the United States distinguishes between recurring and non-recurring subsidies. A non-recurring subsidy is a type of subsidy the benefits of which are allocated to future production. As such, a non-recurring subsidy can be regarded as continuing in existence beyond the period during which it is granted, and may continue to be actionable even after the authorizing program or legislation has expired. A recurring subsidy, by contrast, is typically provided year after year and is provided for current rather than future production. Once production has occurred and a measure has been replaced or superseded, there would no longer be any measure in existence to challenge. Market loss assistance and production flexibility contract payments were both subsidies paid for particular fiscal or crop years. As such, the benefit of these subsidies should have been attributed only to the particular year of payment and should not have been attributed to subsequent years. Thus, by the time of Brazil's consultation and panel requests²⁶, the only measure to consult upon and at issue under the DSU was the 2002 marketing year production flexibility contract payments; the other payments were all outside the Panel's terms of reference.

13. According to the United States, the Panel's conclusion is also inconsistent with Article 6.2 of the DSU, which requires that a panel request "identify the specific measures at issue". A measure that has expired cannot be a measure that is "at issue". This is confirmed by the context provided by Article 3.7 of the DSU, which contemplates the withdrawal of measures found to be inconsistent with the covered agreements, and Article 19.1 of the DSU, which contemplates a measure that "is inconsistent" with a covered agreement.

14. In addition to appealing the Panel's finding that payments under the expired production flexibility contract and market loss assistance programs were within its terms of reference, the United States lists this Panel finding as an example of the Panel's failure to meet the requirements of Article 12.7 of the DSU, which requires panels to set out the findings of fact, the applicability of relevant provisions, and the basic rationale behind its findings.

(b) Article 13(a) of the *Agreement on Agriculture – Planting Flexibility Limitations*

15. The United States appeals the Panel's finding that production flexibility contract payments, direct payments, and the legislative and regulatory provisions that establish and maintain the direct payment program²⁷ are not exempt from actions by virtue of paragraph (a) of Article 13 of the

²⁶Request for Consultations by Brazil, WT/DS267/1, G/L/571, G/SCM/D49/1, G/AG/GEN/54, 3 October 2002; Request for the Establishment of a Panel by Brazil, WT/DS267/7, 7 February 2003.

²⁷Panel Report, para. 7.388.

Agreement on Agriculture (the "peace clause"). The United States observes that the sole basis for this finding was the Panel's conclusion that these measures do not conform fully to paragraph 6(b) of Annex 2 of the *Agreement on Agriculture* (the "green box")²⁸, which conditions green box coverage and exemption under the peace clause upon the amount of payments not being related to the type or volume of production. The United States argues that, to make this finding, the Panel had to find that banning a recipient from producing a certain range of products was the same as conditioning the amount of payment on the type of production. The United States submits that paragraph 6(b) of Annex 2 permits such a partial ban.

16. The United States points out that, in order to receive production flexibility contract payments or direct payments, a producer is not required to produce a particular (or, indeed, any) crop. Instead, payments are based on a farm's historical acreage and yields during a base period. Farmers may plant any commodity or crop, subject to limitations concerning the planting of fruits and vegetables (and wild rice in the case of direct payments).²⁹ Where fruits, vegetables, or wild rice are produced, payments are eliminated or reduced, subject to certain exceptions.

17. Although the ordinary meaning of the term "related to" implies a relation or connection that could be positive or negative, the ordinary meaning does not identify which type of connection is meant under paragraph 6(b) of Annex 2. Turning to the context, the United States notes that this paragraph speaks of the "amount of such payments" not being related to or based on the type or volume of production. The United States argues that "[t]he Panel assumes that the 'amount of such payments' can be related to the current type of production (that is, of fruits or vegetables) because in some circumstances a recipient that produces fruits or vegetables receives less payment than that recipient otherwise would have been entitled to."³⁰ However, given that the payment relating to fruits, vegetables, or wild rice is zero, the "amount of such payments" is not related to fruit, vegetable, or wild rice production, because for the acres concerned, there is no payment at all. As regards the phrase "production ... undertaken by the producer" in paragraph 6(b), the United States notes that the term "undertaken" means, *inter alia*, to "attempt". In this case, the planting flexibility limitations ban a recipient from producing a certain range of products. This does not relate to the production "attempted"; rather, it relates to the type of production *not* attempted. Taken together, the ordinary meaning of the terms "amount of such payments" and "production ... undertaken" indicate that

²⁸Paragraph 6(b) of Annex 2 to the *Agreement on Agriculture* provides that:

The amount of such payments in any given year shall not be related to, or based on, the type or volume of production (including livestock units) undertaken by the producer in any year after the base period.

²⁹Panel Report, paras. 7.376-7.382.

³⁰United States' appellant's submission, para. 26 (referring to Panel Report, para. 7.383).

payments are not "related to" current production within the meaning of paragraph 6(b) when a Member conditions payments on a recipient not producing certain products.

18. According to the United States, this interpretation is consistent with the "fundamental requirement" set out in paragraph 1 of Annex 2 of the *Agreement on Agriculture* that measures exempted from reduction commitments "have no, or at most minimal, trade-distorting effects or effects on production". The United States submits that "a condition that a recipient not produce certain products serves the fundamental requirement of Annex 2".³¹ The United States further argues that the effect of the planting flexibility limitations at issue is minimal and does not result in increased production, pointing to evidence on the record showing that 47 per cent of farms receiving production flexibility contract payments or direct payments in the 2002 marketing year planted no upland cotton at all. Indeed, in finding that Brazil had not established that the effect of the United States' decoupled income support payments was significant price suppression, the Panel implicitly found that production flexibility contract payments and direct payments do not have more than minimal effects on production. For the United States, an explicit decision not to support a particular type of production does not relate the amount of payments to the type of production undertaken by the producer. Rather, such a decision serves the fundamental requirement that "green box" measures have no more than minimal trade-distorting effects, because a measure that conditions payment on not producing something does not create production inducements.

19. The United States also submits that the context provided by paragraph 6(e) confirms its reading of paragraph 6(b). Paragraph 6(e) provides: "[n]o production shall be required in order to receive such payments"; it does not preclude a Member from requiring non-production. A proper reading reveals that paragraphs 6(b) and 6(e) serve different purposes. As a Member may, under paragraph 6(e), require a recipient not to produce, it would not make sense to then prohibit a Member, under paragraph 6(b), from making the amount of payment contingent on fulfilling the requirement not to produce.

20. Furthermore, the United States argues that the Panel was incorrect to find contextual support for its interpretation of paragraph 6(b) in paragraphs 11(b) and 11(e) of Annex 2. Paragraphs 6(b) and 11(b) contain similar requirements about not relating payments to the type or volume of production, but paragraph 11(b) refers explicitly to paragraph 11(e), which permits requirements not to produce a particular product. The United States maintains that the context in which paragraphs 6(b) and 11(b) appear is very different. In the context of paragraph 6, an explicit authorization of requirements not to produce is not required as it is already implicit within the

³¹United States' appellant's submission, para. 22.

provisions. The United States notes that paragraph 11 pertains to payments "to assist the financial or physical restructuring of a producer's operations".³² Although such aid is for restructuring of operations that will continue to produce, paragraph 11(e) imposes a constraint on the degree to which a government can interfere in the form that restructuring will take, by requiring that payments must not "mandate or in any way designate the agricultural products to be produced". A requirement not to produce certain products could be understood to fall within the prohibition in paragraph 11(e) against "in any way" designating the products to be produced. In order to allow such requirements, paragraph 11(e) clarifies that they are permitted. The United States submits that, in the light of the broad prohibition in paragraph 11(e), the requirement in paragraph 11(b) could be understood to *preclude* conditioning payment on *not* producing certain products, as this could be understood to be designating, in some way, the products to be produced. According to the United States, this would undermine the prohibition in paragraph 11(e). The cross-reference in paragraph 11(b) to the exception in paragraph 11(e) thus simply serves to make clear that conditioning payments on *not* producing does not conflict with the prohibition under paragraph 11(e) on designating in any way the products to be produced.

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221. In addition, the United States submits that the Panel's reading of paragraph 6(b) would require payments even if a recipient's production was illegal. Therefore, a Member would be prohibited from reducing or eliminating payments for prohibited types of production such as narcotic crops, unapproved biotech varieties, or environmentally damaging production.

(c) Article 13(b) of the *Agreement on Agriculture*

22. The United States appeals the Panel's finding that the United States' non-green box domestic support measures are not exempt from actions by virtue of paragraph (b) of Article 13 of the *Agreement on Agriculture*. The Panel found that those measures failed to satisfy, for each marketing year from 1999-2002, the proviso to Article 13(b)(ii), which reads "provided that such measures do not grant support to a specific commodity in excess of that decided during the 1992 marketing year".

(i) *Interpretation of "support to a specific commodity"*

23. The United States contends that the Panel erred in interpreting the phrase "support to a specific commodity" in Article 13(b)(ii). The ordinary meaning of this phrase encompasses "assistance or backing' 'specially ... pertaining to a particular' 'agricultural crop' or ... for a precise,

exact, definite' 'agricultural crop'".³³ The ordinary meaning implies that support to a specific commodity excludes support that is not for a precise, exact, definite agricultural crop.

24. Context for interpreting the phrase "support to a specific commodity" may be found in other provisions of the *Agreement on Agriculture* that contain the terms "support", "specific" and "commodity". Annex 3 deals with "Calculation of the Aggregate Measurement of Support" ("AMS"). Paragraph 1 of that Annex clarifies that two types of support are to be calculated: first, support is calculated "on a product-specific basis", and, second, "[s]upport which is non-product specific shall be totalled into one non-product-specific AMS in total monetary terms". Article 1(a) of the *Agreement on Agriculture* contains this same distinction between "support ... provided for an agricultural product in favour of the producers of the basic agricultural product" and a residual category of "non-product-specific ... support". Article 1(h) also makes this distinction by dividing total support into "non-product-specific support" and "support for basic agricultural products". For the United States, the terms "support for basic agricultural products" in Article 1(h) and "support ... provided for an agricultural product in favour of the producers of the basic agricultural product" in Article 1(a) are virtually synonymous with the phrase "support for a specific commodity" in Article 13(b)(ii). The context of these provisions thus suggests that this phrase also means product-specific support.

25. The Panel relied on the different choice of specific words in Articles 1(a) and 13(b)(ii) in finding that the former was not pertinent to the interpretation of the latter. The United States argues, however, that the concept of product-specific support is expressed in different terms in different places in the *Agreement on Agriculture*. Indeed, nowhere in the Agreement is the precise phrase "product-specific support" used, although the Panel had no difficulty in finding that such a concept exists. Thus, the fact that the phrase "product-specific support" was not used in Article 13 does not prevent an interpretation that the concept nevertheless applies.

26. The United States disagrees with the Panel's reasoning that the categories of product-specific and non-product-specific support are not pertinent to the analysis under Article 13(b) because the proviso to Article 13(b)(ii) begins with the phrase "such measures", which refers to all the domestic support measures falling under Article 6 identified in the chapeau to Article 13(b), and not just to product-specific and non-product-specific support subject to reduction commitments. The United States notes that the Panel itself recognized that certain domestic support measures falling under Article 6 could be excluded from the comparison of support under Article 13(b)(ii): the Panel's approach "exclud[es] all other support, which either grants support to other specific commodities or

³²United States' appellant's submission, para. 45 (quoting paragraph 11(a) of Annex 2 to the *Agreement on Agriculture*).

³³United States' appellant's submission, para. 85 (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 2, pp. 2972 and 3152).

does not grant support to any specific commodity".³⁴ The Panel also noted that "Brazil acknowledges this implicitly in that it does not challenge very widely available support, such as infrastructure or irrigation subsidies, some of which, presumably, deliver support to upland cotton either directly or indirectly".³⁵ Thus the mere fact that all domestic support measures falling under Article 6 are identified in the chapeau of Article 13(b) does not resolve the issue of whether a particular measure grants "support to a specific commodity".

27. The United States finds relevant context in Articles 3 and 6 of the *Agreement on Agriculture*. Under these provisions, a Member must comply with its domestic support reduction commitments. These commitments, however, are expressed on a total aggregate basis with no product-specific caps on support. Because there are no product-specific caps, a Member can comply with its overall reduction commitments while increasing support to a particular agricultural commodity. Article 13(b) provides shelter from actions for domestic support measures that conform to the reduction commitments. However, Members recognized that an increase in product-specific support, even within overall reduction commitment levels, could present an enhanced risk of production or trade effects. The proviso to Article 13(b)(ii) thus makes the exemption it provides conditional upon a Member not shifting support between commodities such that the level of product-specific support exceeds that decided for any one commodity in the 1992 marketing year.

28. Turning to the measures at issue, the United States observes that the Panel's reasoning means that payments to producers that do not produce cotton at all are deemed to be "support to upland cotton". The United States contends that the Panel erred in finding that payments based on past production during a base period currently grant support to production of that commodity. Production flexibility contract payments, market loss assistance, direct payments, and counter-cyclical payments do not specify upland cotton as a commodity to which they grant support, as the Panel implied. In fact, payments under these programs do not require any production at all. Indeed, uncontested facts show that 47 per cent of the farms receiving these payments did not plant a single acre of upland cotton. The United States asserts that payments cannot be deemed to grant support to a crop the recipient does not produce. Such payments do not grant support to a specific commodity. In the light of the context provided by Articles 1(a), 1(h), and 6.4 and Annex 3 of the *Agreement on Agriculture*, such payments are properly seen as non-product-specific support to agricultural producers in general.

³⁴United States' appellant's submission, para. 96 (quoting Panel Report, para. 7.502).

³⁵*Ibid.*

29. The United States observes that the Panel correctly rejected all six of the methodologies proposed by Brazil for allocating decoupled payments as support to upland cotton. However, in the "Attachment to Section VII:D" the Panel included one allocation methodology that reduced payments on base acres to account only for the number of acres planted with upland cotton. The United States argues that, by including this methodology, the Panel endorsed it as an alternative to its own approach, in the event that the Panel's approach was found to be incorrect. The Panel labelled its finding in this regard as factual; however, the finding is patently legal, not sheltered from appellate review. The United States also contends that any methodology that allocates payments under the decoupled programs to upland cotton planted as a result of independent producer decisions beyond government control cannot reflect the support to a specific commodity that a Member has "decided", and thus is not appropriate for Article 13(b)(ii).

(ii) *Calculation methodology for price-based measures*

30. The United States submits that the Panel did not compare properly the support current measures "grant" to that "decided" during the 1992 marketing year. The ordinary meaning of "grant" is to "bestow as a favour" or "[g]ive or confer (a possession, a right, etc.) formally".³⁶ The ordinary meaning of "decide" is to "[d]etermine on as a settlement, pronounce in judgement" and "[c]ome to a determination or resolution *that, to do, whether*".³⁷ Read in their context, as two halves of a comparison, these terms must allow the relevant "support" to be compared. The phrase "grant support", read in the light of the verb "decided", means the support that Members determine to "bestow" or "give or confer", and thus the focus of the peace clause comparison is on the support a Member decides. The United States submits that the Panel essentially agreed "that the Peace Clause proviso compares the support a Member determines through its measures, not 'support [that] was spent due to reasons beyond the control of the government'".³⁸

31. Against this background, the United States contends that a proper application of Article 13(b)(ii) must reflect the way in which the United States "decided" support in the 1992 and 1999-2002 marketing years. In those years, the support "decided" by the United States was a rate of support.

³⁶United States' appellant's submission, para. 65 (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 1, p. 1131).

³⁷*Ibid.*, para. 65 (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 1, p. 607) (original emphasis)

³⁸*Ibid.*, para. 66 (quoting Panel Report, para. 7.487).

32. The United States submits that it was possible for the Panel to have recourse to the rules for the calculation of the AMS set out in Annex 3 of the *Agreement on Agriculture*, so long as the appropriate calculation method was used. In the case of price-based measures (such as marketing loan program payments in the 1992 marketing year and the implementation period, and deficiency payments in the 1992 marketing year only), paragraph 10 of Annex 3 permits two different approaches: budgetary outlays or using "the gap between the fixed reference price and the applied administered price multiplied by the quantity of production eligible to receive the administered price" ("price gap" methodology). In the context of a comparison under the peace clause, only the price gap methodology reflects the support "decided" by the United States' price-based measures. By focusing on the gap between an external reference price (here, the actual price for determining rates for the years 1986-1988) and the applied administered price, the price gap methodology eliminates movements in market prices as a component of the measurement of support and focuses solely on those elements that a Member can control. By holding the reference price "fixed", support measured using a price gap calculation shows the effect of changes in the level of support decided by a Member, rather than changes in budgetary outlays that result from movements in market prices that Members do not control.

(iii) *Recalculation of the peace clause comparison*

33. On the basis of its arguments regarding calculation methodology and the interpretation of the phrase "support to a specific commodity", the United States recalculates the support to upland cotton in the 1992 marketing year and implementation period support between 1999-2002 using the price gap methodology for marketing loan program payments and deficiency payments, on the one hand, and excluding production flexibility contract payments, market loss assistance, direct payments, and counter-cyclical payments, on the other hand, because they are not "support to a specific commodity". The result is that the United States' support to upland cotton does not exceed that decided in the 1992 marketing year in any year of the implementation period. The United States accordingly requests the Appellate Body to reverse the Panel's findings regarding Article 13(b) and to find that it is entitled to the protection of the peace clause.

2. Serious Prejudice

(a) Significant Price Suppression under Article 6.3(c) of the *SCM Agreement*

34. The United States appeals the Panel's finding that the effect of the price-contingent subsidies³⁹ is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*. The United States asks the Appellate Body to reverse the Panel's finding that the effect of the price-contingent subsidies is significant price suppression. The United States also submits that the Panel failed to set out the findings of fact, the applicability of relevant provisions, and the basic rationale behind several aspects of this finding, as required by Article 12.7 of the DSU.

35. First, the United States submits that the Panel erred in interpreting the term "same market" in Article 6.3(c) of the *SCM Agreement* as including a "world market". Under Article 6.3(c), the price suppression must occur in a market that includes the subsidized product and the like product. Identifying the relevant market as a world market fails to give meaning to the word "same" in Article 6.3(c) because "there is no 'other' world market where the products can be found".⁴⁰ The United States relies on Article 6.6 and Annex V of the *SCM Agreement* on "Procedures for Developing Information Concerning Serious Prejudice" to substantiate this view. The United States also indicates that, although the subsidized product and the like product must be found in the same market, the Panel did not make a finding that United States and Brazilian upland cotton compete in the world market that it had identified for upland cotton. In addition, the United States contends that the Panel acknowledged that different conditions of competition would prevail in the markets of different Members and that, therefore, each market in which the two products are found would need to be examined separately.

36. The United States submits that the Panel's reading of "same market" in Article 6.3(c) contradicts its reasoning in relation to Article 6.3(d) of the *SCM Agreement*, which, according to the United States, demonstrates that no "world market" price prevails in any "world market" for upland cotton. Moreover, according to the United States, the Panel should have focused on the effect of the challenged subsidies on the *Brazilian* price of upland cotton, rather than their effect on any "world

³⁹The Panel characterized marketing loan program payments, user marketing (Step 2) payments, market loss assistance payments, and counter-cyclical payments as "price-contingent" subsidies. (Panel Report, para. 8.1(g)(i))

⁴⁰United States' appellant's submission, para. 311.

market" price, because only significant suppression of Brazilian prices could lead to serious prejudice to the interests of Brazil under Article 5(c) of the *SCM Agreement*.

37. Secondly, the United States argues that, in finding significant price suppression, the Panel "prejudged the result of its analysis of 'the effect of the subsidy'".⁴¹ According to the United States, the Panel used circular logic: first, assuming causation in finding price suppression, and then, using its conclusion on price suppression to support its finding of causation. In addition, the Panel failed to take into account the effect of removing the price-contingent subsidies on all participants in the relevant market. Even if removing these subsidies would lead to lower United States production of cotton (which the United States contests), other producers could be expected to enter the market to increase supply. These supply changes would need to be included in assessing the effect on prices of removing the price-contingent subsidies. The United States also claims that, in concluding that the price suppression it had found was "significant", the Panel should have identified the degree of price suppression it had found and should have explained why it regarded this degree as "significant". The United States argues that, in failing to do so, the Panel failed to comply with Article 12.7 of the DSU.

38. Thirdly, the United States contends that the Panel erred in finding that "the effect of" the price-contingent subsidies is significant price suppression under Article 6.3(c) of the *SCM Agreement*. The United States refers to the Panel's conclusion that the price-contingent subsidies are linked to world prices for upland cotton, "thereby numbing the response of United States producers to production adjustment decisions when prices are low".⁴² However, according to the United States, the "relevant economic decision"⁴³ for a farmer is what to plant and, at the time of planting, the relevant price is what the farmer expects to receive when the crop is subsequently harvested, not the current price. Therefore, the Panel should have examined whether the price-contingent subsidies stimulate *planting* of upland cotton, rather than whether they stimulate *production* or harvesting. The United States submits that the Panel failed to set out the basic rationale for its analysis of the "effect of the subsidy" as required by Article 12.7.

39. The United States also suggests that the Panel failed to examine evidence showing that the price-contingent subsidies did not suppress upland cotton prices: United States planting of cotton acreage corresponded with expected market prices of cotton and competing crops; changes in United States cotton acreage corresponded with changes by cotton farmers throughout the world; and the United States' share of world cotton production was stable during the relevant period. In addition, the

⁴¹United States' appellant's submission, para. 158.

⁴²*Ibid.*, para. 162 (quoting Panel Report, para. 7.1308).

⁴³*Ibid.*, para. 161.

Panel's identification of the relative shares of world cotton exports cannot demonstrate the effect of the subsidy in the absence of an analysis of competition between United States cotton and cotton from other sources. Moreover, according to the United States, the Panel's finding of a "discernible temporal coincidence"⁴⁴ between suppressed market prices and the price-contingent subsidies is flawed and, in any case, could involve only correlation and not causation.

40. The United States further disputes, in relation to the Panel's reasoning in determining the "effect" of the subsidy, the Panel's conclusion that a comparison between the average total cost of production and market revenue in the United States demonstrates that the effect of the price-contingent subsidies is significant price suppression. As reflected in economics literature, farmers make planting decisions based on *variable* rather than *total* costs of production. The Appellate Body's decision in *Canada – Dairy (Article 21.5 – New Zealand and US)* is not relevant to this issue. Had the Panel examined variable costs, it would have seen that United States upland cotton producers more than covered their variable costs from 1997 to 2002, apart from in 2001. In addition, even if average total costs were not covered, the evidence before the Panel demonstrates that farmers had other sources of income to cover the shortfall.

41. Fourthly, the United States argues that the Panel erred in finding that Brazil need not demonstrate, and that the Panel need not find, the amount of the challenged subsidies that benefits upland cotton in establishing serious prejudice under Articles 5(c) and 6.3(c) of the *SCM Agreement*. The United States contends that the Panel "misunderstood"⁴⁵ the United States' argument as requiring the transposition of methodologies from Part V to Part III of the *SCM Agreement*. Instead, it is the text of Articles 5(c) and 6.3(c) that requires a quantification of benefit. Articles 5(c) and 6.3(c) of the *SCM Agreement* both use the word "subsidy", which is defined in Article I as involving the conferral of a benefit, as confirmed by Article 14 of the *SCM Agreement*. Article 6.3(c) refers to a "subsidized product". Therefore, what is at issue is the amount of the subsidy that benefits a particular product. This reading is supported by Article 6.8 of the *SCM Agreement*, which provides for panels to determine serious prejudice on the basis of, *inter alia*, information submitted under Annex V of the *SCM Agreement*. According to the United States, this includes information necessary to establish the amount of subsidization (paragraph 2 of Annex V) and information concerning the amount of the subsidy (paragraph 5 of Annex V).

42. For Brazil's claims to succeed, therefore, the United States maintains that the challenged subsidies would have to subsidize upland cotton and confer a benefit on United States "producers,

⁴⁴United States' appellant's submission, para. 208 (referring to Panel Report, paras. 7.1351-7.1352).

⁴⁵*Ibid.*, para. 258.

users, and/or exporters of upland cotton".⁴⁶ In addition, any benefit conferred by the challenged subsidies on products other than upland cotton cannot be included in determining the effect of the subsidies. However, the Panel attributed all counter-cyclical and market loss assistance payments to upland cotton. In fact, counter-cyclical and market loss assistance payments to recipients who did not produce upland cotton did not benefit upland cotton at all and therefore could not have caused serious prejudice and, in fact, fell outside the Panel's terms of reference altogether. As for counter-cyclical and market loss assistance payments to recipients who produced both upland cotton and other products, the Panel should have allocated the payments across the different products in assessing the effects of the payments in respect of upland cotton. Annex IV of the *SCM Agreement*⁴⁷ provides an "economically neutral" allocation methodology⁴⁸, and paragraphs 2 and 5 of Annex V of the *SCM Agreement* provide support for the argument that it may be necessary to allocate subsidies across the total value of the recipient's sales. As the Panel did not identify the amount of counter-cyclical and market loss assistance payments benefiting upland cotton, its serious prejudice finding regarding those payments is invalid. In addition, the United States submits that this amounted to a failure by the Panel to set out the basic rationale behind its findings and recommendations in accordance with Article 12.7 of the DSU.

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43. Along similar lines, the United States contends that the Panel should have determined the extent to which subsidies provided with respect to *raw cotton* benefit *processed cotton*. Instead, the Panel "improperly assumed"⁴⁹ that subsidies provided to producers of raw cotton flowed to producers of processed cotton. The United States maintains that the Appellate Body's conclusion in *US – Softwood Lumber IV* that a subsidy bestowed on an input cannot be presumed to have passed through to the processed product is based on the definition of a subsidy, which applies to both Part III and Part V of the *SCM Agreement*.⁵⁰ Therefore, according to the United States, the Panel erred in finding that "pass-through" principles do not apply to Part III of the *SCM Agreement*.

44. Finally, the United States asserts that the Panel erred in making serious prejudice findings with respect to the price-contingent subsidies for marketing years 1999 to 2001. Even if the Panel was not required to determine the amount of the benefit flowing from the price-contingent subsidies to the subsidized product, the Panel had to determine whether the benefit from these subsidies continued

⁴⁶United States' appellant's submission, para. 245 (quoting Brazil's request for establishment of a panel, *supra*, footnote 26, p. 1).

⁴⁷"Calculation of the Total Ad Valorem Subsidization (Paragraph 1(a) of Article 6)".

⁴⁸United States' appellant's submission, para. 269.

⁴⁹*Ibid.*, para. 303.

⁵⁰*Ibid.*, paras. 304 and 305 (referring to Appellate Body Report, *US – Softwood Lumber IV*, paras. 140 and 142).

when the Panel was established in 2002. This is because, under Article 11 of the DSU, the Panel could make findings only with respect to subsidies that could "form part of Brazil's claims"⁵¹ and, under Article 19.1 of the DSU, the Panel could make recommendations only with respect to measures that still exist. In addition, the United States maintains that the Panel "failed to adequately set out the legal basis for its examination of subsidies that no longer existed at the time of panel establishment" as required by Article 12.7 of the DSU.⁵²

45. According to the United States, an annually recurring subsidy should be "allocated" or "expensed"⁵³ to the year to which it relates, whereas a non-recurring subsidy, such as an investment subsidy or equity infusion, should be allocated over time. In the United States' view, a payment no longer confers a benefit after the year to which it is allocated, and therefore it is no longer a "subsidy" under Article 1 of the *SCM Agreement*. Price-contingent subsidies for marketing years 1999 to 2001 were annually recurring subsidies that the Panel should have allocated to those years. The United States argues that the Panel did not find that these subsidies had "continuing effects" when the Panel was established and, therefore, that the Panel could not have found that these subsidies were "causing present serious prejudice".⁵⁴

46. For these reasons, the United States requests the Appellate Body to reverse the Panel's finding that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*.

3. Import Substitution Subsidies and Export Subsidies

(a) Step 2 Payments

(i) *To domestic users*

47. The United States claims that the Panel erred in concluding that user marketing (Step 2) payments ("Step 2 payments") provided to domestic users of United States upland cotton, under Section 1207(a) of the FSRI Act of 2002, constitute import substitution subsidies that are inconsistent with Articles 3.1(b) and 3.2 of the *SCM Agreement*.

⁵¹United States' appellant's submission, para. 296.

⁵²*Ibid.*, para. 327.

⁵³*Ibid.*, para. 283.

⁵⁴*Ibid.*, para. 292.

48. In the United States' view, the Panel's conclusion fails to give meaning to the introductory phrase "Except as provided in the Agreement on Agriculture" in Article 3 of the *SCM Agreement*. This phrase applies not only to export subsidies covered by Article 3.1(a) of the *SCM Agreement*, but also to import substitution subsidies covered by Article 3.1(b). The United States contends that giving proper meaning to the introductory phrase of Article 3 of the *SCM Agreement* requires treating Step 2 payments to domestic users as domestic support subject to reduction commitments under Article 6 of the *Agreement on Agriculture*.

49. The United States points out that paragraph 7 of Annex 3 of the *Agreement on Agriculture* requires that "[m]easures directed at agricultural processors shall be included [within a WTO Member's AMS] to the extent that such measures benefit the producers of the basic agricultural products". This is consistent with the objective of the *Agreement on Agriculture* of providing for substantial progressive reductions in agricultural support and protection sustained over an agreed period of time. The United States submits that it has regularly reported Step 2 payments among the domestic support measures it provides to agricultural producers and includes them in the calculation of total AMS. Thus, the United States asserts, provided that they are within its domestic support reduction commitments, Step 2 payments to domestic users are not inconsistent with the United States' WTO obligations.

50. The United States explains that the lack of any reference to domestic content subsidies in Article 13(b) of the *Agreement on Agriculture* does not support the Panel's interpretation. Article 13(b) does not refer to Article 3 of the *SCM Agreement* because the substantive obligation of Article 3.1(b) does not apply to domestic content subsidies in favour of agricultural producers.

51. Consequently, the United States requests that the Appellate Body reverse the Panel's finding that Step 2 payments to domestic users of United States upland cotton are import substitution subsidies that are inconsistent with Articles 3.1(b) and 3.2 of the *SCM Agreement*.

(ii) *To exporters*

52. The United States claims that the Panel erred in concluding that Step 2 payments provided to exporters of United States upland cotton, under Section 1207(a) of the FSRI Act of 2002, are export subsidies covered by Article 9.1(a) of the *Agreement on Agriculture* and, therefore, inconsistent with Articles 3.3 and 8 of that Agreement. The United States also asserts that the Panel erroneously concluded that Step 2 payments to exporters are inconsistent with Articles 3.1(a) and 3.2 of the *SCM Agreement*, because they are not exempted from action by Article 13(c) of the *Agreement on Agriculture*.

53. The United States argues that Step 2 payments are not contingent on export performance because upland cotton does not need to be exported to trigger eligibility; domestic users are also eligible. The program under which Step 2 payments are granted is indifferent as to whether the recipient of the payment is an exporter or a domestic user. Step 2 payments to exporters and domestic users are governed by a single legislative provision and a single set of regulations. The form and payment rate to domestic users and exporters are identical, and payments are made from a unified fund. Rather than being an export-contingent subsidy, the United States reports Step 2 payments as product-specific amber box domestic support for cotton within its AMS.

54. The United States submits that the facts in this case are similar to those before the panel in *Canada – Dairy*, where the panel found that payments contingent on use, without regard to the nature of the use, do not involve an export subsidy for purposes of Articles 9 and 10 of the *Agreement on Agriculture*.⁵⁵ The distinctions drawn by the Panel between the circumstances in this case and those in *Canada – Dairy* are based on a mischaracterization by the Panel of facts in the latter case.⁵⁶ Finally, the United States contends that the Panel's finding in respect of Step 2 payments to *exporters* seems to be based on the Panel's determination to find that Step 2 payments to *domestic users* are a prohibited import substitution subsidy.

55. The United States therefore requests that the Appellate Body reverse the Panel's finding that Step 2 payments to exporters are an export subsidy listed in Article 9.1(a) that is inconsistent with the United States' obligations under Articles 3.3 and 8 of the *Agreement on Agriculture*. The United States also requests that the Appellate Body reverse the Panel's findings that Step 2 payments to exporters are not exempt from action under Article 13(c) of the *Agreement on Agriculture* and are inconsistent with Articles 3.1(a) and 3.2 of the *SCM Agreement*.

(b) Export Credit Guarantees

(i) *Panel's terms of reference*

56. The United States asserts that the Panel erred in concluding that export credit guarantees⁵⁷ to facilitate the export of United States agricultural commodities other than upland cotton were within its

⁵⁵United States' appellant's submission, paras. 444-445 (referring to Panel Report, *Canada – Dairy*, para. 7.41 and footnote 496 to para. 7.124).

⁵⁶*Ibid.*, paras. 447-452 (referring to Panel Report, paras. 7.718 and 7.725).

⁵⁷The export credit guarantees at issue are the General Sales Manager 102 and 103 programs and the Supplier Credit Guarantee Program, which are described *infra*, paras. 586-589. See also Panel Report, paras. 7.236-7.244.

terms of reference. According to the United States, there is a clear progression between the measures included in the request for consultations under Article 4 of the DSU and the measures identified in the request for the establishment of a panel, which forms the basis for a panel's terms of reference.⁵⁸ The United States contends that a measure that is not included in the request for consultations may not form part of a panel's terms of reference.

57. In this case, the United States argues, the Panel erred in finding that Brazil's request for consultations identified export credit guarantees to agricultural commodities other than upland cotton as challenged measures. A plain reading of Brazil's request for consultations does not support the Panel's conclusion. The request identified the challenged measures as "subsidies provided to US producers, users and/or exporters of upland cotton".⁵⁹ Although footnote 1 to this sentence reads "Except with respect to export credit guarantee programs as explained below", none of the subsequent references to export credit guarantees in the request for consultations identified other United States agricultural commodities. Moreover, the statement of evidence attached to Brazil's request for consultations, pursuant to Article 4 of the *SCM Agreement*, did not mention commodities other than upland cotton, providing further proof that the request for consultations did not extend beyond export credit guarantees for upland cotton. That the request for consultations did not include export credit guarantees to other agricultural commodities is confirmed by the fact that Brazil included new language in its request for the establishment of a panel.

58. According to the United States, the Panel also erred in finding that "actual" consultations included export credit guarantees to agricultural commodities other than upland cotton. The fact that Brazil posed written questions to the United States about export credit guarantees for other commodities does not mean that Brazil and the United States held consultations about the topic. Were it otherwise, a complaining party could unilaterally alter the scope of consultations without regard to the requirements of Article 4.4 of the DSU, the time-frames, and the impact on third parties seeking to determine whether to join the consultations. The Panel also ignored the fact that, at the first consultations meeting, the United States expressed the view that Brazil's request with respect to export credit guarantees was clearly limited to upland cotton, and that no discussion of export credit guarantees for any commodity other than upland cotton took place during the consultations. The United States also argues that what is determinative of the scope of consultations is the text of Brazil's request for consultations and not the text of Brazil's written questions.

⁵⁸United States' appellant's submission, para. 466 (referring to Appellate Body Report, *Brazil – Aircraft*, para. 131).

⁵⁹*Ibid.*, para. 457 (quoting the Request for Consultations by Brazil, *supra*, footnote 26).

59. The United States contends that the facts in this case are similar to those in *US – Certain EC Products*. In that case, the Appellate Body found that a particular measure was not part of the panel's terms of reference because it was not the subject of consultations.⁶⁰ Similarly, in this case, export credit guarantees to other agricultural commodities may not form part of the Panel's terms of reference because they were not the subject of consultations.

60. The United States therefore requests that the Appellate Body reverse the Panel's conclusion that export credit guarantees to United States agricultural commodities other than upland cotton were within the Panel's terms of reference. The United States adds that, because the Panel had no authority to make findings with respect to export credit guarantees for agricultural commodities other than upland cotton, all of the Panel's findings with respect to such commodities must also be reversed.

(ii) *Statement of available evidence*

61. The United States submits that the Panel erroneously concluded that Brazil provided a statement of available evidence with respect to export credit guarantee measures relating to United States agricultural commodities other than upland cotton, as required by Article 4.2 of the *SCM Agreement*.

62. The United States explains that the statement of evidence that was annexed to Brazil's request for consultations contains two paragraphs specifically referring to the United States' export credit guarantee programs. The Panel correctly noted that the first paragraph is textually limited to upland cotton.⁶¹ The United States submits, however, that the Panel failed to draw the proper conclusion about the second paragraph. Although the second paragraph does not refer to upland cotton, it contains no suggestion that it expands on the programs described in the preceding paragraph, which refers to export credit guarantee programs that allegedly provide certain benefits to United States upland cotton. In the context of the paragraph that precedes it, the second paragraph must be understood to refer to the same programs—that is, to export credit guarantee programs that allegedly provide certain benefits to upland cotton. In addition, the United States points out that the second paragraph in Brazil's request for consultations does not refer to any commodity. Consequently, even if the second paragraph is construed to refer to programs that provide benefits to products other than cotton, it is difficult to see how that paragraph meets the requirements of Article 4.2 of the

⁶⁰United States' appellant's submission, para. 485 (referring to Appellate Body Report, *US – Certain EC Products*, para. 70).

⁶¹*Ibid.*, para. 495 (referring to Panel Report, para. 7.84).

SCM Agreement, as it does not provide information about the "existence" or "nature" of the subsidies allegedly provided by the export credit guarantee programs to products other than upland cotton.

63. The United States therefore requests that the Appellate Body reverse the Panel's finding and that it find, instead, that Brazil did not provide a statement of available evidence with respect to the United States' export credit guarantee programs as they relate to agricultural commodities other than upland cotton.

(iii) *Article 10.2 of the Agreement on Agriculture*

64. The United States alleges that the Panel erred in finding that the United States' export credit guarantee programs in respect of exports of upland cotton and other unscheduled agricultural products, and in respect of one scheduled product (i.e., rice), are export subsidies applied in a manner that results in circumvention of the United States' export subsidy commitments within the meaning of Article 10 of the *Agreement on Agriculture* and are therefore inconsistent with Article 8 of that Agreement. In addition, the United States submits that, although the Panel did not find that the United States had circumvented such commitments with respect to scheduled commodities other than rice, it nevertheless erred in concluding that the programs as applied to these scheduled agricultural products constitute export subsidies within the meaning of the *Agreement on Agriculture*.

65. The United States contends that the Panel erroneously analyzed whether export credit guarantees are export subsidies subject to the disciplines of Article 10.1 solely by reference to the *SCM Agreement*, ignoring important context in Article 10 of the *Agreement on Agriculture*. According to the United States, the proper context in which to analyze the meaning of Article 10.1 with respect to export credit guarantees is Article 10.2 of the *Agreement on Agriculture*, the only provision that explicitly addresses these specific kinds of measures. Article 10.2 reflects the fact that, during the Uruguay Round, WTO Members did not agree on disciplines applicable to agricultural export credits, export credit guarantees, or insurance programs. Unable to reach agreement on such disciplines within the Uruguay Round, WTO Members opted to continue discussions, deferring the imposition of substantive disciplines until a consensus was achieved.

66. According to the United States, this interpretation of Article 10.2 is consistent with Article 10 as a whole. Article 10.2 contributes to the prevention of circumvention of export subsidy commitments by imposing two obligations on Members: first, they must undertake to work toward the development of internationally agreed disciplines on export credit guarantees; and, second, "after agreement on such disciplines", they must provide export credit guarantees "only in conformity

therewith".⁶² Moreover, excluding export credit guarantees from the application of Article 10.1 is consistent with the treatment of food aid transactions under Article 10. Because Article 10.4 of the *Agreement on Agriculture* does not explicitly exempt food aid transactions from the applicability of Article 10.1, the Panel's interpretative approach would mean that all food aid transactions constitute export subsidies under Article 10.1.

67. The United States submits that the negotiating history confirms its interpretation that Article 10.2 excludes export credit guarantees from the export subsidy disciplines in Article 10.1. The negotiating history reflects that WTO Members initially included export credit guarantees as a subject for negotiation but later specifically elected not to include those practices as exports subsidies in respect of goods covered by the *Agreement on Agriculture*. The Panel's explanation that the negotiators deleted the language on export credits from a 1991 draft of Article 9 because it was "mere surplusage"⁶³ is inconsistent with the fact that other practices included in the Illustrative List of Export Subsidies of the *SCM Agreement* were also listed in Article 9.1 of the *Agreement on Agriculture*, such as direct subsidies contingent upon export performance, or transport and freight charges provided at more favourable rates.

68. The United States argues that reliance on the negotiating history in this case is appropriate, under Article 32 of the *Vienna Convention on the Law of Treaties* (the "*Vienna Convention*"⁶⁴), because the Panel's interpretation leads to a manifestly unreasonable result. Had export credit guarantees remained in Article 9, then the United States and other providers of export credit guarantees would have been expressly permitted to include such measures in their respective export subsidy reduction commitments. In the absence of a reference in Article 9, the United States was foreclosed from including them. It defies logic, as well as the object and purpose of the *Agreement on Agriculture*, to take the view of the Panel whereby such measures would be treated as already disciplined export subsidies, yet such measures would not be permitted to be included within the applicable reduction commitments expressly contemplated by the text.

69. The United States also requests that the Appellate Body reverse the Panel's finding that export credit guarantees for agricultural commodities are subject to Articles 3.1 and 3.2 of the *SCM Agreement*. The United States explains that export credit guarantees are not listed in Article 9.1 of the *Agreement on Agriculture* and are exempt, through the operation of Article 10.2, from the export subsidy disciplines in Article 10.1. Because export credit guarantees are not subject to export subsidy disciplines under the *Agreement on Agriculture*, the export subsidy disciplines of the

⁶²Quoting from Article 10.2 of the *Agreement on Agriculture*.

⁶³United States' appellant's submission, para. 379 (quoting Panel Report, para. 7.940).

⁶⁴Done at Vienna, 23 May 1969, 1155 U.N.T.S. 331; 8 International Legal Materials 679.

SCM Agreement are also inapplicable to these measures pursuant to Article 21.1 of the *Agreement on Agriculture* and the introductory language of Article 3.1 of the *SCM Agreement*.

(iv) *Burden of proof*

70. The United States submits that the Panel erred in three different ways in respect of the application of the burden of proof in assessing the United States' export credit guarantee programs under item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement*.

71. First, the United States asserts that the Panel erred by applying the "special rules" on burden of proof provided in Article 10.3 of the *Agreement on Agriculture* in its examination of Brazil's claim under the *SCM Agreement*. The United States argues that the special rules in Article 10.3 of the *Agreement on Agriculture* do not apply in the context of the *SCM Agreement*.

72. In addition, the United States submits that the Panel erred by applying the special rules on burden of proof in Article 10.3 of the *Agreement on Agriculture* in examining whether the United States circumvented its export subsidy commitments with respect to upland cotton and certain other *unscheduled* agricultural products. According to the United States, Article 10.3 does not apply at all in respect of export subsidies to an agricultural good for which the respondent has no reduction commitments.

73. Finally, the United States refers to three specific instances in which the Panel allegedly erred in applying the burden of proof. The first example is the Panel's statement that the premiums charged by the Commodity Credit Corporation (the "CCC") for the export credit guarantees "are not geared toward *ensuring* adequacy to cover long-term operating costs and losses for the purposes of item (j)".⁶⁵ The United States asserts that this is a much higher threshold than that provided in the text of item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement*. Next, the United States takes issue with the Panel's statements that "[i]n terms of the structure, design and operation of the ... programmes [we] believe that the programmes are not designed to avoid a net cost to government"⁶⁶ and that the Panel was entitled to inquire whether revenue "would be likely to cover the total of all operating costs and losses under the programme".⁶⁷ According to the United States, "[t]o 'avoid a net cost' prospectively is simply not the requirement of item (j)", and the "likelihood"

⁶⁵United States' appellant's submission, para. 406 (quoting Panel Report, para. 7.859). (emphasis added by the United States)

⁶⁶*Ibid.*, para. 407 (quoting Panel Report, para. 7.857).

⁶⁷*Ibid.*, para. 407 (quoting Panel Report, para. 7.805).

standard of performance" imposed by the Panel is higher than that found in item (j).⁶⁸ The third example cited by the United States is the Panel's statement that "[w]e have not been persuaded that cohort re-estimates over time, will *necessarily* not give rise to a net cost to the United States government."⁶⁹ The United States contends, however, that under the applicable burden of proof it is not for the United States to make such incontrovertible demonstrations to the Panel.

(v) *Necessary findings of fact*

74. The United States asserts that the Panel erred by failing to make certain factual findings that were necessary for the Panel's analysis of whether premiums are adequate to cover the long-term costs and losses of the United States' export credit guarantee programs, under item (j) of the Illustrative List of Export Subsidies. According to the United States, the Panel made no findings "on the basis for and monetary extent to which the United States has allegedly not covered its long-term operating costs and losses for the CCC export credit guarantee programs".⁷⁰

75. In particular, the United States asserts that the Panel should have made a specific finding on the treatment of rescheduled debt. The United States explains that the Panel did not conclude that rescheduled debt was an operating cost or loss. Instead, the Panel "stated only vaguely" that it shared Brazil's concern that the United States' treatment of rescheduled debt understates the net cost to the United States government associated with the export credit guarantee programs.⁷¹

76. The United States argues that the Panel's failure to make these factual findings compels the reversal of the Panel's determination in respect of item (j) of the Illustrative List of Export Subsidies.

B. *Arguments of Brazil – Appellee*

1. Domestic Support

(a) Terms of Reference – Expired Measures

77. Brazil submits that the Appellate Body should reject the United States' request to reverse the Panel's finding that expired production flexibility contract and market loss assistance payments were

⁶⁸United States' appellant's submission, para. 407.

⁶⁹*Ibid.*, para. 408 (quoting Panel Report, para. 7.853). (emphasis added by the United States) In the same paragraph, the United States mentions the following statement by the Panel: "[w]hile there may be a possibility (based on the experience of certain of other cohorts) that this figure may diminish over the lifetime of the cohort concerned, there is no assurance that this figure will *necessarily* evolve towards, and conclude as, zero or a negative figure." (Panel Report, footnote 1028 to para. 7.853) (emphasis added by the United States)

⁷⁰United States' appellant's submission, para. 419.

⁷¹*Ibid.*, para. 416.

outside the Panel's terms of reference. Brazil argues that neither Article 4.2 nor Article 6.2 of the DSU precludes a panel from analyzing payments made in the past in the context of serious prejudice claims. Brazil focuses on the context provided by Article 3.3 of the DSU, which states that a purpose of dispute settlement is the "prompt settlement of situations in which a Member considers that any benefits accruing to it ... are being impaired by measures taken by another Member". For Brazil, as long as the impairment is current, then the status in domestic law of the measure causing impairment is irrelevant.

78. Brazil notes that the current case involves allegations of "adverse effects" and "serious prejudice" under the provisions of the *SCM Agreement* and the GATT 1994. A breach of these provisions does not necessarily arise when an actionable subsidy is granted, but only when adverse effects occur, and the breach continues for the entire period during which the adverse effects continue. The effects of an actionable subsidy, which "affect[] the operation of" the *SCM Agreement* in the sense of Article 4.2 of the DSU, may well linger even after the measure providing for the subsidy expires. There is thus no basis for the United States' claim that the subsidies in question "cannot" be measures affecting the operation of any covered agreement. In particular, there is no justification in this context for the distinction, drawn by the United States, between recurring and non-recurring subsidies. The inquiry as to whether a subsidy continues to cause adverse effects beyond the year in which it was granted is a substantive judgment, and cannot be treated as a "jurisdictional hurdle".⁷² Brazil finds support for its position in the view of the panel in *Indonesia – Autos*, which found that past, present, and future subsidies can be the subject of dispute settlement, as the effect of such measures may cause serious prejudice to the interests of a Member.

79. Brazil also disputes the United States' claims regarding Article 12.7 of the DSU. In Brazil's view, the Panel fulfilled the requirements of Article 12.7 in its Report. Many of the United States' claims under Article 12.7 are, in reality, allegations of error concerning the Panel's exercise of its discretion under Article 11 of the DSU and should be dismissed for want of specification of a claim under that provision.

(b) Article 13(a) of the *Agreement on Agriculture – Planting Flexibility Limitations*

80. Brazil considers that production flexibility contract and direct payment programs are not green box measures falling under Annex 2 of the *Agreement on Agriculture* and are thus not exempt from actions pursuant to Article 13(a) of that Agreement. Brazil requests the Appellate Body to

⁷²Brazil's appellee's submission, para. 255.

uphold the Panel's finding, under paragraph 6(b) of Annex 2, that production flexibility contract payments under the FAIR Act of 1996⁷³ and direct payments under the FSRJ Act of 2002 relate the amount of the payment to the type of production undertaken by recipients because these payments are made solely if a producer grows crops other than fruits and vegetables (and, in the case of direct payments, wild rice as well).

81. Brazil relies upon the Panel's finding that paragraph 6(b) of Annex 2 addresses both positive requirements that certain products be produced and negative requirements that certain products not be produced. Brazil submits that the Panel correctly held that the words "related to," in paragraph 6(b) of Annex 2, preclude the establishment of any kind of relationship between the amount of a payment and the type of production undertaken. Accordingly, the text requires that the amount of a decoupled payment not be affected, influenced, or dependent, in any way, upon the type of crop planted. Brazil contends that the United States inappropriately seeks to read into paragraph 6(b) an exception for planting restrictions. Brazil observes that where the drafters intended to provide such an exception, they did so explicitly, as is evidenced by paragraphs 11(b) and 11(e) of Annex 2. For Brazil, Annex 2 cannot simply be reduced to the proposition that a measure is exempt if it is consistent with the fundamental requirement established in paragraph 1 that such measures have no, or at most minimal, trade-distorting effects or effects on production. Such an interpretation would overlook the policy-specific criteria in the other paragraphs of Annex 2.

82. Brazil nevertheless agrees with the United States that the expression in paragraph 6(b) "related to ... the type ... of production" does not preclude a Member from making decoupled payments conditional upon producers undertaking no production at all. Brazil highlights, however, that a total ban on production is different from a partial ban, because payment is conditional upon the planting of certain crops as opposed to others. The Panel's factual findings support this view: the Panel found that the planting flexibility limitations impose a "significant constraint" on production decisions.⁷⁴ Brazil argues that, under the production flexibility contract and direct payment measures, the amount of payment is always "related to" the type of production undertaken. If permitted crop "types" are produced exclusively, a full payment is made. If a small quantity of "prohibited" crops is produced, the amount of payment is reduced. If a larger quantity of prohibited crops is produced, no payment is made.

83. Furthermore, the various findings by the Panel contradict the United States' basic assertion that "a condition that a recipient not produce certain products serves the fundamental requirement of

⁷³Federal Agriculture Improvement and Reform Act of 1996 (the "FAIR Act of 1996"); Public Law 104-127.

⁷⁴Brazil's appellee's submission, para. 287 (quoting Panel Report, para. 7.386).

Annex 2, that measures have no more than minimal trade-distorting effects and effects on production.⁷⁵ Rather, a partial prohibition creates incentives for the production of certain crops, and disincentives for the production of prohibited crops. In essence, the Panel found that planting flexibility limitations *did* channel production away from fruits, vegetables (and wild rice) and towards other commodities, such as upland cotton. Brazil thus disputes the distinction put forward by the United States between measures that make payment contingent upon the production of "permitted" crops and those that make payment contingent upon the non-production of "prohibited" crops. As the Panel found on the facts of this case, their effects are the same. The Panel found that "the planting flexibility limitations provide a monetary incentive for payment recipients not to produce the prohibited crops"⁷⁶, and that production flexibility contract payments and direct payments have positive production effects by restricting production choices and keeping land dedicated to the production of the permitted crops. Thus, providing income support, whilst also excluding income support when certain types of crop are produced, relates the amount of the income support to the type of production undertaken within the meaning of paragraph 6(b).

84. Finally, Brazil takes issue with the United States' assertion that the Panel's interpretation would require a Member to make decoupled income support payments even if the recipient produced illegal crops or crops damaging to the environment. There was no basis for the Panel to address this issue because the planting flexibility limitations at issue do not pertain to the production of illegal or environmentally-damaging crops. In any event, nothing in the *Agreement on Agriculture* suggests that the word "production" means anything other than *lawful* production. The Panel properly declined to consider the hypothetical situations not created by the United States' measures at issue in the dispute.

(c) Article 13(b) of the *Agreement on Agriculture*

85. Brazil submits that the United States' non-green box domestic support measures are not exempt from actions by virtue of Article 13(b)(ii) of the *Agreement on Agriculture*, and asks the Appellate Body to uphold the Panel's finding that the United States granted implementation period support to upland cotton in excess of that decided in the 1992 marketing year, within the meaning of that provision. Brazil argues that the Panel's interpretation of Article 13(b)(ii) was consistent with its ordinary meaning, context and object and purpose, and that the methodological choices made by the Panel in undertaking the comparison required by Article 13(b)(ii) were reasonable and within the bounds of its discretion as the trier of fact.

⁷⁵Brazil's appellee's submission, para. 291 (quoting the United States' appellant's submission, para. 22).

⁷⁶*Ibid.*, para. 320 (quoting Panel Report, para. 7.386).

(i) *Interpretation of "support to a specific commodity"*

86. Brazil contends that the Panel correctly interpreted the phrase "support to a specific commodity" in Article 13(b)(ii) of the *Agreement on Agriculture* to mean "all non-green box support measures that clearly or explicitly define a commodity as one to which they bestow or confer support".⁷⁷ This includes crop insurance and the three subsidies described by the United States as "product-specific" domestic support (marketing loan program payments, Step 2 payments, and cottonseed payments), as well as the four measures characterized by the United States as "decoupled" payments (production flexibility contract payments, direct payments, market loss assistance, and counter-cyclical payments).

87. Brazil submits that the United States' interpretation of the phrase "support to a specific commodity" in Article 13(b)(ii) of the *Agreement on Agriculture* is that support falling within the proviso to Article 13(b)(ii) must require production of only one specific crop. Brazil observes that this argument was rejected by the Panel, which concluded that nothing in the text of Article 13(b)(ii) suggests that relevant measures must provide support only to a single commodity, and noted that a single measure could provide support to multiple specific commodities. Brazil agrees with the Panel that "[i]f a measure specifies more than one commodity, it would be appropriate to measure the amount of support granted to each of them in accordance with the terms of the measure itself."⁷⁸ The practical effect of the extremely narrow United States reading of Article 13(b)(ii) is to erase US \$4.2 billion in production flexibility contract payments, direct payments, market loss assistance, and counter-cyclical payments to recipients who actually grew upland cotton in the 1999-2002 marketing years, even though these four subsidies covered a significant portion of upland cotton producers' costs of production during this period. Brazil contends that the crucial conclusion drawn by the Panel from this data was a clear linkage between historic upland cotton producers and present upland cotton producers. The Panel found that "the overwhelming majority of farms enrolled in the programmes which plant upland cotton also hold upland cotton base", specifically, 96.1 per cent in the 2002 marketing year.⁷⁹ For Brazil, the evidence on record and the Panel's findings contradict the United States' factual assertions that there is no connection between current payments under the production flexibility contract, direct payment, market loss assistance, and counter-cyclical payment programs on the one hand, and current upland cotton production on the other.

88. Brazil agrees with the Panel's conclusion that the deliberate decision of the drafters *not* to use in Article 13(b)(ii) readily available terms, such as "product-specific" and "non-product-specific"

⁷⁷Brazil's appellee's submission, para. 358 (quoting Panel Report, para. 7.494).

⁷⁸*Ibid.*, para. 371 (quoting Panel Report, para. 7.483).

⁷⁹*Ibid.*, para. 383 (quoting Panel Report, para. 7.636).

(and the definitions in Articles 1(a) and (h) of the *Agreement on Agriculture*) means that the drafters intended the term "support to a specific commodity" to have a unique meaning. The Panel properly found that this unique phrase does not mean "product-specific domestic support" because "the class of measures which is covered by paragraph (b) [of Article 13] is broader than either" that term or the phrase "support ... provided for an agricultural product in favour of the producers".⁸⁰ The Panel correctly focused on the fact that the term "support to a specific commodity" in Article 13(b)(ii) refers to *all* measures set out in the chapeau to Article 13(b). There was therefore no basis in the text to limit the measures covered by Article 13(b)(ii) solely to measures requiring production of a single commodity. Brazil adds that such an interpretation would be contrary to the object and purpose of the *Agreement on Agriculture*, creating a new category of trade-distorting domestic support that would evade the limits set by the Members for exempting domestic support measures from actions under the *SCM Agreement* and the GATT 1994. Under the United States' interpretation, as long as measures do not require production of a *single* commodity, they would *never* be counted as implementation period support for purposes of the peace clause comparison, effectively insulating such measures from serious prejudice actions.

305 89. In addressing the manner in which the value of support under the production flexibility contract, market loss assistance, direct payment, and counter-cyclical payment programs should be calculated, Brazil submits that the Appellate Body should be wary of setting the evidentiary bar too high for complaining Members seeking to demonstrate precise amounts of support to a specific commodity for purposes of Article 13(b)(ii). Brazil contends that the Appellate Body should affirm the Panel's use of the total budgetary outlays to upland cotton base acres. Brazil observes, however, that the Panel endorsed in the "Attachment to Section VII-D" two other approaches for allocating implementation period support under these programs to upland cotton: the "cotton-to-cotton" methodology and "Brazil's methodology". Brazil maintains that, under any of these approaches, the United States granted support to upland cotton in the years 1999, 2000, 2001, and 2002 in excess of that decided during the 1992 marketing year.

(ii) *Calculation methodology for price-based measures*

90. In addressing the United States' arguments regarding the appropriate methodology for calculating the value of certain United States price-based measures (the marketing loan program payments and deficiency payments), Brazil agrees with the Panel that "the use of the verb 'decided' stands in contrast to the use of the verb 'grant' in relation to the same noun 'support' in the same

proviso."⁸¹ The Panel found that "despite the contrast, the proviso calls for a comparison which necessarily requires the two halves of the comparison to be expressed in the same units of measurement."⁸² The Panel further noted that "[a] difference between the support that a government decides and the support that its measures grant is that one is expressed in terms of prior determinations of levels of support and the other in terms of subsequent support provided."⁸³ The Panel concluded by stating that "[d]ecided" refers to what the government determines, but 'grant' refers to what its measures provide."⁸⁴ Brazil submits that the Panel's explanation and reasoning for its interpretation are consistent with the ordinary meaning of the term in its context, and are supported by the Appellate Body's decision in *Brazil – Aircraft*.

91. Brazil contends that the United States incorrectly implies that the Panel agreed with the United States that the peace clause proviso "compares the support a Member determines through its measures, not 'support [that] was spent due to reasons beyond the control of the government'".⁸⁵ Brazil argues that the Panel explicitly rejected this contention and concluded that "the text indicates that implementation period support must be measured in terms of support that measures 'grant', rather than what was budgeted or *estimated*."⁸⁶

92. Against this background, Brazil argues that the plain text of paragraph 10 of Annex 3 to the *Agreement on Agriculture* permits the use of *either* a budgetary outlay *or* a price gap methodology for calculating the value of price-based payments. There is no textual basis for concluding, for purposes of the peace clause, that only price gap methodology may be used. Brazil also notes the Panel's factual finding that the United States adopted a budgetary outlay methodology in accounting for marketing loan program payments in its AMS notifications. Brazil observes that when the United States agreed with other WTO Members on its base level AMS, the United States chose to calculate marketing loan program payments using a budgetary outlay methodology. Brazil argues that the United States' decision to use budgetary outlays instead of price gap methodology for notifying the value of marketing loan program payments is legally binding on the United States. This conclusion follows from the text of Articles 6.3 and 3.2 of the *Agreement on Agriculture*. Nothing in Article 6 or any other provision of the *Agreement on Agriculture* permits a Member to change the methodology

⁸¹ Brazil's appellee's submission, para. 340 (quoting Panel Report, para. 7.435).

⁸² Panel Report, para. 7.435.

⁸³ *Ibid.*, para. 7.436.

⁸⁴ *Ibid.*, para. 7.476.

⁸⁵ Brazil's appellee's submission, para. 346 (quoting the United States' appellant's submission, para. 66).

⁸⁶ *Ibid.*, para. 346 (quoting Panel Report, para. 7.557). (emphasis added by Brazil)

used to calculate the value of price-based measures, once that methodology has been used in AMS notifications.

93. Brazil also notes that, although the Panel primarily relied on a budgetary outlay methodology, it also made alternative factual findings regarding the use of price gap methodology for the calculation of marketing loan program payments in the implementation period and for the 1992 benchmark period, as well as for deficiency payments in the 1992 benchmark period only. Brazil highlights the Panel's finding that under *either* approach the United States grants support to upland cotton in excess of that decided in the 1992 marketing year; the Panel found that "both methodologies lead to the same result."⁸⁷ As a result, even if the legal grounds for the United States' appeal were valid, the facts on record would require the Appellate Body to uphold the Panel's conclusions that the United States granted support in each of the 1999-2002 marketing years that exceeded the "support decided during the 1992 marketing year".

2. Serious Prejudice

(a) Significant Price Suppression under Article 6.3(c) of the *SCM Agreement*

94. Brazil submits that the Panel properly found that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*. Brazil asks the Appellate Body to uphold this finding, and to find that the Panel set out the findings of fact, the applicability of relevant provisions, and the basic rationale behind this finding, as required by Article 12.7 of the DSU. Brazil argues that many of the United States' arguments⁸⁸, and particularly those concerning serious prejudice, involve allegations that the Panel failed to "make an objective assessment of the matter before it, including an objective assessment of the facts of the case" pursuant to Article 11 of the DSU. Brazil requests the Appellate Body to ignore these arguments because the United States has not made a proper claim of error under Article 11 of the DSU.

95. First, in response to the United States' argument that the market in which a panel assesses significant price suppression under Article 6.3(c) cannot be a "world market", Brazil maintains that the subsidized and like products must be present in the market examined. Brazil submits that the ordinary meaning of the text of Article 6.3(c) of the *SCM Agreement* indicates that this provision

"may apply to *any* 'market,' from local to global, and everything in between".⁸⁹ This contrasts with paragraphs (a), (b), and (d) of Article 6.3, which expressly qualify the type of market at issue. It is also consistent with the object and purpose of the *Marrakesh Agreement Establishing the World Trade Organization* (the "*WTO Agreement*") (which addresses barriers to "world trade") and the *Agreement on Agriculture* (which addresses "world agricultural markets").⁹⁰ Brazil maintains that the Panel found, as a matter of fact, that a world market exists for upland cotton.⁹¹ In addition, contrary to the assertion of the United States, Brazil contends that the Panel did find that United States and Brazilian cotton are present in the world market.⁹² However, Brazil agrees with the Panel that the existence of a world market does not preclude the possibility of other markets, and that a world market does not necessarily exist for all products. Brazil refutes the United States' suggestion that the Panel did not find that *Brazilian* prices in the world market for upland cotton were significantly suppressed.⁹³ In Brazil's view, the Panel found that "Brazilian prices, *i.e.*, prices in Brazil and prices received for Brazilian exports, are significantly suppressed".⁹⁴

96. Secondly, in relation to the United States' allegation that the Panel used circular reasoning to find "significant price suppression", Brazil emphasizes that several factors relate to both the "effect of the subsidy" and "significant price suppression", and the Panel gave separate explanations of these factors in terms of the "effect" and the "suppression". Brazil states that the Panel did take into account supply responses from third countries that would flow from removal of the price-contingent subsidies, in taking into account econometric models that incorporated such supply responses.⁹⁵ Brazil also states that the Panel examined the ordinary meaning of the word "significant", properly concluded that it is the degree of price suppression that matters rather than the degree of significance, and provided substantial reasons for its conclusion that the degree of price suppression it had found in the present dispute was significant.

97. Thirdly, in relation to the United States' challenge to the Panel's finding of the "effect" of the price-contingent subsidies, Brazil points out that the Panel did examine the United States' arguments regarding the "farmer's planting decision" and the responsiveness of United States producers to price

⁸⁸Brazil's appellee's submission, para. 628. (original emphasis)

⁸⁹*Ibid.*, para. 633. (emphasis omitted)

⁹⁰*Ibid.*, paras. 619 and 622 (referring to Panel Report, paras. 7.1274 and 7.1311).

⁹¹*Ibid.*, paras. 644 and 808 (referring to Panel Report, paras. 7.1266, 7.1282-7.1284 and 7.1313).

⁹²*Ibid.*, paras. 799-801 (referring to Panel Report, paras 7.1311 and 7.1313).

⁹³*Ibid.*, para. 802.

⁹⁴*Ibid.*, paras. 793-798 (referring to Panel Report, paras. 7.1205, 7.1209, and 7.1215).

⁸⁷Panel Report, para. 7.555.

⁸⁸Brazil lists the relevant arguments in Annex A of its appellee's submission.

signals.⁹⁶ Brazil explains that United States upland cotton farmers base planting decisions on expected net returns, meaning expected market prices together with expected government support. According to Brazil, the record contains ample evidence to support the Panel's view that the United States exercises a significant influence on the world market price for upland cotton. Even if movements in planted upland cotton acreage of United States producers correspond with those of other producers (which Brazil disputes), this would not detract from the Panel's finding that the overall level of upland cotton production by United States producers would be significantly lower in the absence of the price-contingent subsidies. The Panel properly assessed the nature of the price-contingent subsidies and properly found a temporal coincidence between those payments and suppressed upland cotton prices, based not merely on the end points of the 1998-2001 marketing year period, but on more detailed data. Finally, Brazil maintains that the Panel properly found that United States upland cotton producers were able to continue to produce upland cotton by virtue of the price-contingent subsidies. Although variable costs may be most relevant in the short term, the Panel found that upland cotton producers must cover their total costs of production in the mid- to long-term. According to Brazil, the fact that United States producers might have been able to cover the costs of upland cotton production through other agricultural production as well as "off-farm income"⁹⁷ is irrelevant to the question of the effect of the price-contingent subsidies on the United States industry producing upland cotton.

98. Fourthly, in response to the United States' arguments regarding the quantification of subsidies, Brazil states that neither the text nor the context of Articles 5(c) and 6.3 of the *SCM Agreement* imposes a "preliminary requirement to quantify exactly the amount of each subsidy prior to examining whether it causes adverse effects".⁹⁸ Brazil supports its interpretation by reference to Article 6.1(a) and Annex IV of the *SCM Agreement*, which, unlike Article 6.3, impose quantification methodologies. Brazil also distinguishes the analysis required under Part III of the *SCM Agreement* from that required under Part V of that Agreement. Under Part V, it is necessary to calculate the exact amount of subsidization in order to avoid imposing excess countervailing duties. However, the remedy under Part III focuses on the effects of the subsidy, rather than the imposition of duties, and, according to Brazil, the size of a subsidy does not necessarily determine its effects. Finally, Brazil contests the United States' reliance on Annex V of the *SCM Agreement*. In Brazil's view, Annex V sets out procedures for the collection of information and does not require the Panel to

⁹⁶Brazil's appellee's submission, para. 168 (referring to the United States' appellant's submission, para. 324).

⁹⁷*Ibid.*, para. 788 (referring to the United States' appellant's submission, para. 224).

⁹⁸*Ibid.*, para. 467.

use such information, and the references to an "amount" in paragraphs 2 and 5 of Annex V are directed towards Article 6.1(a) rather than Article 6.3 of the *SCM Agreement*.

99. In response to the United States' arguments regarding the allocation of counter-cyclical payments and market loss assistance payments to upland cotton, Brazil argues that the methodology in Annex IV of the *SCM Agreement* applies only to Article 6.1 and not to Article 6.3(c), and that Annex IV has now expired. In any case, the Panel did find a "strongly positive relationship" between those payments and the production of upland cotton.⁹⁹

100. Brazil contends that the United States' arguments distinguishing between "raw" and "processed" cotton improperly raise new factual and legal issues not before the Panel, including a suggestion that raw cotton is a product distinct from processed cotton. Brazil submits that the Panel found, and the parties agreed, that upland cotton lint is the only subsidized product at issue in this dispute. Moreover, according to Brazil, the Panel found that all price-contingent subsidies benefited the subsidized product (upland cotton), regardless of the stage at which they were provided. Brazil rejects the United States' reliance on the Appellate Body Report in *US – Softwood Lumber IV*.

101. Finally, Brazil responds to the United States' arguments as to the allocation of recurring subsidies to a particular year as follows. Articles 5(c) and 6.3 of the *SCM Agreement* do not explicitly exempt consideration of effects of annually recurring subsidies beyond the year in which they are paid. Furthermore, the United States' interpretation would create a new category of non-actionable subsidies. For example, according to Brazil, the United States' argument would exclude all the subsidies challenged by Brazil because they would be deemed to have no effects after 1 August 2003, well before the Panel circulated its Report. The possibility of making an "as such" claim against the subsidy programs as a whole would provide little comfort because these types of claims can be difficult to prove. Brazil also suggests that "WTO Members provide agricultural subsidies largely on a recurring annual basis"¹⁰⁰ and, therefore, one would have expected an explicit exclusion of such subsidies from the disciplines of particularly Part III of the *SCM Agreement* and the *Agreement on Agriculture* if this were the intention of the drafters. The United States' contrary assertion improperly excludes the possibility for Members to seek the removal of adverse effects of any subsidies (whether recurring or otherwise), as reflected in Article 7.8 of the *SCM Agreement*.

102. In relation to the findings that the Panel made regarding the subsidies at issue in this dispute, Brazil challenges the United States' contention that the Panel made no findings regarding the effects in marketing year 2002 of subsidies paid in marketing years 1999 to 2001. The Panel explained its

⁹⁹Brazil's appellee's submission, para. 523 (quoting Panel Report, para. 7.1226).

¹⁰⁰*Ibid.*, para. 559.

decision to examine serious prejudice over a period including marketing year 2002, and its findings indicate that it regarded the effects of certain subsidies as continuing in that year. In addition, Brazil submits that no "bright lines"¹⁰¹ can be drawn between upland cotton subsidies paid in different marketing years, because the marketing year runs from 1 August to 31 July, and upland cotton is planted in one marketing year and harvested in the next.

3. Import Substitution Subsidies and Export Subsidies

(a) Step 2 Payments

(i) *To domestic users*

103. Brazil requests that the Appellate Body uphold the Panel's conclusion that Step 2 payments to domestic users of United States upland cotton, provided under Section 1207(a) of the FSRI Act of 2002, are inconsistent with Articles 3.1(b) and 3.2 of the *SCM Agreement*. Brazil submits that the Panel correctly held that the *Agreement on Agriculture* and the *SCM Agreement* apply cumulatively, unless there is an exception or a conflict. Such an exception must be explicitly stated.¹⁰² According to Brazil, in *EC – Bananas III*, the Appellate Body found that the *Agreement on Agriculture* permits inconsistencies with obligations in other covered agreements solely if this is "explicitly" stated in the text.¹⁰³ Similarly, an explicit exception would be required for the *Agreement on Agriculture* to exempt certain measures from the prohibition in Article 3.1(b) of the *SCM Agreement*.

104. Brazil contends that no such exception is provided in the *Agreement on Agriculture* or in the *SCM Agreement*. The introductory phrase in Article 3.1 of the *SCM Agreement* ("[e]xcept as provided in the Agreement on Agriculture") does not mean that Article 3.1 does not apply to domestic support measures conforming to the *Agreement on Agriculture*; instead, it confirms that Article 3.1 of the *SCM Agreement* applies unless it conflicts with specific provisions of the *Agreement on Agriculture*. This interpretation is confirmed by Article 21.1 of the *Agreement on Agriculture* and by the absence of any exception in Article 13 of the *Agreement on Agriculture* regarding Article 3.1(b).

105. Brazil asserts that, under the *Agreement on Agriculture*, WTO Members are entitled to grant domestic support in favour of agricultural producers. However, this does not create a conflict with Article 3.1(b) of the *SCM Agreement*, because it is perfectly possible for Members to grant domestic

¹⁰¹ Brazil's appellee's submission, para. 570.

¹⁰² *Ibid.*, para. 832 (referring to Appellate Body Report, *US – Cotton Yarn*, para. 120).

¹⁰³ *Ibid.*, para. 833 (referring to Appellate Body Report, *EC – Bananas III*, para. 157).

support without making payments contingent on domestic content. In other words, Members can fully enjoy their right to grant domestic support and still comply with Article 3.1(b) of the *SCM Agreement*. This interpretation is consistent with a primary objective of the WTO agreements, namely, avoiding discrimination under the national treatment rule. It is also consistent with an adopted GATT panel report regarding a domestic support measure to agricultural producers that was contingent on the purchase of domestic goods. That panel recognized that the GATT contracting parties were entitled to grant support to agricultural producers but found that this could be done without granting domestic content subsidies.¹⁰⁴ The panel held that a domestic content subsidy in favour of agricultural producers was inconsistent with Article III:4 of the GATT 1947. Therefore, Brazil contends that domestic support under the *Agreement on Agriculture* can and must be granted consistently with Article 3.1(b) of the *SCM Agreement*.

(ii) *To exporters*

106. Brazil requests the Appellate Body to uphold the Panel's findings that Step 2 payments to exporters of United States upland cotton are contingent upon export performance and, consequently, are inconsistent with Articles 3.3 and 8 of the *Agreement on Agriculture* and are prohibited under Articles 3.1(a) and 3.2 of the *SCM Agreement*.

107. Brazil agrees with the Panel that the principles set out by the Appellate Body in *US – FSC (Article 21.5 – EC)* apply to Step 2 payments to exporters.¹⁰⁵ In one situation under the Step 2 measure, proof of exportation is required as a condition of payment. This export contingency is not dissolved because the payment can also be made in another situation, on other conditions.

108. Brazil adds that, contrary to the United States' argument on appeal, this is not a measure that establishes a single set of conditions applying to all upland cotton produced in the United States.¹⁰⁶ On its own terms, the measure does not apply to all United States production of upland cotton. Instead, the measure carves out of that overall production two classes of upland cotton that may, on certain conditions, receive subsidies. In so doing, the measure targets two well-defined classes of

¹⁰⁴ Brazil's appellee's submission, para. 860 (referring to GATT Panel Report, *Italy – Agricultural Machinery*, para. 16).

¹⁰⁵ *Ibid.*, paras. 881-884 (referring to Appellate Body Report, *US – FSC (Article 21.5 – EC)*, paras. 113 and 119 and Appellate Body Report, *Canada – Aircraft*, para. 179).

¹⁰⁶ *Ibid.*, para. 890 (referring to the United States' appellant's submission, para. 444).

recipients and does not address either all United States production of upland cotton, or all "uses" of United States upland cotton.

109. Brazil also takes issue with the United States' assertion that Step 2 payments are contingent on use and not exportation. According to Brazil, Step 2 payments are not contingent on "use" in any meaningful sense. The measure is indifferent as to whether, how or when the upland cotton is "used." The criterion is not "use", but simply "exportation". Provided that the upland cotton is "shipped" from the United States, it would not matter if the upland cotton were never used, for instance, because its quality deteriorated during shipping or even because the ship carrying it sank. A subsidy would still be paid because of "exportation" from the United States.

110. Finally, Brazil distinguishes the facts in the present dispute from those before the panel in *Canada – Dairy*. In that case, a single regulatory class applied to all Canadian production of milk destined for a particular end-use.¹⁰⁷ In contrast, in the present case, the measure under which Step 2 payments are made explicitly establishes two mutually exclusive regulatory categories that apply to some, but not all, United States production of upland cotton.

111. Brazil requests, therefore, that the Appellate Body reject the United States' appeal and uphold the Panel's finding that Step 2 payments to exporters of United States upland cotton are contingent upon export performance and, consequently, are inconsistent with Articles 3.3 and 8 of the *Agreement on Agriculture* and are prohibited under Articles 3.1(a) and 3.2 of the *SCM Agreement*.

(b) Export Credit Guarantees

(i) *Panel's terms of reference*

112. Brazil asks the Appellate Body to uphold the Panel's conclusion that export credit guarantees to facilitate the export of United States agricultural commodities other than upland cotton were within the Panel's terms of reference.

113. Brazil asserts that the measures included in its request for consultations, as well as in its request for establishment of a panel, were the General Sales Manager 102 ("GSM 102") program, the General Sales Manager 103 ("GSM 103") program, and the Supplier Credit Guarantee Program (the "SCGP"). Under United States law, each of these measures applies to all eligible agricultural products. Adding a particular product or products to Brazil's request for establishment would not, therefore, have constituted the addition of *measures*. In any event, Brazil argues that its request for

¹⁰⁷Brazil's appellee's submission, paras. 894-899 (referring to Panel Report, *Canada – Dairy*, paras. 2.39 and 7.41).

consultations, in fact, identified the United States' export credit guarantee measures in connection with all eligible commodities, without any limitation to upland cotton.

114. Additionally, Brazil asserts that, irrespective of the measures identified in Brazil's request for consultations, the Panel found, as a matter of fact, that "consultations were held" on the export credit guarantee measures in connection with all eligible commodities, as required by Article 6.2 of the DSU.¹⁰⁸ Brazil explains that the Appellate Body has held that as long as consultations were held on a measure included in a request for establishment of a panel, that measure is properly within a panel's terms of reference, irrespective of whether the measure was included in the request for consultations.¹⁰⁹ This is consistent with the purpose of consultations, which is to offer Members the opportunity to engage in good faith discussions with a view to resolving a trade dispute. The process necessarily involves collecting information that will shape the substance and scope of the dispute, should consultations fail.

(ii) *Statement of available evidence*

115. Brazil asks the Appellate Body to deny the United States' claim that the Panel erred in concluding that Brazil provided a statement of available evidence with respect to the United States' export credit guarantee programs as they relate to agricultural commodities other than upland cotton, as required by Article 4.2 of the *SCM Agreement*.

116. According to Brazil, its statement of available evidence not only identified the measures at issue—the export credit guarantee measures—but also indicated the characteristics of those measures that had led Brazil to suspect that they constituted export subsidies. Brazil argues that this is consistent with the Appellate Body's interpretation of the requirements of Article 4.2 of the *SCM Agreement*.¹¹⁰ Specifically, Brazil's statement describes the failure of the United States' export credit guarantee programs to establish premium rates that cover long-term operating costs and losses, which are central elements in determining whether a program constitutes an export subsidy under item (j) of the Illustrative List of Export Subsidies included as Annex I to the *SCM Agreement*. Further, the Panel found that the documentary evidence cited by Brazil to support its preliminary view was a link to a United States government website with data showing that revenues for the export credit guarantee programs do not cover long-term operating costs and losses.¹¹¹ The evidence

¹⁰⁸Brazil's appellee's submission, para. 211 (quoting Panel Report, para. 7.61).

¹⁰⁹*Ibid.*, para. 213 (referring to Appellate Body Report, *Brazil – Aircraft*, paras. 132-133).

¹¹⁰*Ibid.*, paras. 228-229 (referring to Appellate Body Report, *US – FSC*, para. 161).

¹¹¹*Ibid.*, para. 226 (referring to Panel Report, paras. 7.92-7.93).

addressed the failure of the export credit guarantee programs to cover long-term operating costs and losses overall, rather than in connection with upland cotton alone.

117. Thus, Brazil asserts, its statement of available evidence meets the requirements of Article 4.2, by identifying the export credit guarantee programs, and providing and describing available evidence of the character of those measures as export subsidies, across all eligible commodities.

(iii) *Article 10.2 of the Agreement on Agriculture*

118. Brazil requests that the Appellate Body reject the United States' appeal of the Panel's finding that export credit guarantees are subject to the export subsidy disciplines in Article 10.1 of the *Agreement on Agriculture*.

119. Brazil asserts that subsidized export credit guarantees are covered by the general definition of "export subsidies" under Article 1(e) of the *Agreement on Agriculture*. These measures are, therefore, subject to Article 10.1 of the *Agreement on Agriculture*, unless an express exception is provided in Article 10.2. The text of Article 10.2 establishes two obligations, but does not provide an exception. It requires WTO Members to negotiate multilateral rules to regulate agricultural export credit measures specifically, and to apply those rules once they are agreed. The text of Article 10.2 may be contrasted with several other WTO provisions that also require negotiations, but that state explicitly that the existing disciplines do not apply in the meantime.¹¹² The inclusion of such exceptions in other provisions highlights the lack of an exception in Article 10.2.

120. Brazil argues that the Panel's interpretation is consistent with the context and object and purpose of Article 10.2. Each of the paragraphs in Article 10 pursues the aim of preventing circumvention of export subsidy commitments and, thereby, contributes to the purpose of the *Agreement on Agriculture* of establishing specific binding commitments on export competition. Article 10.1 does so by disciplining export subsidies not listed in Article 9.1, as well as non-commercial transactions. Article 10.3 does so by reversing the usual rules on the burden of proof where Members have exported products in excess of their quantity reduction commitment levels. Article 10.4 does so by providing specific disciplines on food aid that ensure it is used for legitimate purposes and not to circumvent export subsidy commitments. Therefore, Article 10.2 must be interpreted in a manner that ensures that it contributes to the purpose of preventing circumvention of commitments on export competition. The United States' interpretation of Article 10.2 would leave

¹¹²Brazil's appellee's submission, paras. 916-917 (referring to footnote 15 to Article 6.1(a) and footnote 24 to Article 8.2(a) of the *SCM Agreement*, and Article XIII of the *General Agreement on Trade in Services*).

Members free to grant unlimited export subsidies in the form of export credit guarantees and would permit wholesale circumvention of commitments.

121. Brazil takes issue with the United States' assertion that the Panel's interpretation is an "assault" on international food aid.¹¹³ According to Brazil, food aid is subject to the specific disciplines in Article 10.4 of the *Agreement on Agriculture*, as well as the general disciplines in Article 10.1. Article 10.4 pursues the aim of preventing circumvention by ensuring that, consistently with the international regulation of food aid, such transactions do not result in "harmful interference" with trade.¹¹⁴ Further, Article 10.4(a) adds to the disciplines by prohibiting food aid that is "tied" to or contingent upon "commercial exports" of agricultural products. This is not an "assault" on food aid; rather, it ensures that food aid is used for legitimate humanitarian purposes and not for illegitimate trade-distortion.

122. Brazil, moreover, disagrees with the conclusions drawn by the United States from the negotiating history of the *Agreement on Agriculture*. Brazil explains that the negotiating history confirms that export credit guarantees are, indeed, subject to Article 10.1. Members had known since 1960 that subsidized export credit guarantees were covered by the term "export subsidies". During the negotiations, Members repeatedly expressed the intention to subject these measures to export subsidy disciplines, and they never once expressed the intention to exclude them from such disciplines. In addition, Brazil rejects the United States' contention that the Panel's reading of Article 10.2 gives rise to a result that is "manifestly unreasonable".¹¹⁵ At the close of the Uruguay Round, Members agreed that they would calculate their respective export subsidy commitment levels exclusively on the basis of the export subsidies listed in Article 9.1. They chose to leave out of that calculation the export subsidies in Article 10.1.¹¹⁶ This is not an unjust implementation of the Uruguay Round, but the logical consequence of the bargain Members struck. Brazil emphasizes that the Panel's interpretation does not mean that Members cannot grant export credit guarantees. Instead, it means that *subsidized* export credit guarantees are subject to discipline as trade-distorting measures, and cannot be used to override export subsidy commitments.

¹¹³Brazil's appellee's submission, para. 940 (quoting the United States' appellant's submission, para. 350).

¹¹⁴*Ibid.*, para. 940 (quoting paragraph 3, FAO "Principles of Surplus Disposal and Consultative Obligations", and Article IX(d) of the Food Aid Convention).

¹¹⁵*Ibid.*, para. 926 (quoting the United States' appellant's submission, para. 384).

¹¹⁶*Ibid.*, para. 927.

123. Finally, Brazil asserts that, even if Article 10.2 were to exempt export credit guarantees for agricultural commodities from the disciplines in the *Agreement on Agriculture*, these measures would still be subject to Article 3 of the *SCM Agreement*.¹¹⁷

(iv) *Burden of proof*

124. Brazil submits that, even if correct, none of the United States' arguments in respect of the Panel's application of the burden of proof would lead to a reversal of the Panel's conclusion that the United States' export credit guarantee programs constitute export subsidies under the *Agreement on Agriculture* and the *SCM Agreement*. Irrespective of which party bore the burden of proof and the role of Article 10.3 of the *Agreement on Agriculture*, the Panel explicitly found that Brazil had established that the premiums charged under the United States' export credit guarantee programs were inadequate to cover long-term operating costs and losses for purposes of item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement*.¹¹⁸ Having concluded that Brazil had successfully demonstrated that the United States' export credit guarantee programs constitute export subsidies under item (j) as context for the interpretation of the term "export subsidies" in Articles 10.1 and 8 of the *Agreement on Agriculture*, the Panel similarly concluded that the export credit guarantee programs constitute prohibited export subsidies under item (j) of the Illustrative List of Export Subsidies and Articles 3.1(a) and 3.2 of the *SCM Agreement*.¹¹⁹

125. Brazil also takes issue with the United States' assertion that the Panel required the United States to offer "incontrovertible demonstrations to the Panel" that, under the net present value accounting methodology, data trends indicated profits for the programs.¹²⁰ Brazil explains that, as the party asserting that these trends existed, the United States bore the burden of proving their existence. In the statement challenged by the United States, the Panel simply found that the United States had not met this burden. The Panel made this finding based on data submitted by the United States. Given that the United States has not alleged that the Panel failed to make an objective assessment of the facts under Article 11 of the DSU, Brazil argues that the United States' appeal should be denied on these grounds alone.

¹¹⁷ At the oral hearing, however, Brazil clarified that if Article 10.2 were to exempt export credit guarantees for agricultural commodities from the disciplines in the *Agreement on Agriculture*, Article 3 of the *SCM Agreement* would not be applicable to such measures.

¹¹⁸ Brazil's appellee's submission, paras. 1023-1024 (referring to Panel Report, para. 7.867).

¹¹⁹ *Ibid.*, para. 1024 (referring to Panel Report, paras. 7.946-7.948).

¹²⁰ *Ibid.*, para. 1025 (quoting the United States' appellant's submission, para. 408).

(v) *Necessary findings of fact*

126. Brazil asserts that the United States' claim that the Panel did not make the necessary findings of fact should have been brought under Article 11 of the DSU and that, having failed to bring such a claim, the United States is precluded from challenging the Panel's appreciation of the facts.

127. In any event, Brazil submits that neither item (j), nor Articles 3.1(a) and 3.2 of the *SCM Agreement*, nor Articles 10.1 and 8 of the *Agreement on Agriculture*, required the Panel to make specific factual findings on the "monetary extent to which" premium rates are inadequate to cover the long-term operating costs and losses of the United States' export credit guarantee programs.¹²¹ It was sufficient for the Panel to have found that, under any and all methodologies that it reviewed and accepted, premium rates are *inadequate* to cover the long-term operating costs and losses of the export credit guarantee programs.

128. In addition, Brazil asserts that the Panel made sufficient factual findings for its conclusion that premium rates are inadequate to cover the long-term operating costs and losses of the export credit guarantee programs. Specifically, the Panel assessed the performance of the export credit guarantee programs under the elements of item (j) in various ways. In its assessment of the *past* performance of the export credit guarantee programs during the period 1992-2002, the Panel used two accounting methodologies—net present value accounting and cash basis accounting—to determine whether premium rates are inadequate to cover the long-term operating costs and losses of the programs.

129. Brazil therefore requests that the Appellate Body uphold the Panel's finding that the United States' export credit guarantee programs constitute export subsidies within the meaning of item (j) of the Illustrative List of Export Subsidies and Articles 3.1 and 3.2 of the *SCM Agreement*.

C. *Claims of Error by Brazil – Appellant*

1. Domestic Support

(a) Article 13(a) of the *Agreement on Agriculture* – Base Period Update

130. Brazil conditionally appeals the Panel's exercise of judicial economy with respect to Brazil's claim that the "updating" of base acreage for direct payments under the FSRI Act of 2002 renders that program inconsistent with paragraph 6(a) of Annex 2 of the *Agreement on Agriculture*. Brazil's appeal is conditional on the Appellate Body reversing the Panel's finding that production flexibility

¹²¹ Brazil's appellee's submission, para. 1046 (quoting the United States' appellant's submission, para. 419).

contract payments and direct payments are not decoupled income support under paragraph 6(b) of Annex 2 and thus not entitled to peace clause protection by virtue of Article 13(a) of the *Agreement on Agriculture*.

131. Brazil argues that the Panel made factual findings to the effect that the FSRI Act of 2002 created a new "base period" of time (marketing years 1998-2001) according to which upland cotton producers' eligibility for direct payments could be calculated. This new base period could replace the base period that had prevailed under the FAIR Act of 1996 (i.e., 1993-1995) for the calculation of production flexibility contract payments. In practical terms, the FSRI Act of 2002 gave producers who planted more upland cotton during 1998-2001 the chance to "update", that is, increase, the quantity of base acres for which they received direct payments.

132. Brazil recalls that paragraph 6(a) of Annex 2 states that "[e]ligibility for such payments shall be determined by clearly-defined criteria such as income, status as a producer or landowner, *factor use or production level in a defined and fixed base period*".¹²² "Factor use" encompasses quantities of eligible farmland used in a historical period, such as the "base acres" used in the production flexibility contract and direct payment programs. Similarly, "production level" encompasses quantities of production based on historical acreage and yields, such as those used under the production flexibility contract and direct payment programs to calculate payments. If either the historical acreage or yields are updated, the result is a change in one of the "clearly-defined criteria". Yet paragraph 6(a) requires that both the "factor use" and "production level" criteria be set out in "a" single "fixed" base period.

133. Brazil notes that the ordinary meaning of the term "fixed" in relation to a base period is that the defined base period cannot be changed or updated. Accordingly, there can be only one period of time to establish these values; there can be no "updating" of the base period. Brazil contends that the context supports its interpretation. Moreover, the object and purpose of paragraph 6 of Annex 2 is to ensure that decoupled payments "have no, or at most minimal, trade-distorting effects or effects on production".¹²³ Paragraphs 5 and 6 of Annex 2 make clear that the purpose of "decoupled income support" is to break the link between production decisions and the amount of support. If that link is maintained, then domestic support is not entitled to the exemption from reduction commitments. Brazil submits that the United States' interpretation would effectively allow a Member to re-link last year's production to this year's payment. This would void paragraph 6(a) of any *effet utile*.

¹²²Brazil's other appellant's submission, para. 246. (emphasis added by Brazil)

¹²³*Ibid.*, para. 251 (quoting para. 1 of Annex 2 of the *Agreement on Agriculture*).

134. Brazil submits that the undisputed facts on the record reveal that production flexibility contract payments and direct payments were made to the same persons, on the same land, based on the same yield and payment formula, under the same conditions, and with the same limitations. Given these similarities, the option for a producer to select a new "fixed base period" other than the original "fixed base period" means that the direct payments are not green box measures under paragraph 6(a) of Annex 2. Brazil requests the Appellate Body to find accordingly.

2. Serious Prejudice

(a) World Market Share under Article 6.3(d) of the *SCM Agreement*

135. Brazil appeals the Panel's finding that Brazil failed to establish a *prima facie* case of inconsistency with Articles 5(c) and 6.3(d) of the *SCM Agreement*. Brazil asks the Appellate Body to reverse the Panel's finding that the words "world market share" in Article 6.3(d) mean "the portion of the world's supply that is satisfied by the subsidizing Member's producers"¹²⁴ and to find instead that "world market share" means "world market share of exports".¹²⁵ In addition, if the Appellate Body reverses the Panel's finding that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*, Brazil calls on the Appellate Body to complete the analysis under Article 6.3(d) and to find that the effect of these subsidies is an increase in the United States' world market share of exports within the meaning of Article 6.3(d), thereby constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*.

136. As regards the interpretation of the term "world market share" in Article 6.3(d) of the *SCM Agreement*, Brazil first draws support from the text of that provision. Article 6.3(d) does not specify whether "world market share" refers to world market share of production or world market share of something else. However, the use of the word "trade" in footnote 17 to Article 6.3(d) suggests that Article 6.3(d) is directed towards a Member's share of world trade in a product, which requires a focus on *exports* rather than *production*.

137. Secondly, Brazil refers to the context of Article 6.3(d). Brazil argues that Article XVI:3 of the GATT 1994 addresses a Member's "share of world export trade" and that similarities between Article XVI:3 and Article 6.3(d) require the phrase "world market share" in the latter provision to be read in the same way. Brazil also points to the context provided by paragraphs (a) and (b) of Article 6.3, as well as Articles 6.4 and 6.7, and argues that the focus of a serious prejudice analysis

¹²⁴Brazil's other appellant's submission, para. 269 (quoting Panel Report, para. 7.1434).

¹²⁵*Ibid.*, para. 380(9). (original emphasis)

under Article 6.3 is on the effects of the subsidies on like products from the complaining Member. According to Brazil, "[t]hese effects are either manifest in aggregated volume effects on the exports of a complaining Member under Articles 6.3(a), 6.3(b) and 6.3(d), or in price effects on the like product of the complaining Member in the 'same market' under Article 6.3(c)".¹²⁶

138. Thirdly, Brazil relies on the object and purpose of Articles 5(c) and 6.3 of the *SCM Agreement*, which it characterizes as being to discipline subsidies causing serious prejudice to the interests of another Member. As stated in Article XVI:1 of the GATT 1994 (to which footnote 13 to Article 5(c) of the *SCM Agreement* refers), serious prejudice is reflected in trade effects, namely decreased imports or increased exports. Increased production is taken into account in a serious prejudice analysis, because it may have trade effects. However, by focusing solely on the United States' share of world upland cotton production, the Panel disregarded the significant increase in the United States' share of world upland cotton exports from 1999 to 2002, which caused serious prejudice to other Members' producers who were competing against the subsidized exports. The Panel's interpretation means that the subsidizing Member's world market share may be significantly affected by unrelated increases in production in third countries, even if this additional production is consumed domestically. Brazil suggests that this would render Article 6.3(d) "largely inutile"¹²⁷ in disciplining the use of subsidies to increase market share.

139. For these reasons, Brazil asks the Appellate Body to reverse the Panel's interpretation of "world market share" under Article 6.3(d) of the *SCM Agreement* and to find instead that "world market share" means world market share of *exports*. Should it do so, and if the Appellate Body reverses the Panel's finding of significant price suppression under Article 6.3(c) of the *SCM Agreement*, Brazil asks the Appellate Body to complete the analysis under Article 6.3(d).

140. According to Brazil, factual findings by the Panel and undisputed facts on the record would allow the Appellate Body to complete the analysis under Article 6.3(d). The Panel's findings show that the United States' world market share of exports in marketing year 2002 was 39.9 percent, representing an increase over the previous three-year average of 28.4 percent.¹²⁸ Moreover, the Panel's assessment of the effects of the subsidies in its analysis under Article 6.3(c) confirms that the subsidies in question result in an increase in world market share, stimulate exports, and enhance the competitiveness of United States producers in world trade. Brazil submits that the Panel's causation and non-attribution analyses under Article 6.3(c) are also relevant for the causation analysis under

¹²⁶Brazil's other appellant's submission, para. 287.

¹²⁷*Ibid.*, para. 295.

¹²⁸*Ibid.*, para. 301.

Article 6.3(d). It is appropriate for the Appellate Body to complete the analysis in this way because the Panel did address all the elements of Brazil's claim under Article 6.3(d) and, even if it had not, Articles 6.3(c) and 6.3(d) claims are "closely related" and "part of a logical continuum".¹²⁹ According to Brazil, both claims relate to the adverse effects of and serious prejudice caused by actionable subsidies pursuant to Article 5(c) of the *SCM Agreement*, and Articles 6.3(c) and 6.3(d) are "closely-linked steps in determining the consistency of"¹³⁰ actionable subsidies under the *SCM Agreement*.

3. Import Substitution Subsidies and Export Subsidies

(a) Share of World Export Trade under Article XVI:3 of the GATT 1994

141. Brazil appeals the Panel's finding that the second sentence of Article XVI:3 of the GATT 1994 applies only to export subsidies as defined in the *Agreement on Agriculture* and the *SCM Agreement*. Brazil asks the Appellate Body to reverse the Panel's finding that this sentence applies only to export subsidies and to find instead that it applies to "any form of subsidy" which operates to increase the export of any primary product.¹³¹ In addition, if the Appellate Body reverses the Panel's finding that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*, and if the Appellate Body does not find that the effect of these subsidies is an increase in the United States' world market share of exports within the meaning of Article 6.3(d) constituting serious prejudice within the meaning of Article 5(c) of the *SCM Agreement*, Brazil calls on the Appellate Body to complete the analysis and to find that these subsidies are applied in a manner that results in the United States having "more than an equitable share of world export trade in" upland cotton, contrary to the second sentence of Article XVI:3 of the GATT 1994.

142. In relation to the subsidies subject to the second sentence of Article XVI:3 of the GATT 1994, Brazil first refers to the text of this sentence and, in particular, the words "any form of subsidy". The ordinary meaning of these words suggests that Article XVI:3 applies to every subsidy, no matter what kind or how many. In addition, the second sentence specifies that it does not matter whether the subsidy is granted "directly or indirectly". Brazil points out that, in contrast to the first sentence of Article XVI:3, which is concerned with subsidies *on the export* of primary products, the second sentence is concerned with any subsidies that have export-enhancing effects.

¹²⁹Brazil's other appellant's submission, paras. 313 and 314 (quoting Appellate Body Report, *Canada – Periodicals*, p. 24, DSR 1997:1, 449 at 469; Appellate Body Report, *EC – Asbestos*, para. 79).

¹³⁰*Ibid.*, para. 314 (quoting Appellate Body Report, *Canada – Periodicals*, p. 24, DSR 1997:1, 449 at 469).

¹³¹*Ibid.*, para. 317 (quoting the GATT 1994, Article XVI:3). (emphasis added by Brazil)

143. Secondly, turning to the broader context of Article XVI:3, Brazil contends that Part A of Article XVI disciplines subsidies in general, and Part B of Article XVI disciplines "Export Subsidies" (as specified in the heading to Part B) in particular. The wording of the provisions in Part B shows that "export subsidies" in this context means "subsidies on the export" of a primary product (under the first sentence of Article XVI:3) and subsidies that operate "to increase the export of any primary product" (under the second sentence of Article XVI:3). Brazil argues that, in contrast, the export subsidy disciplines in the *SCM Agreement* and the *Agreement on Agriculture* are concerned with the narrower concept of "subsidies contingent upon export performance".¹³²

144. Brazil also refers, for contextual support, to Article 13 of the *Agreement on Agriculture*. Article 13(e)(ii) provides a limited exemption for agricultural export subsidies from Article XVI of the GATT 1994, suggesting that Article XVI:3 could otherwise apply to such subsidies. Similarly, Brazil contends that the conditional exemption in Article 13(a)(ii) suggests that, in principle, green box domestic support is subject to challenge under the second sentence of Article XVI:3.

145. Thirdly, with respect to the object and purpose of Article XVI of the GATT 1994 and Articles 5 and 6 of the *SCM Agreement*, Brazil suggests that these provisions are intended to prevent subsidies granted by Members from having certain adverse outcomes or effects. The purpose of disciplining adverse effects of subsidies in the second sentence of Article XVI:3 of the GATT 1994 would be frustrated if this sentence was interpreted to apply only to subsidies contingent on export performance. This interpretation would deprive the second sentence of Article XVI:3 of *effet utile*, because the disciplines in that sentence would no longer apply to many subsidies having export-enhancing effects.

146. Brazil adds that Article XVI:3 of the GATT 1994 continues to apply despite the disciplines in the *SCM Agreement* and the *Agreement on Agriculture*.¹³³ In interpreting the covered agreements harmoniously and giving effect to all of them, the second sentence of Article XVI:3 must apply to measures that are also subject to the *SCM Agreement* and the *Agreement on Agriculture*. The rules in Article 21.1 of the *Agreement on Agriculture* and the General Interpretative Note to Annex 1A of the *WTO Agreement* do not apply, because no conflict exists between the second sentence of Article XVI:3 of the GATT 1994 and the disciplines in the *Agreement on Agriculture* and the *SCM Agreement*.

¹³²Brazil's other appellant's submission, para. 333 (quoting Article 1(e) of the *Agreement on Agriculture* and referring to Article 3.1(a) of the *SCM Agreement*).

¹³³*Ibid.*, para. 345 (referring to Appellate Body Report, *Korea – Dairy*, para. 75; and Appellate Body Report, *Argentina – Footwear (EC)*, para. 81).

147. For these reasons, Brazil asks the Appellate Body to reverse the Panel's finding that the second sentence of Article XVI:3 of the GATT 1994 applies only to export subsidies as defined in the *Agreement on Agriculture* and the *SCM Agreement* and to find instead that this sentence applies to any form of subsidy that operates to increase the export of any primary product. Should it do so, and if the Appellate Body reverses the Panel's finding of significant price suppression under Article 6.3(c) of the *SCM Agreement* and does not find serious prejudice pursuant to Articles 5(c) and 6.3(d) of the *SCM Agreement*, Brazil asks the Appellate Body to complete the analysis under Article XVI:3 of the GATT 1994.

148. Brazil contends that the Panel's factual findings and the undisputed facts on the panel record are sufficient for the Appellate Body to find that the price-contingent subsidies caused the United States to have "more than an equitable share of world export trade", contrary to Article XVI:3 of the GATT 1994. The Panel made factual findings, pursuant to Article 6.3(c) of the *SCM Agreement*, regarding the United States' share of world export trade and the effect of the subsidies on that share. Brazil also submits that the Panel's non-attribution analysis would allow the Appellate Body to conclude that it was the subsidies in question that led to the United States' world market share reaching a level that is more than equitable, at the expense of other, more efficient producers.

(b) Export Credit Guarantees

(i) *Threat of circumvention*

149. Brazil asserts that the Panel erred in the interpretation and application of Article 10.1 of the *Agreement on Agriculture* by finding that "threat" of circumvention of export subsidy commitments would arise only if beneficiaries had an "absolute" or "unconditional statutory legal entitlement" to receive the subsidies such that the United States would "necessarily" be required to grant subsidies after the commitment level had been reached.¹³⁴ Brazil also takes issue with the Panel's statement that a "threat" could not arise if circumvention was just a *possibility*.¹³⁵

150. According to Brazil, by its very nature, an obligation that covers the "threat" of circumvention deals with a future event whose actual occurrence is merely a possibility that cannot be assured with certainty.¹³⁶ Brazil adds that, even though the ordinary meaning of the term "threat" can encompass events that are a possibility or that appear likely, it can also include events whose occurrence is indicated or portended by circumstances. Furthermore, the meaning of the term "threatens" is

¹³⁴Brazil's other appellant's submission, paras. 85-89 (quoting Panel Report, paras. 7.883 and 7.892).

¹³⁵*Ibid.*, paras. 89 and 114 (referring to Panel Report, para. 7.893).

¹³⁶*Ibid.*, para. 94 (referring to Appellate Body Report, *US – Lamb*, para. 125).

clarified by its immediate context, particularly the word "[p]revention" in the title of Article 10. Brazil thus contends that, to give proper meaning to the aim of prevention, the threat obligation should be read so as to thwart, forestall, or stop circumvention from occurring by requiring a Member to take appropriate precautionary action. If, on the contrary, the degree of likelihood necessary to trigger the threat obligation were set too high, the threat obligation would fail to prevent circumvention, contrary to the express aim of the provision.

151. Brazil distinguishes the meaning of "threatens" in the context of Article 10.1 of the *Agreement on Agriculture* from the connotation of that term in other covered agreements. It explains that the *Agreement on Safeguards* and the *Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994* (the "*Anti-Dumping Agreement*") require a higher degree of likelihood because, under both Agreements, the demonstration of "threat" triggers the right of a WTO Member to apply trade remedy measures involving suspension or modification of WTO commitments. In contrast, Article 10.1 of the *Agreement on Agriculture* aims at the effective enforcement of a Member's export subsidy obligations. Brazil submits that the Panel's reading of Article 10.1 runs counter to the Appellate Body's decision in *US – FSC*, where the Appellate Body held that Article 10.1 applies if a measure "allows for" circumvention¹³⁷, whereas the Panel insisted that circumvention must be required by legal entitlement. Brazil submits that the assessment of whether a threat exists under Article 10.1 must be done on a case-by-case basis and suggests a list of factors that could be considered as part of the assessment.¹³⁸

152. Brazil also contends that the Panel erred by confining its examination of threat of circumvention to scheduled agricultural products other than rice and to unscheduled products "not supported"¹³⁹ under the United States' export credit guarantee programs.¹⁴⁰ Brazil explains that, in addition to alleging actual circumvention in respect of rice, it also included this product in its claim of threat of circumvention. Brazil observes, furthermore, that it drew no distinctions between supported and unsupported products. Thus, the Panel's analysis of threat of circumvention should have included rice and all unscheduled products eligible to receive support under the export credit guarantee programs, regardless of whether they were in fact supported by such programs in the past.

¹³⁷Brazil's other appellant's submission, paras. 126-129 (quoting Appellate Body Report, *US – FSC*, para. 152).

¹³⁸*Ibid.*, para. 105.

¹³⁹When the Panel refers to products supported under the export credit guarantee programs, the Panel is referring to products for which there was evidence in the record showing that they were not only eligible under the programs, but that export credit guarantees were in fact received in connection with exports of those products. (Panel Report, para. 6.32)

¹⁴⁰Brazil's other appellant's submission, para. 132 (quoting Panel Report, para. 7.882).

153. Brazil argues that the Panel should have made a finding of threat of circumvention notwithstanding its conclusion on actual circumvention in respect of rice and unscheduled products supported under the United States' export credit guarantee programs. The prohibitions on actual and threatened circumvention are two separate obligations under Article 10.1 of the *Agreement on Agriculture*. The concepts of actual and threatened circumvention in Article 10.1 are different from the notions of injury and threat of injury in the trade remedies context. Article 10.1 does not confer rights, but imposes obligations. Accordingly, to hold that a Member has actually circumvented its export subsidy commitments in the past does not make it irrelevant to conclude that the Member continues to threaten circumvention in the future.

154. If the Appellate Body agrees with Brazil and modifies the Panel's interpretation of Article 10.1, Brazil requests that the Appellate Body complete the analysis of its claims. Brazil argues that the United States maintains export credit guarantees for a very wide range of scheduled and unscheduled agricultural products. These measures are subject to special budgetary rules that provide permanent and unlimited budget authority to the CCC to grant export credit guarantees. Therefore, Brazil asserts, no budgetary limits are imposed on the value of the subsidies that can be granted.

155. Brazil states that, even though the United States alleged before the Panel that the export credit guarantee programs are not unlimited because they impose certain conditions on the grant of subsidies, these conditions have no rational relationship whatsoever to ensuring respect for the United States' export subsidy commitments. There is no evidence on the record, according to Brazil, to demonstrate that any of the applicable conditions has ever been applied with a view to ensuring respect for the United States' export subsidy commitments. Moreover, none of these conditions has prevented the United States from consistently granting export credit guarantees for both scheduled and unscheduled products in violation of these commitments. Brazil contends that the authority that the United States enjoys to grant export credit guarantees in violation of its export subsidy commitments, coupled with the consistent pattern of granting behaviour in violation of those commitments, establishes that the United States' export credit guarantees are applied in a manner that threatens to lead to circumvention of the United States' export subsidy commitments for all eligible products, under Article 10.1 of the *Agreement on Agriculture*.

(ii) *Actual circumvention*

156. Brazil claims that the Panel erred in the application of Article 10.1 of the *Agreement on Agriculture*, and did not discharge its duties under Article 11 of the DSU, by finding that the United States' export credit guarantees are applied in a manner that results in circumvention of the United States' export subsidy commitments for only one scheduled product, namely rice.

157. Brazil submits that, according to uncontested evidence on the record, supplied by the United States, actual circumvention also occurred for pig meat and poultry meat in 2001.¹⁴¹ According to figures supplied by the United States, in fiscal year 2001, the volume of pig meat and poultry meat benefiting from export credit guarantees exceeded the United States' reduction commitment levels for these products. The Panel took explicit cognizance of this information, but nonetheless failed to apply a proper interpretation of Article 10.1 to the admitted facts. Likewise, the Panel failed to make an objective assessment of the matter, including of admitted and uncontested facts supplied by the United States, as required by Article 11 of the DSU.

158. Therefore, Brazil requests that the Appellate Body modify the Panel's finding that the United States' export credit guarantees are applied in a manner that results in actual circumvention with respect to only one scheduled product, namely, rice, and that it find, based on the undisputed facts on the record, that export credit guarantees are applied in a manner that also results in actual circumvention with respect to pig meat and poultry meat.

(iii) *Articles 1.1 and 3.1(a) of the SCM Agreement*

159. Brazil appeals the Panel's finding that, having found that the United States' export credit guarantee programs are export subsidies under item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement*, it was unnecessary to address Brazil's claim that these programs constitute export subsidies under the terms of Articles 1.1 and 3.1(a) of the *SCM Agreement*. In declining to make a finding under these two Articles, the Panel erred in the interpretation and application of Article 3.1(a) of the *SCM Agreement*, as well as of Article 3.7 of the DSU.

160. According to Brazil, the Panel failed to recognize that Article 3.1(a) includes multiple and distinct obligations that differ from those deriving from item (j) of the Illustrative List of Export Subsidies. Most importantly, while a measure may no longer constitute an export subsidy under

¹⁴¹In its other appellant's submission, Brazil also claimed that the Panel erred by failing to find actual circumvention of the United States' export subsidy reduction commitments for vegetable oil in 2002. (Brazil's other appellant's submission, paras. 208-209) At the oral hearing, however, Brazil indicated that it was no longer pursuing this claim in respect of vegetable oil.

item (j), the same measure can still constitute an export subsidy under Articles 1.1 and 3.1(a) of the *SCM Agreement*. In the present dispute, a claim under item (j) of the Illustrative List of Export Subsidies requires a determination whether the programs involved a "net cost" to the United States government. In contrast, a claim under Articles 3.1(a) and 1.1 necessitates a determination of whether the programs constitute "financial contributions" that confer a "benefit" (within the meaning of Article 1.1 of the *SCM Agreement*) on recipients of export credit guarantees¹⁴² and are "contingent ... upon export performance" (within the meaning of Article 3.1(a) of the *SCM Agreement*). These are two separate claims regarding two separate obligations imposed upon the United States. The first obligation of the United States is to refrain from maintaining export credit guarantee programs that entail financial contributions, confer benefits, and are contingent upon export performance, while its second obligation is to refrain from maintaining export credit guarantee programs that incur a net cost to the United States government.

161. Brazil submits that, by failing to examine these distinct claims, the Panel misapplied the principle of judicial economy¹⁴³ and failed to provide for a "prompt settlement" and "positive solution" of the dispute as required by Articles 3.3 and 3.7 of the DSU. The Panel's misapplication of the principle of judicial economy means that the recommendations and rulings of the DSB may not be sufficiently precise to resolve the dispute. The Panel left unresolved the dispute between the parties as to whether the export credit guarantee programs involve a "benefit", and the steps that the United States must take to implement its obligations under the *SCM Agreement* will therefore be unclear.

162. If the Appellate Body were to reverse the Panel's finding, Brazil requests that the Appellate Body complete the analysis and find that the United States' export credit guarantee programs constitute export subsidies under Articles 1.1 and 3.1(a) of the *SCM Agreement*. Brazil submits that it is undisputed that export credit guarantees constitute "financial contributions" and that the programs are "contingent ... upon export performance". Regarding the third element, i.e. whether the export credit guarantee programs confer a benefit within the meaning of Article 1.1(b) of the *SCM Agreement*, Brazil notes that the Appellate Body has sufficient factual findings and undisputed facts on the record to complete the analysis. Brazil explains that the record demonstrates that the United States' export credit guarantee programs confer a benefit because they: (i) are not risk-based; (ii) are below relevant benchmarks, including the fees charged by the United States Export-Import Bank for its own guarantees; and (iii) enable non-creditworthy purchasers of United States agricultural exports to secure loans they would otherwise be unable to secure.

¹⁴²Brazil's other appellant's submission, paras. 29-30 (referring to Appellate Body Report, *Canada – Aircraft*, paras. 154, 157).

¹⁴³*Ibid.*, paras. 33-34 (referring to Appellate Body Report, *Australia – Salmon*, paras. 222-224).

(iv) *ETI Act of 2000*

163. Brazil appeals the finding of the Panel that Brazil did not establish a *prima facie* case of inconsistency of the FSC Repeal and Extraterritorial Income Exclusion Act of 2000 (the "ETI Act of 2000"), and export subsidies granted thereunder in respect of upland cotton, with Articles 8 and 10.1 of the *Agreement on Agriculture*. Brazil acknowledges that the United States enacted legislation, on 25 October 2004, that "seems to repeal most of the illegal aspects of the ETI Act of 2000"¹⁴⁴ and, consequently, Brazil does not ask the Appellate Body to complete the analysis and to find that ETI Act export subsidies provided with respect to upland cotton exports are inconsistent with Articles 8 and 10.1 of the *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement*.

164. Brazil contends that it challenged before the Panel exactly the same measure that the panel and the Appellate Body in *US – FSC (Article 21.5 – EC)* held to be inconsistent with the *Agreement on Agriculture* and the *SCM Agreement*. Except for the fact that Brazil challenges only the ETI Act export subsidies to upland cotton (and not with respect to all products), the "measure" and the "claims" in the present case are identical to those in *US – FSC (Article 21.5 – EC)*. According to Brazil, the United States has never challenged this identity.

165. Brazil alleges that the United States "effectively admitted" the inconsistency of the ETI Act of 2000 with Articles 10.1 and 8 of the *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement* and never contested Brazil's claims on their merits.¹⁴⁵ Brazil explains that it presented to the Panel all the evidence and argumentation that had been before the panel and the Appellate Body in the earlier dispute relating to the ETI Act of 2000. Brazil incorporated by reference into its submissions (i) the panel report in *US – FSC (Article 21.5 – EC)*, (ii) the Appellate Body Report in *US – FSC (Article 21.5 – EC)*, and (iii) all submissions of the European Communities in that case. Brazil contends that an approach whereby the complaining Member incorporates by reference the reasoning of another panel, as modified by the Appellate Body, is consistent with the Appellate Body's reasoning in *Mexico – Corn Syrup (Article 21.5 – US)*.¹⁴⁶

¹⁴⁴Brazil's other appellant's submission, para. 214.

¹⁴⁵*Ibid.*, para. 222.

¹⁴⁶*Ibid.*, para. 224 (referring to Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 109).

166. Brazil asserts that, in addition to referencing the European Communities' claims and arguments in *US – FSC (Article 21.5 – EC)*, it presented arguments and evidence that addressed the specific nature of its claims, in particular with respect to Article 13(c)(ii) of the *Agreement on Agriculture*. Brazil submits that it identified the relevant portions of the *US – FSC (Article 21.5 – EC)* panel report that determined that the ETI Act of 2000 provides export subsidies. Specifically, that panel found that the ETI Act of 2000 (i) provides financial contributions within the meaning of Article 1.1(a)(ii) of the *SCM Agreement*, (ii) confers benefits within the meaning of Article 1.1(b), and thus (iii) bestows subsidies within the meaning of the *SCM Agreement* that (iv) are contingent upon export performance within the meaning of Article 3.1(a) of the *SCM Agreement*. Based on these arguments and findings, the Panel had more than sufficient evidence and arguments before it to conduct an objective examination of the consistency of the measure with the *Agreement on Agriculture* and the *SCM Agreement*. According to Brazil, the distinctions drawn by the Panel between the present dispute and the claims in *US – FSC (Article 21.5 – EC)* have no basis.

167. Brazil adds that, under Article 17.14 of the DSU, the parties to a dispute are unconditionally bound by adopted panel and Appellate Body reports.¹⁴⁷ Therefore, the United States is bound by the decision of the DSB to adopt the panel and Appellate Body Reports in *US – FSC (Article 21.5 – EC)* and the recommendation by the DSB that the United States bring the ETI Act of 2000 into conformity with the *Agreement on Agriculture* and the *SCM Agreement*. Despite the legal impossibility of the United States arguing that an identical measure subject to identical claims is WTO-consistent, the Panel nevertheless refused to take this into account in its assessment of the facts of the case and the matter before it.

168. Brazil states, moreover, that the ETI Act of 2000 is a measure that *all* WTO Members, *including the respondent*, have decided, through the adoption by the DSB of the relevant panel and Appellate Body reports, is inconsistent with the obligations of the United States under a covered agreement. The general rules on the burden of proof under the DSU, in essence, *presume* that a Member is in compliance with its obligations under WTO law and require a complaining Member to make a *prima facie* case that this presumption is misplaced. However, where the Members have decided in the DSB that a measure does not conform to a covered agreement, there is no basis for presuming that the same measure is in compliance with WTO law in another dispute. Any such presumption contradicts a formal DSB decision of the Members of the WTO.

¹⁴⁷Brazil's other appellant's submission, para. 234 (referring to Appellate Body Report, *US – Shrimp (Article 21.5 – Malaysia)*, para. 97 and Appellate Body Report, *EC – Bed Linen (Article 21.5 – India)*, paras. 90-96).

169. Accordingly, Brazil requests the Appellate Body to find that the Panel erred in the interpretation and application of the burden of proof when finding that Brazil had not established *prima facie* that the ETI Act of 2000 violates Articles 8 and 10.1 of the *Agreement on Agriculture* and Article 3.1(a) and 3.2 of the *SCM Agreement*.

D. *Arguments of the United States – Appellee*

1. Domestic Support

(a) Article 13(a) of the *Agreement on Agriculture – Base Period Update*

170. The United States submits that the Appellate Body should reject Brazil's conditional appeal that direct payments under the FSRI Act of 2002 are not in conformity with the green box criteria set forth in paragraph 6(a) of Annex 2 to the *Agreement on Agriculture*, because the program uses a "defined and fixed base period" different from that established for the production flexibility contract program under the FAIR Act of 1996. The United States argues that the direct payment program employs "a defined and fixed base period" within the meaning of paragraph 6(a) and Brazil's appeal relies on an erroneous reading of that paragraph, such that once one type of green box payment to producers is made, *all* subsequent measures providing such support must be made with respect to the same base period.

171. The United States argues that the ordinary meaning of the terms "defined and fixed base period", as used in paragraph 6(a), requires a base period to be "set out precisely" and to be kept "stationary or unchanging in relative position."¹⁴⁸ Direct payments under the FSRI Act of 2002 satisfy this requirement because eligibility is determined by historical production of any of a number of crops (including upland cotton) in a base period that is "definite" (set out in the FSRI Act of 2002) and "stationary or unchanging in a relative position" (that is, does not change for the duration of the FSRI Act of 2002). There is no textual requirement in paragraph 6(a) that new decoupled income support measures must utilize the *same* "defined and fixed base period" as any prior measures. Furthermore, the use of "a" defined and fixed base period contrasts with the use of the phrase "the base period" in other provisions of Annexes 2 and 3 of the *Agreement on Agriculture*. The United States emphasizes that the direct payment and production flexibility contract programs are different measures. There is thus no legal requirement that they use the same base period, so long as they each make use of a "defined and fixed" base period.

¹⁴⁸United States' appellee's submission, para. 128 (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 1, pp. 618 and 962).

172. The United States argues that Brazil's interpretation would foreclose reform options to Members with past green-box support programs, contrary to the object and purpose of the *WTO Agreement*. In addition, Brazil's interpretation of paragraph 6(a) would render direct payments under the FSRI Act of 2002 non-green box, even though the Panel implicitly found that such payments had no more than minimal trade-distorting effects or effects on production.

2. Serious Prejudice

(a) World Market Share under Article 6.3(d) of the *SCM Agreement*

173. The United States maintains that the Panel correctly found that Brazil did not establish a *prima facie* case of inconsistency with Articles 5(c) and 6.3(d) of the *SCM Agreement*. The United States requests the Appellate Body to uphold this finding. In particular, the United States requests the Appellate Body to dismiss Brazil's argument that the words "world market share" in Article 6.3(d) refer to "world market share of exports".¹⁴⁹ Even if the Appellate Body accepts this argument by Brazil, the United States requests the Appellate Body to dismiss the conditional request of Brazil that the Appellate Body complete the analysis and find that the effect of the price-contingent subsidies is an increase in the United States' world market share within the meaning of Article 6.3(d), thereby constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*.

174. According to the United States, Brazil's reading of "world market share" as meaning "world market share of export trade" is erroneous. First, the United States endorses the Panel's finding that, by using the term "market", Members intended a meaning broader than the share of "exports" or "trade". The United States contests Brazil's view that the Panel's interpretation of Article 6.3(d) reduces the provision to inutility. The United States agrees with the Panel that Article 6.3(d) calls for an examination of the portion of the world *market* that is satisfied by the subsidizing Member's producers. Nevertheless, the United States stresses that the Panel erroneously equated this examination with an examination of only that portion of the world's *supply* that is satisfied by the subsidizing Member's producers. The United States contends that the Panel should have looked at the level of world *sales* or *consumption* of cotton, rather than simply the world supply.

175. Secondly, as to the context of Article 6.3(d), the United States submits that the Panel was correct to conclude that the use of the phrase "world market share" (as opposed to the different formulations found in Article XVI:3 of the GATT 1994 and Article 27.6 of the *SCM Agreement*)

¹⁴⁹United States' appellee's submission, para. 145 (quoting Brazil's other appellant's submission, para. 271). (original emphasis)

implies that Members did not want to restrict "world market share" to a Member's share of "world export trade" or "world trade". Similarly, unlike paragraphs (a) and (b) of Article 6.3, paragraph (d) of Article 6.3 is not explicitly restricted to any particular exports or imports or geographical area. The United States contends that the use of the word "trade" in footnote 17 to Article 6.3(d), but not in the text of the Article itself, implies that "world market share" does not include merely shares in world "trade".

176. Even if Brazil's interpretation of the words "world market share" in Article 6.3(d) were correct, the United States submits that the Appellate Body would not have sufficient factual findings and uncontroverted facts before it to complete the analysis under Article 6.3(d). The United States emphasizes that the Panel made no analysis with respect to causation and market share under Article 6.3(d). In the United States' submission, the Panel's "flawed"¹⁵⁰ analysis regarding the effect of the subsidy under Article 6.3(c) is not relevant to Brazil's request that the Appellate Body complete the analysis under Article 6.3(d) of the *SCM Agreement*.

3. Import Substitution Subsidies and Export Subsidies

(a) Share of World Export Trade under Article XVI:3 of the GATT 1994

177. The United States submits that the Panel properly found that Article XVI:3 of the GATT 1994 applies only to export subsidies as defined in the *Agreement on Agriculture* and the *SCM Agreement*. However, if the Appellate Body finds that Article XVI:3 applies to subsidies other than export subsidies, the United States asks the Appellate Body to find that Brazil has not established that the United States acted inconsistently with Article XVI:3 of the GATT 1994.

178. Beginning with the scope of Article XVI of the GATT 1994, the United States emphasizes that the text of Article XVI distinguishes between "Subsidies in General" (Part A) and "Additional Provisions on Export Subsidies" (Part B). By locating Article XVI:3 in Part B, Members agreed that Article XVI:3 is an additional provision on export subsidies. The term "export subsidy" is now defined in the *SCM Agreement* and the *Agreement on Agriculture* as referring to subsidies that are contingent on export performance. Both the context provided by these Agreements, as well as their drafting history, confirm that the export subsidies referred to in Article XVI:3 are also subsidies contingent on export performance. According to the United States, the Panel was correct to rely on Article 3.1(a) of the *SCM Agreement*, item (l) of the Illustrative List of Export Subsidies in Annex I

of the *SCM Agreement*, and the drafting history of the *Tokyo Round Subsidies Code* in concluding that Article XVI:3 of the GATT 1994 is concerned with certain export subsidies on primary products.

179. The United States contends that, even if the Appellate Body reverses the Panel's interpretation of the scope of Article XVI:3, there would be insufficient undisputed facts on the record or factual findings by the Panel for the Appellate Body to complete the analysis. The United States observes that the Panel made no findings on causation relative to trade share. As the "causation"¹⁵¹ requirement under Article XVI:3 of the GATT 1994 differs from that under Article 6.3(c) of the *SCM Agreement*, and as the United States has appealed the Panel's analysis under Article 6.3(c), that analysis cannot support a finding of inconsistency under Article XVI:3. Regarding the standard for determining what is "more than an equitable share" of world export trade under Article XVI:3, the United States understands Brazil to argue that the demonstration of "any causal relationship between an increase in exports and the subsidies provided" would suffice.¹⁵² However, the United States regards this standard as inadequate, because it renders the language "more than an equitable share" inutile, and it would transform Article XVI:3 into an outright prohibition on export-enhancing subsidies.

(b) Export Credit Guarantees

(i) *Threat of circumvention*

180. The United States requests that the Appellate Body uphold the Panel's finding that no threat of circumvention exists under Article 10.1 of the *Agreement on Agriculture* with respect to "unsupported" agricultural products for which no export credit guarantees have been provided.

181. The United States asserts that, contrary to Brazil's argument, the Panel's finding that the export credit guarantee programs do not threaten circumvention of export subsidy commitments is not an articulation of a broad standard that circumvention of export subsidy commitments would be "threatened" only "if beneficiaries had an 'absolute' or 'unconditional ... legal entitlement' to receive the subsidies such that the United States would 'necessarily' be [required] to grant subsidies after the commitment level had been reached".¹⁵³ Rather, in concluding that the programs did not pose a threat of circumvention, the Panel was simply responding to and declining to adopt Brazil's erroneous factual and legal characterizations of the program.

¹⁵¹United States' appellee's submission, para. 182.

¹⁵²*Ibid.*, para. 183 (quoting Brazil's other appellant's submission, para. 373).

¹⁵³*Ibid.*, para. 6 (quoting Brazil's other appellant's submission, para. 3).

182. The United States submits, furthermore, that the Panel rightly distinguished these programs from the mandatory subsidies at issue in *US – FSC*, and that the Panel's decision presents no conflict with that Appellate Body Report. Brazil effectively argued that a mere possibility of issuance of export credit guarantees presented a threat of circumvention, and the Panel simply did not adopt this theory in the context of the export credit guarantee programs.

183. In addition, the United States asserts that the Appellate Body need not complete the analysis regarding threat of circumvention as requested by Brazil. First, the Panel did not err in its analysis of threat of circumvention. Secondly, the Panel appropriately exercised judicial economy in declining to examine threat of circumvention with respect to those agricultural products for which it found actual circumvention. Further analysis was not necessary to resolve the matter in dispute as it would not affect implementation of the obligation to apply export subsidies only in conformity with applicable WTO commitments.

(ii) *Actual circumvention*

184. The United States asserts that the Appellate Body should reject Brazil's request for additional findings of actual circumvention of export subsidy commitments for pig meat and poultry meat.¹⁵⁴ According to the United States, Brazil has not asserted a proper claim under Article 11 of the DSU. The United States points out that Brazil does not appeal the Panel's findings that the facts did not demonstrate that subsidized exports exceeded the United States' quantitative reduction commitments for poultry meat and pig meat. Therefore, Brazil's appeal pursuant to Article 11 of the DSU is improper as it does not "stand by itself" and is not "substantiated with respect to the challenged findings".¹⁵⁵

185. The United States submits that, in any event, the data do not support the conclusions that Brazil advances. Brazil's allegation of actual circumvention related to the period July 2001 through June 2002. In contrast, quantitative data on exports under the United States' export credit guarantee programs are maintained on a fiscal year basis, which extends from 1 October to 30 September. Even if this difference between periods can be overcome, the United States argues that the actual data also support the Panel's finding that Brazil did not demonstrate actual circumvention for these products.

¹⁵⁴The United States also rejected the allegations in respect of vegetable oil made by Brazil in its other appellant's submission.

¹⁵⁵United States' appellee's submission, para. 50 (referring to Appellate Body Report, *US – Steel Safeguards*, para. 498).

(iii) *Articles 1.1 and 3.1(a) of the SCM Agreement*

186. The United States asserts that the Appellate Body should reject Brazil's request for further findings under Article 3.1(a) of the *SCM Agreement* in addition to the finding the Panel made in respect of item (j) of the Illustrative List of Export Subsidies. The United States submits that, in the light of the Panel's finding that the United States' export credit guarantee programs constitute a prohibited export subsidy because the premium rates were inadequate to cover the long-term operating costs and losses of the program, any additional findings by the Panel would have been redundant. Neither item (j) nor the Illustrative List of Export Subsidies imposes obligations *per se*; instead, the obligation regarding export subsidies is found in Articles 3.1(a) and 3.2 of the *SCM Agreement*. Furthermore, Brazil's interpretation would render the Illustrative List of Export Subsidies meaningless. In the United States' view, a practice that does not constitute a prohibited export subsidy under the standard set forth in a particular item of the Illustrative List, such as item (j), cannot constitute a prohibited export subsidy under some other standard. This was the approach advocated by Brazil in the *Brazil – Aircraft* dispute. Moreover, the United States argues that an additional finding by the Panel would have had no effect on implementation. Whether or not a separate finding of "benefit" were made under Article 1.1, the Panel's recommendations would remain precisely the same.

187. The United States also observes that Brazil misconstrues what the Panel decided. The Panel did not decline to address a claim raised by Brazil. Instead, the Panel declined to make additional *factual findings* that Brazil requested. In any event, the United States contends that Brazil misinterprets the concept of judicial economy and that, even if Brazil made a separate claim, the Panel was within the bounds of its discretion in exercising judicial economy with respect to that claim.

188. Finally, the United States disagrees with Brazil's assertion that there are sufficient undisputed facts in the record that would enable the Appellate Body to complete the analysis. According to the United States, it vigorously contested Brazil's allegations of fact in this regard and affirmatively demonstrated that the export credit guarantee programs do not confer such a benefit. The United States explains that no benefit is conferred because identical financial instruments are available in the marketplace in the form of "forfeiting"¹⁵⁶; there is no correlation between the issuance of the export credit guarantee and the ability of an importer to secure a loan; and the CCC conducts a risk assessment with respect to the foreign banks to whose risk it is exposed.

¹⁵⁶United States' appellee's submission, para. 93.

(iv) *ETI Act of 2000*

189. The United States submits that the Appellate Body should reject Brazil's request that it find that the Panel erred in concluding that Brazil did not make a *prima facie* case that the ETI Act of 2000 is inconsistent with the United States' WTO obligations.

190. According to the United States, the Appellate Body should not rule on Brazil's appeal because Brazil acknowledges that the appeal is not necessary to resolve the dispute between the parties. Brazil states that it does not ask the Appellate Body to complete the analysis with respect to its claims. Brazil, therefore, is not asking the Appellate Body to make findings that would result in DSB rulings and recommendations with respect to the ETI Act of 2000.¹⁵⁷ For that reason alone, the Appellate Body should decline to decide Brazil's appeal.

191. The United States contends that, in any event, Brazil did not make a *prima facie* case with respect to the ETI Act of 2000. Brazil simply did not present any evidence at all regarding the ETI Act of 2000 itself. In its submission, Brazil gave a brief description of the proceedings in the *US – FSC (Article 21.5 – EC)* dispute and then asked the Panel "to apply the reasoning as developed by the panel and as modified by the Appellate Body in that case *mutatis mutandis*".¹⁵⁸ In essence, therefore, Brazil was not asking the Panel to make an objective assessment of the ETI Act of 2000, but merely to adopt findings from a previous proceeding. The Panel acted properly under the DSU, including Article 11, by declining to find that the "short shrift" that Brazil gave to the ETI Act of 2000 satisfied Brazil's burden to make its *prima facie* case concerning that Act.¹⁵⁹

192. The United States asserts that the rules of burden of proof in the WTO are well settled. Contrary to Brazil's arguments, a finding of inconsistency in one dispute does not establish a finding of inconsistency in another dispute between different parties. Such an approach would in effect impose the concept of *stare decisis* on the WTO dispute settlement system. The United States also disagrees with Brazil's assumption that it is legally impossible for a party to argue that an identical measure subject to identical claims that were successful in a previous WTO dispute is WTO-consistent. The reasoning of a panel or the Appellate Body in one dispute is not binding on another panel or the Appellate Body in a separate dispute. Furthermore, while the measure may remain the

¹⁵⁷United States' appellee's submission, paras. 101-104 (referring to Appellate Body Report, *US – Steel Safeguards*, para. 483 and Appellate Body Report, *US – Wool Shirts and Blouses*, p. 19, DSR 1997:1, 323 at 340).

¹⁵⁸*Ibid.*, para. 106 (quoting Brazil's written submission to the Panel, paras. 315-327).

¹⁵⁹*Ibid.*, para. 12.

same, the circumstances may change. Thus, irrespective of the ruling in the previous dispute, Brazil had the burden of establishing a *prima facie* case.

193. Finally, the United States argues that the Appellate Body's reasoning in *Mexico – Corn Syrup (Article 21.5 – US)* does not support Brazil's approach. Brazil exaggerates the Appellate Body's statements in that Report and does not explain why a complainant's obligation to make a *prima facie* case should be interpreted similarly to a panel's obligation to set forth its basic rationale pursuant to Article 12.7 of the DSU.

E. *Arguments of the Third Participants*1. Argentina(a) Article 13(a) of the *Agreement on Agriculture*

194. Argentina considers that green box measures must respect the "fundamental requirement" of paragraph 1 of Annex 2 of avoiding trade-distorting or production effects. Argentina submits that this requirement is additional to compliance with the policy-specific criteria of paragraph 6.

(i) *Article 13(a) of the Agreement on Agriculture – Planting Flexibility Limitations*

195. Argentina submits that production flexibility contract payments and direct payments do not comply with paragraph 6(b) of Annex 2 of the *Agreement on Agriculture* because the amount of these payments is related to the type of production after the base period. Argentina disagrees with the United States' view that paragraph 6(b) does not prevent the conditioning of payment upon fulfilling the requirement not to produce certain crops. Argentina considers that the Panel rightly affirmed that "the planting flexibility limitations provide a monetary incentive for payment recipients not to produce the prohibited crops".¹⁶⁰ For Argentina, there is effectively little difference between a "positive" and a "negative" list of permitted crops. The context provided by paragraphs 11(b) and 11(e) of Annex 2 supports this view. Although Argentina agrees with the United States that paragraph 6(b) ensures that the amount of payments must not be used to induce a recipient to produce a particular type of crop, the production flexibility contract and direct payments fail to meet this requirement. Argentina considers that the flexibility enjoyed by producers to plant different crops is illusory. The amount of the payments depends on the type of production. The growing of fruits and vegetables is prohibited under these programs, with the effect of channelling production towards other, permitted crops.

¹⁶⁰Argentina's third participant's submission, para. 15 (quoting Panel Report, para. 7.386).

(ii) *Article 13(a) of the Agreement on Agriculture – Base Period Update*

196. Argentina agrees with Brazil that the option under the FSRI Act of 2002 to update base acres is inconsistent with paragraph 6(a) of Annex 2 of the *Agreement on Agriculture*. Argentina submits

that the term "defined" in paragraph 6(a) refers to the need for the base period to be clearly determined. Likewise, the term "fixed" refers to the need for the base period to be defined in terms that prevent it from being shifted or modified *a posteriori*. The term "fixed" indicates that payments made in accordance with the criteria stipulated in paragraph 6(a) must always rely on the same base period, and no change is possible. Paragraph 6(a) thus allows Members to identify their own base period; however, once that period is determined, the period must remain fixed. Otherwise, the choice of the word "a" in paragraph 6(a) would be difficult to explain. Argentina thus agrees with Brazil that if the structure, design, and eligibility criteria of an original measure containing a "fixed base period" and the structure, design, and eligibility criteria of its successor have not been significantly modified, then it is not legitimate to update the "fixed base period" under the successor measure. Accordingly, the terms of the direct payment program under the FSRI Act of 2002 are inconsistent with the requirements set forth in paragraph 6(a) of Annex 2.

(b) *Significant Price Suppression under Article 6.3(c) of the SCM Agreement*

197. Argentina agrees with Brazil that the market examined in assessing significant price suppression under Article 6.3(c) of the *SCM Agreement* may be a world market, and that a panel need not quantify precisely the amount of a subsidy in conducting such an assessment.¹⁶¹

(c) *World Market Share under Article 6.3(d) of the SCM Agreement*

198. Argentina agrees with Brazil that the words "world market share" in Article 6.3(d) of the *SCM Agreement* refer to the subsidizing Member's share of the world export market.¹⁶²

(d) *Step 2 Payments to Domestic Users*

199. Argentina agrees with the Panel's conclusion that Step 2 payments to domestic users of upland cotton constitute a subsidy contingent upon the use of domestic over imported goods that is prohibited by Articles 3.1(b) and 3.2 of the *SCM Agreement*, and that WTO Members are not authorized by the *Agreement on Agriculture* to provide such subsidies.

¹⁶¹ Argentina's statement at the oral hearing.

¹⁶² *Ibid.*

(e) Export Credit Guarantees – Articles 10.1 and 10.2 of the *Agreement on Agriculture*

200. Argentina submits that the United States' export credit guarantee programs constitute export subsidies in breach of the anti-circumvention provision contained in Article 10.1 of the *Agreement on Agriculture* and, consequently, they are inconsistent with Article 8 and are not exempt from action under Article 13(c) of that Agreement. Argentina disagrees with the United States' view that no disciplines apply to export credit guarantee programs. On the contrary, under the terms of Article 10.1 of the *Agreement on Agriculture*, export credit guarantee programs constituting export subsidies should not be applied in a manner that results in, or threatens to lead to, circumvention of export subsidy commitments.

(f) Export Credit Guarantees – Articles 1 and 3.1(a) of the *SCM Agreement*

201. According to Argentina, the Panel's findings in respect of the United States' export credit guarantee programs are not complete. In not finding that such programs are also subsidies in accordance with the definition contained in Article 1 of the *SCM Agreement* and the prohibition in Article 3.1(a) of the same Agreement, the Panel did not bear in mind that different obligations stem from those Articles and that, similarly, the course of implementation adopted by a Member in respect of a finding of inconsistency only on the basis of item (j) of the Illustrative List of Export Subsidies may be different. Accordingly, Argentina contends that a finding of inconsistency in respect of the United States' export credit guarantees programs is also possible and should be made on the basis of Articles 1 and 3.1(a) of the *SCM Agreement*.

2. Australia

(a) Article 13(a) of the *Agreement on Agriculture* – Planting Flexibility Limitations

202. Australia requests that the Appellate Body uphold the Panel's conclusion that production flexibility contract payments, direct payments, and the legislative and regulatory provisions that establish and maintain the direct payment program, do not fully conform to paragraph 6(b) of Annex 2 of the *Agreement on Agriculture*. Australia submits that making a payment conditional upon the non-production of a particular product is one way in which a Member can relate the "amount of ... payment[]" to the current "type or volume of production". Australia contends that the argument advanced by the United States would introduce an exception into paragraph 6(b) of Annex 2 that has no textual basis. Australia submits that the Panel's interpretation does not prevent payments from being disallowed in the case of illegal production because reducing the payment to zero would be

based on the illegality of the activity, not "the type or volume of production". In addition, a Member could otherwise justify such a measure pursuant to Article XX of the GATT 1994.

(b) Article 13(a) of the *Agreement on Agriculture* – Base Period Update

203. Australia submits that the updating of base acres by the FSRI Act of 2002 means that the direct payments are not green box measures. Australia argues that the meaning of paragraph 6(b) of Annex 2 of the *Agreement on Agriculture* is that, once a base period has been "defined and fixed" pursuant to paragraph 6(a), decoupled income support payments may not be "connected" to or "[found]ed, built[er] or construct[er]ed" on the type of production or the volume of production undertaken by a producer in a later period.¹⁶³ Australia says that the Panel found that the direct payments program is the successor to the production flexibility contract program and that the two programs are identical in a number of important respects. The option under the FSRI Act of 2002 for producers to update their base acres is not consistent with the requirement of paragraph 6(a) that there be one "defined and fixed base period".

(c) Significant Price Suppression under Article 6.3(c) of the *SCM Agreement*

204. Australia refers to the United States' argument that the Panel failed to set out the findings of fact, the applicability of relevant provisions, and the basic rationale behind certain of its findings and recommendations regarding Article 6.3(c) of the *SCM Agreement*, as required by Article 12.7 of the DSU.¹⁶⁴ According to Australia, this argument suggests that the Panel failed to make an objective assessment of the matter before it, as required by Article 11 of the DSU. Australia notes that the Appellate Body has recognized the discretion of a panel in choosing the evidence on which it relies.¹⁶⁵

(d) Step 2 Payments to Domestic Users and Exporters

205. Australia requests that the Appellate Body uphold the Panel's conclusions that Step 2 payments to domestic users constitute subsidies that are inconsistent with the requirements of Article 3.1(b) of the *SCM Agreement*.

¹⁶³ Australia's third participant's submission, para. 42 (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 1, p. 187 and Vol. 2, p. 2534 in relation to the words "based on" and, "related to" in paragraph 6(b) of Annex 2 to the *Agreement on Agriculture*).

¹⁶⁴ *Ibid.*, para. 19 (referring to the United States' appellant's submission, paras. 150 and 322-331).

¹⁶⁵ *Ibid.*, para. 21 (referring to Appellate Body Report, *EC – Hormones*, para. 135).

206. Australia submits that the Appellate Body should also uphold the Panel's conclusions that Step 2 payments to exporters are inconsistent with Articles 3.3 and 8 of the *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement*. In the event that the Appellate Body determines that the Step 2 program is not export-contingent, Australia requests that the Appellate Body find that the Step 2 program *as a whole* is contingent upon the use of domestic over imported goods within the meaning of Article 3.1(b) of the *SCM Agreement*. Furthermore, in that case, the Appellate Body should find that the chapeau to Article 3.1 of the *SCM Agreement* does not serve to exempt such local content subsidies from the application of Article 3.1(b) of that Agreement.

(e) Export Credit Guarantees – Articles 10.1 and 10.2 of the *Agreement on Agriculture*

207. Australia disagrees with the United States' argument that export credit guarantees are excluded from the application of Article 10.1 of the *Agreement on Agriculture* and Article 3.1(a) of the *SCM Agreement*. According to Australia, the United States has incorrectly applied Articles 31 and 32 of the *Vienna Convention* to the interpretation of Article 10.1 of the *Agreement on Agriculture*. Article 10.1 applies to all "[e]xport subsidies not listed in paragraph 1 of Article 9". The meaning of this provision is clearly discernible from its text and it does not provide for any exceptions. The context of Article 10.2 does not support an interpretation that would be contrary to its plain words, particularly because it is not constructed as an exception provision. The object and purpose of Article 10.1 relate to the prevention of circumvention of commitments, in relation to *all* export subsidies other than those listed in Article 9.1 of the *Agreement on Agriculture*. Furthermore, the application of Article 10.1 to export credit guarantees defined as export subsidies does not lead to a result that is manifestly unreasonable because not all export credit guarantees are export subsidies within the meaning of the *Agreement on Agriculture* and the *SCM Agreement*. It is open to the United States, within the existing WTO framework, to design and maintain measures that fall outside the definition of an export subsidy, which is, in fact, what the United States asserts it has done. In contrast, acceptance of the United States' arguments could lead to a result that is manifestly absurd or unreasonable by encouraging other WTO Members to seek to avoid the anti-circumvention obligations of Article 10.1 of the *Agreement on Agriculture*.

208. Australia also rejects the United States' contention that Article 21.1 of the *Agreement on Agriculture* and the chapeau to Article 3.1 of the *SCM Agreement* render Article 3.1(a) of the *SCM Agreement* inapplicable to export credit guarantee programs.

3. Benin and Chad

(a) Significant Price Suppression under Article 6.3(c) of the *SCM Agreement*

209. Benin and Chad agree with Brazil that the Panel correctly found that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*. Benin and Chad contend that many of the United States' arguments regarding Article 6.3(c) relate to factual findings by the Panel that are not subject to appellate review in the absence of a claim by the United States that the Panel failed to comply with Article 11 of the DSU.

210. Benin and Chad agree with the Panel's finding that it was not required to quantify precisely the amount of the subsidy in assessing Brazil's claim under Article 6.3(c) of the *SCM Agreement*, and that the amount of a subsidy is not necessarily determinative in such an assessment. This is consistent with the different purposes of Parts III and V of the *SCM Agreement*.

(b) World Market Share under Article 6.3(d) of the *SCM Agreement*

211. Benin and Chad support the request by Brazil that the Appellate Body reverse the Panel's interpretation of the term "world market share" in Article 6.3(d) of the *SCM Agreement*. Benin and Chad agree with Brazil that "world market share" means world market share of *exports*. If the Appellate Body adopts this interpretation, Benin and Chad request the Appellate Body to complete the analysis under Article 6.3(d) and to find that the effect of the price-contingent subsidies was an increase in the world market share of the United States contrary to Article 6.3(d). In turn, Benin and Chad ask the Appellate Body to find that they have also suffered serious prejudice under Article 6.3(d) as a result of the increase in the United States' world market share of exports.

212. According to Benin and Chad, the Panel's interpretation of "world market share" as world market share of *production* inappropriately shifts the inquiry away from the *effect* of the subsidy towards unrelated factors, such as production levels in third country markets. A subsidy may have the effect of increasing significantly the exports of a Member, even though the Member's world share of production remains stable or diminishes. Therefore, in the submission of Benin and Chad, the Panel's interpretation could lead to a situation where changes in the supply by a third country determine whether a subsidizing Member's world market share increases or decreases.

213. Benin and Chad state that, if the Appellate Body rejects the Panel's interpretation of "world market share" under Article 6.3(d), there are sufficient undisputed facts on the record for the Appellate Body to complete the analysis and to find that the United States acted inconsistently with Article 6.3(d). The evidence before the Panel indicates that those Members that have lost market

share as a result of the price-contingent subsidies include, at least, Brazil and the "Francophone African nations of Benin and Chad".¹⁶⁶ Benin and Chad disagree with the Panel's finding that "the serious prejudice under examination by a WTO panel is the serious prejudice experienced by the complaining Member".¹⁶⁷

214. Benin and Chad argue that the Appellate Body should take into account the impact of United States upland cotton subsidies on the "fragile economies of West and Central Africa"¹⁶⁸, as reflected in the Panel's findings and evidence on the record. Benin and Chad point out that Article 24.1 of the DSU, which requires particular consideration to be given to the special situation of least-developed country Members, would be given meaning if the Appellate Body acknowledged that the increase in the United States' world market share caused serious prejudice to Benin and Chad by reducing their market share. Furthermore, nothing in the text of Article 6.3(d) limits a finding of serious prejudice to the complaining party. Therefore, Benin and Chad urge the Appellate Body to draw conclusions under Article 6.3(d) that would require the United States to withdraw the subsidy or remove the adverse effects, not only with respect to Brazil, but also with respect to Benin and Chad.

(c) Export Credit Guarantees – Articles 1 and 3.1(a) of the *SCM Agreement*

215. Benin and Chad support Brazil's position that the Panel improperly exercised judicial economy by refusing to address Brazil's claim that the United States violated Articles 1.1 and 3.1(a) of the *SCM Agreement* with respect to export credit guarantees. Benin and Chad also support Brazil's request that the Appellate Body complete the analysis as it has sufficient factual findings before it to do so.

216. Benin and Chad explain that, under item (j) of the Illustrative List of Export Subsidies, Brazil's claim is that the export credit guarantee programs operate at a loss or below the cost to the government. In contrast, under Article 3.1(a), Brazil's claim is that the programs are financial contributions that confer a benefit on recipients within the meaning of Article 1.1 of the *SCM Agreement* and that they are contingent upon export performance. Thus, Brazil's claims under item (j) of the Illustrative List of Export Subsidies and Article 3.1(a) were distinct, and the Panel's

¹⁶⁶Benin and Chad's third participants' submission, para. 85. (emphasis omitted)

¹⁶⁷*Ibid.*, para. 6 (quoting Panel Report, para. 7.1403).

¹⁶⁸*Ibid.*, para. 9.

refusal to address Brazil's claim under Article 3.1(a) leaves an important and distinct claim unresolved. Accordingly, it was improper for the Panel to have exercised judicial economy.¹⁶⁹

4. Canada

(a) Article 13(a) of the *Agreement on Agriculture – Planting Flexibility Limitations*

217. Canada considers that the Panel was correct in finding that production flexibility contract payments and direct payments do not meet the requirements of paragraph 6(b) of Annex 2 of the *Agreement on Agriculture*. For Canada, nothing in the text of paragraph 6(b) supports the distinction the United States seeks to draw between "positive" and "negative" effects on production. If payments are conditioned on a recipient not undertaking a type of production, then the payment is related to the type of production. Canada thus agrees with the Panel's interpretation that paragraph 6(b) excludes any "[t]ype] of relationship between the amount of such payments and the type of production after the base period".¹⁷⁰ Canada argues that this approach is supported by the object and purpose of Annex 2 and the context provided by the fundamental requirement set out in paragraph 1 of Annex 2.

218. Canada agrees with the United States that the fundamental requirement in paragraph 1 of Annex 2 is relevant context in understanding the criterion in paragraph 6(b) that the measure not be related to the type or volume of production. However, a Member does not have an independent basis for claiming that the measure qualifies as a "green box" measure because it has minimal trade-distorting effects. Canada disagrees with the United States' conclusion, based on its interpretation of paragraph 6(e), that a Member is not prohibited under paragraph 6(b) from conditioning payment on non-production of a particular product. Canada considers that paragraph 6(e) is a prohibition against requiring production as a condition of payment, but does not necessarily authorize a Member to impose a requirement not to produce a particular crop. With regard to the planting flexibility limitations under the production flexibility contract payment and direct payment programs, Canada disagrees with the United States that the amount of payments "does not relate to fruit or vegetable production since for that base act there would be *no payment at all*".¹⁷¹ For Canada, this interpretation is contrary to the ordinary meaning of the term "related to" and leads to the unreasonable result that a Member could circumvent the requirement in paragraph 6(b) by

¹⁶⁹Benin and Chad's third participants' submission, paras. 105-108 (referring to Appellate Body Report, *Australia – Salmon*, para. 223 and Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 133).

¹⁷⁰Canada's third participant's submission, para. 13 (quoting Panel Report, para. 7.366).

¹⁷¹*Ibid.*, para. 20 (quoting the United States' appellant's submission, para. 26). (original emphasis)

encouraging certain types of production as long as it does so through a negative list by excluding certain other types of production.

(b) Article 13(a) of the *Agreement on Agriculture* – Base Period Update

219. Canada argues that the direct payments do not fully conform to paragraph 6(a) of Annex 2 of the *Agreement on Agriculture* because of the base period update in the FSRI Act of 2002. Canada submits that the ordinary meaning of the terms "defined and fixed base period" in paragraph 6(a) indicates that the base period cannot vary or change. This is confirmed by the context provided by paragraphs 6(b) and (d), which refer to "any year after the base period", as well as the object and purpose of paragraph 6, which is to identify the types of payments that are minimally trade-distorting. Canada contends that, as the Panel found that direct payments under the FSRI Act of 2002 are closely related to and a successor to the production flexibility contract payments, the base period for direct payments should not be different from the base period for production flexibility contract payments. The fact that payments are provided under new legislation does not in itself allow a modification to the base period under the predecessor program. Otherwise, the requirement that there be a "fixed base period" would become meaningless. By allowing updating of base acreage, the United States is altering the base period contrary to paragraph 6(a).

(c) Export Credit Guarantees – Articles 10.1 and 10.2 of the *Agreement on Agriculture*

220. Canada submits that the Panel correctly found that, to the extent that export credit guarantees meet the definition of export subsidies, they will be subject to the anti-circumvention disciplines of Article 10.1 of the *Agreement on Agriculture*. The United States' argument that Article 10.2 of the *Agreement on Agriculture* exempts export credit guarantees from the subsidy disciplines under that Agreement has no basis in the text, context, object and purpose, or negotiating history. Canada asserts that the text of Article 10.2 does not explicitly indicate an intention to exclude the application of other, existing disciplines. Indeed, such an interpretation would contradict the stated object and purpose of Article 10 as a whole, which is the "Prevention of Circumvention of Export Subsidy Commitments". Furthermore, the fact that export credit guarantee programs may not be subject to the notification requirement of the *Agreement on Agriculture* does not lead to the conclusion that they are not subject to the other disciplines of that Agreement.

221. Canada also agrees with the Panel's conclusion that the United States violated Articles 3.3 and 8 of the *Agreement on Agriculture* by providing export subsidies otherwise than in conformity with that Agreement with respect to upland cotton and other unscheduled commodities. In addition, Canada states that the Panel's interpretation of Article 10.1 with respect to scheduled products is consistent with the Appellate Body's analysis in *US – FSC*.¹⁷²

(d) Export Credit Guarantees – Articles 1 and 3.1(a) of the *SCM Agreement*

222. Canada asserts that, if the Appellate Body reverses the Panel's finding that the United States' export credit guarantee programs constitute *per se* prohibited export subsidies under item (j) of the Illustrative List of Export Subsidies, it will still be necessary to consider whether the export credit guarantee programs constitute export subsidies under Articles 1 and 3.1(a) of the *SCM Agreement*. Even if the United States' export credit programs charge adequate fees under the item (i) standard, they may still confer an export subsidy. If they did, the export credit guarantees would have to be provided in a manner consistent with Article 10.1 of the *Agreement on Agriculture*.

5. China

(a) Terms of Reference – Expired Measures

223. China submits that the Panel was correct to find that expired production flexibility contract and market loss assistance payments were within the Panel's terms of reference. The Panel's interpretation of Articles 4.2 and 6.2 of the DSU is in accordance with the text, context, and object and purpose of the DSU, as well as the intention of the drafters. China recalls that Article 4.2 of the DSU indicates that consultations are to cover "any representations made by another Member concerning measures affecting the operation of any covered agreement taken within the territory of the former". China "agrees with the Panel that based on the analysis of the context and the object of Article 4.2, the term 'affecting' in Article 4.2 is used as a gerund, describing the way in which they relate to a covered agreement, and has no temporal significance".¹⁷³ China notes that Brazil's claims in this case relate to serious prejudice under the provisions of the *SCM Agreement* and the GATT 1994. China agrees with the panel in *Indonesia – Autos* that, "[i]f ...past subsidies were not relevant to [a] serious prejudice analysis as they were 'expired measures' ..., it is hard to imagine any situation where a panel would be able to determine the existence of actual serious prejudice".¹⁷⁴

¹⁷²Canada's third participant's submission, para. 40 (referring to Appellate Body Report, *US – FSC*, para. 152).

¹⁷³China's third participant's submission, para. 19.

¹⁷⁴*Ibid.*, para. 26 (quoting Panel Report, *Indonesia – Autos*, para. 14,206).

China submits that neither the context cited by the United States nor the decisions of the panel and Appellate Body in *US – Certain EC Products* support the view that expired measures may not fall within the terms of reference of a panel.

- (b) Article 13(b) of the *Agreement on Agriculture* - Interpretation of "support to a specific commodity"

224. China supports the Panel's finding that the phrase "support to a specific commodity" in Article 13(b) of the *Agreement on Agriculture* does not mean "product-specific domestic support". China submits that the word "specific" in Article 13(b)(ii) is inserted to avoid lump-sum treatment of measures generally applicable to a number of commodities. Unlike the phrase "product-specific support", the phrase "support to a specific commodity" refers to the level of support delivered to a specific commodity, thus combining both product-specific support and the portion of support attributable to upland cotton under a program that is available to a number of products.

- (c) Terms of Reference – Export Credit Guarantees

225. China submits that the Appellate Body should uphold the Panel's conclusion that export credit guarantees to facilitate the export of United States agricultural commodities other than upland cotton were within the Panel's terms of reference. According to China, the Panel correctly concluded that Brazil identified export credit guarantees to agricultural commodities other than upland cotton in its request for consultations. During the consultations, Brazil also posed questions to the United States on the export credit guarantees that related to agricultural commodities other than upland cotton. These questions did not expand the scope of the consultations request, but merely clarified its content. In addition, China states that Brazil's recognition that the United States objected to the questions relating to agricultural commodities other than upland cotton does not lead to the conclusion that consultations were not held on the subject. Finally, China asserts that a WTO Member cannot refuse to respond to questions during consultations on the basis of its own uncertainty as to the scope of the consultations.

6. European Communities

- (a) Article 13(a) of the *Agreement on Agriculture* – Planting Flexibility Limitations

226. The European Communities supports the United States' appeal of the Panel's finding that planting flexibility limitations disqualify a measure from the coverage of paragraph 6 of Annex 2 of the *Agreement on Agriculture*. The European Communities notes that the United States has placed limitations on the crops that may be grown by farmers receiving production flexibility contract

payments and direct payments. In doing so, the United States ensures fair competition domestically and limits distortions internationally. If upheld, the Panel's findings would have the perverse effect of increasing subsidization and the likelihood of trade distortions.

227. The European Communities observes that paragraph 6(b) prevents the amount of the payments from being related to the type of production; it does not address eligibility for payments. With this in mind, the European Communities submits that "the fact of making ineligible for payments the land used to produce a certain commodity is not incompatible with paragraph 6(b)".¹⁷⁵ Furthermore, the Panel correctly noted that paragraphs 6(b) and 6(c) lay down distinct requirements and that each of them must be given meaning. The European Communities considers that the Panel's interpretation of paragraph 6(b) would render redundant paragraph 6(c). The Panel's reading is that any payment conditional upon a production requirement (which, as such, is incompatible with paragraph 6(e)) would be deemed to be "related to" the "volume" of production and would therefore be incompatible with paragraph 6(b). The European Communities argues that the Panel should not have relied upon paragraph 11 of Annex 2 because that provision appears in a context very different from that of the provisions of paragraph 6.

- (b) Article 13(a) of the *Agreement on Agriculture* – Base Period Update
228. With regard to Brazil's conditional cross-appeal regarding base period updates, the European Communities notes that the Panel made factual findings that there was no evidence to suggest that farmers expected further updates in future years. The European Communities does not consider that paragraph 6(a) of Annex 2 of the *Agreement on Agriculture* precludes adjustments to base periods, although it agrees with Brazil that a "defined and fixed" base period cannot be determined from the perspective of five-yearly subsidization legislation, but rather should be viewed in a longer-term perspective. The European Communities considers that it cannot be open to a Member to resort to wholesale updating of base periods by linking the criteria of "defined and fixed" to specific legislative packages.

- (c) Article 13(b) of the *Agreement on Agriculture*

229. The European Communities supports the United States' request for the Appellate Body to reverse the Panel's interpretation of Article 13(b) of the *Agreement on Agriculture*, particularly in respect to the methodology for calculating support and the meaning of "support to a specific commodity". With regard to the methodology, the European Communities agrees with the United States that the Panel should not have used budgetary outlays to calculate support "decided" in respect

¹⁷⁵European Communities' third participant's submission, para. 15.

of price-based measures, but rather should have used price gap methodology. The European Communities contends that this approach is crucial for the interpretation of the specific term "decided", in contrast to the term "granted". The European Communities also agrees with the United States that the Panel was incorrect in finding that support under schemes based on historical production of specific crops could be considered "support to a specific commodity" in the implementation period in the sense of Article 13(b)(ii).

(d) Significant Price Suppression under Article 6.3(c) of the *SCM Agreement*

230. In relation to the United States' arguments regarding the quantification of subsidies, the European Communities agrees with Brazil that, in assessing significant price suppression under Article 6.3(c) of the *SCM Agreement*, it is not necessary to determine the precise amount of the subsidy or the amount of the benefit conferred on the subsidized product. This is consistent with the differences between Parts III and V of the *SCM Agreement*. Paragraph 7 of Annex IV of the *SCM Agreement*, to which the United States refers, is an exception to the general rule that a panel need not quantify or allocate a subsidy (other than a pre-WTO subsidy) to the products concerned.

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231. The European Communities contests the United States' arguments regarding past "recurring" subsidies. Article 6.3(c) is drafted in the present tense and therefore should apply to the past, present, and future. The European Communities asserts that a subsidy comprises an act (a financial contribution) and that it may have an effect on the recipient (a benefit) and an effect on the market and other Members (adverse effects). However, the United States erroneously equates the concepts of "benefit" and "adverse effects". The subsidies challenged in the present dispute are programs that continue and that therefore may have adverse effects in the future, even if they confer a benefit in only one particular year. Therefore, the European Communities considers that the Panel correctly included past recurring subsidies in its analysis under Article 6.3(c). However, the European Communities maintains that it would have been "desirable"¹⁷⁶ for the Panel to distinguish between programs that had expired and programs that were still in force when the Panel was established.

(e) Relationship between the *Agreement on Agriculture* and the *SCM Agreement*

232. The European Communities raises an issue concerning the Panel's jurisdiction that it considers the Appellate Body should take up on its own motion. According to the European Communities, the *SCM Agreement* does not apply to domestic support and export subsidies in

respect of agricultural products because the *Agreement on Agriculture* contains "provisions dealing specifically with the same matter".¹⁷⁷

(f) Step 2 Payments to Domestic Users

233. The European Communities agrees with the United States' claim that the Panel erred in finding that Step 2 payments to domestic users are inconsistent with Article 3.1(b) of the *SCM Agreement*. In addition to endorsing the arguments put forward by the United States, the European Communities argues that the Panel incorrectly sought an explicit carve out from Article 6.3 of the *Agreement on Agriculture* for import substitution subsidies, when such a carve out is unnecessary in the light of Article 21.1 of that Agreement and the introductory phrase of Article 3.1 of the *SCM Agreement*. The European Communities submits that paragraph 7 of Annex 3 of the *Agreement on Agriculture* recognizes that WTO Members have a right to provide import substitution subsidies. The Panel's interpretation to the contrary renders the language of paragraph 7 of Annex 3 redundant.

7. India

234. Pursuant to Rule 24 of the *Working Procedures*, India chose not to submit a third participant's submission. In its statement at the oral hearing, India disagreed with the United States that Brazil had to establish the amount of the price-contingent subsidies that benefit upland cotton in making its claim of serious prejudice under Articles 5(c) and 6.3 of the *SCM Agreement*.

8. New Zealand

(a) Article 13(a) of the *Agreement on Agriculture* – Base Period Update

235. New Zealand supports Brazil's contention that the direct payments under the FSRI Act of 2002 do not meet the criteria set out in paragraph 6(a) of Annex 2 of the *Agreement on Agriculture*. According to New Zealand, the factual findings made by the Panel establish that direct payments cannot be green box payments because farmers had an opportunity to update base acreage, contrary to this provision. New Zealand notes that the language and context of paragraph 6(a) contemplate a single base period that is fixed and unchanging to ensure that such support is clearly de-linked from production. To conclude otherwise would create an internal inconsistency in paragraph 6, because a Member could avoid obligations under paragraphs 6(b), 6(c), and 6(d) not to link payments to production, prices, or factors of production employed in subsequent years, by establishing a new base period from time to time. New Zealand observes that the Panel found that the direct payment

¹⁷⁶European Communities' third participant's submission, para. 61.

¹⁷⁷European Communities' third participant's submission, para. 6 (quoting Appellate Body Report, *EC – Bananas III*, para. 155).

program is a successor to the production flexibility contract program and that the base period update had the effect of increasing the level of payments under the program.

(b) Article 13(b) of the *Agreement on Agriculture*

236. New Zealand contests the United States' appeal of the Panel's finding that the United States' measures at issue are not exempt from action pursuant to Article 13(b)(ii) of the *Agreement on Agriculture*. New Zealand argues that Members drafting the proviso to Article 13(b) were principally concerned with limiting the effect of domestic support measures on trade. New Zealand argues that the manner in which "support" is identified and calculated in the comparison required by Article 13(b)(ii) must reflect Members' intentions to limit the effects of such measures to those that existed in the 1992 marketing year and to ensure that measures are not exempt from actions when their effect is a significantly higher level of trade distortion in the implementation period than in the 1992 marketing year.

(i) *Calculation methodology for price-based measures*

237. New Zealand considers that the Appellate Body should uphold the Panel's finding that, on the facts of this case, budgetary outlays provide an appropriate measurement of support for the purposes of the comparison required by Article 13(b)(ii). New Zealand argues that a Member may not justify a failure to meet its obligations under the *Agreement on Agriculture* on the ground that it has adopted measures that rely on factors beyond the government's control. If a Member adopts a non-green box domestic support measure that determines the amount of support provided on the basis of factors the government cannot control, then the Member must accept the risk that support granted in the implementation period may be in excess of that decided in the 1992 marketing year. Furthermore, New Zealand disagrees with the argument advanced by the United States that only a price gap calculation can reflect support "decided" by the United States' price-based measures. New Zealand argues that this argument would read the term "grant" out of Article 13(b)(ii) altogether.

(ii) *Interpretation of "support to a specific commodity"*

238. New Zealand argues that the Appellate Body should reject the United States' argument that Article 13(b)(ii) of the *Agreement on Agriculture* requires a comparison of only "product-specific" support. For New Zealand, the chapeau of Article 13(b) makes it clear that the measures subject to the proviso of Article 13(b)(ii) are all "domestic support measures that conform fully to the provisions of Article 6" of the *Agreement on Agriculture* (that is, both product-specific and non-product-specific support to upland cotton). The use of the word "specific" in Article 13(b)(ii) refers only to the fact that the comparison is to be made on a commodity-by-commodity basis. In New Zealand's

view, the Panel correctly found that "support to a specific commodity" means all support to a commodity, whether product-specific or not. New Zealand also agrees with the Panel's finding that measures that "identify and allocate support based on an express linkage to specific commodities"¹⁷⁸ provide support to those commodities within the meaning of Article 13(b)(ii). Accordingly, even a measure that provides support to a number of different commodities also provides support to those specific commodities individually. New Zealand adds that not only do the words "product-specific support" not appear in Article 13(b)(ii), but the concept of product-specific support is not relevant to the comparison under this provision because Article 13(b)(ii) requires an analysis that is fundamentally different from that required under those provisions of the *Agreement on Agriculture* that distinguish between product-specific and non-product-specific support.

239. Finally, New Zealand disagrees with the United States' assertion that counter-cyclical payments and market loss assistance payments are "decoupled". As the Panel recognized, the amount of payment under these programs is clearly linked to current prices, which means that they cannot be green box measures in terms of Annex 2 of the *Agreement on Agriculture*.

(c) Significant Price Suppression under Article 6.3(c) of the *SCM Agreement*

240. New Zealand agrees with Brazil that the Panel correctly found that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c), constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*.

241. New Zealand agrees with Brazil that the term "in the same market" in Article 6.3(c) can include a world market, although this does not preclude the possibility of other markets. New Zealand also agrees that, although a world market does not necessarily exist for every product, a world market and a world price do exist for upland cotton.

242. New Zealand submits that the Panel was correct in rejecting the United States' argument that the price-contingent subsidies did not suppress prices because, in the absence of these subsidies, new suppliers would have increased supply and maintained the world price. In response to the United States' arguments regarding the effect of the subsidies on the planting decisions of farmers, New Zealand argues that this effect is a key aspect of the Panel's analysis under Article 6.3(c), which led it to conclude that the subsidies insulated United States cotton producers from declines in world prices. Moreover, the Panel correctly found that the gap between total production costs and market revenue

¹⁷⁸New Zealand's third participant's submission, para. 3.16 (quoting Panel Report, para. 7.484).

constituted evidence that the price-contingent subsidies enabled United States upland cotton producers to increase supply, leading to price suppression in the world market.

243. New Zealand agrees with Brazil that a panel is not required, in assessing significant price suppression under Article 6.3(c), to quantify precisely the amount of the subsidy. As the Panel found, claims under Parts III and V of the *SCM Agreement* differ, and the quantitative and pass-through methodologies applicable under Part V are not necessarily transferable to Part III. Although the magnitude of a subsidy may be relevant in some cases, it is not necessarily determinative of the nature or extent of the effects of the subsidy.

244. New Zealand disagrees with the United States' arguments regarding past recurring subsidies, which would effectively preclude Members from bringing claims of serious prejudice against recurring subsidies, even though payments under subsidy programs over an extended period can have effects in later years.

(d) World Market Share under Article 6.3(d) of the *SCM Agreement*

245. New Zealand supports Brazil's appeal of the Panel's finding that the "world market share" of the subsidizing Member under Article 6.3(d) refers to the share of the world market supplied by the subsidizing Member. Defining "world market share" as including all production, instead of only exports, distracts from the trade focus of the *SCM Agreement* and subverts the underlying rationale of Article 6.3(d). New Zealand supports Brazil's request for the Appellate Body to complete the analysis under Article 6.3(d).

(e) Export Credit Guarantees – Articles 10.1 and 10.2 of the *Agreement on Agriculture*

246. New Zealand asserts that the Panel was correct in finding that export credit guarantee programs are subject to the non-circumvention obligation under Article 10.1 of the *Agreement on Agriculture*, and that the United States' export credit guarantee programs provide export subsidies that breach Article 10.1 and are not exempt from action under the *SCM Agreement*. In New Zealand's view, Article 10.1 clearly applies to export credit guarantee programs that involve the granting of export subsidies. Article 10.2 does not create any exception that may contradict the clear meaning of Article 10.1. The United States' interpretation would create a loophole for WTO Members to circumvent their export subsidy reduction commitments through export credit guarantee programs. In such a case, New Zealand observes that Article 10.2 would, itself, circumvent the anti-circumvention provisions.

(f) Export Credit Guarantees – Articles 1 and 3.1(a) of the *SCM Agreement*

247. New Zealand agrees with Brazil that the Panel erred in exercising judicial economy by refusing to make a finding relating to the United States' export credit guarantee programs under Articles 1.1 and 3.1(a) of the *SCM Agreement*. In New Zealand's view, a measure that no longer constitutes an export subsidy under item (j) of the Illustrative List of Export Subsidies may still constitute an export subsidy under Articles 1.1 and 3.1(a) of the *SCM Agreement*. Therefore, New Zealand requests the Appellate Body to complete the analysis and find that the United States' export credit guarantee programs are export subsidies under Articles 1.1 and 3.1(a) of the *SCM Agreement*.

9. Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu

248. Pursuant to Rule 24 of the *Working Procedures*, the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu chose not to submit a third participant's submission. In its statement at the oral hearing, the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu agreed with the United States that using planting flexibility limitations in association with production flexibility contract payments and direct payments does not render these measures inconsistent with paragraph 6(b) of Annex 2 to the *Agreement on Agriculture*.

III. Issues Raised in this Appeal

249. The following issues are raised in this appeal:

(a) as regards procedural matters:

(i) in relation to production flexibility contract payments and market loss assistance payments:

- whether the Panel erred in finding, in paragraphs 7.118, 7.122, 7.128, and 7.194(ii) of the Panel Report, that Articles 4.2 and 6.2 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU") do not exclude expired measures from the potential scope of consultations or a request for establishment of a panel and, therefore, that production flexibility contract payments and market loss assistance payments fell within the Panel's terms of reference; and

- whether the Panel, contrary to Article 12.7 of the DSU, failed to set out the findings of fact, the applicability of relevant provisions, or the basic rationale behind this finding; and
- (ii) in relation to export credit guarantee programs:
 - whether the Panel erred in finding, in paragraph 7.69 of the Panel Report, that the United States' export credit guarantees relating to eligible United States agricultural commodities other than upland cotton were within its terms of reference; and
 - whether the Panel erred in finding, in paragraph 7.103 of the Panel Report, that Brazil provided a statement of available evidence with respect to export credit guarantees relating to eligible United States agricultural commodities other than upland cotton, as required by Article 4.2 of the *Agreement on Subsidies and Countervailing Measures* (the "*SCM Agreement*");

(b) as regards the application of Article 13 of the *Agreement on Agriculture* to this dispute:

- (i) in relation to Article 13(a)(ii):
 - whether the Panel erred in finding, in paragraphs 7.388, 7.413, 7.414, and 8.1(b) of the Panel Report, that production flexibility contract payments and direct payments are not green box measures that fully conform to paragraph 6(b) of Annex 2 of the *Agreement on Agriculture* based on its finding, in paragraph 7.385 of the Panel Report, that the amount of production flexibility payments and direct payments is related to the type of production undertaken by a producer after the base period; and, therefore, that these measures are not exempt from actions based on Article XVI of the *General Agreement on Tariffs and Trade 1994* (the "*GATT 1994*") and Part III of the *SCM Agreement* by virtue of Article 13(a)(ii) of the *Agreement on Agriculture*; and
- whether the updating of base acres for direct payments under the FSRI Act of 2002 means that direct payments are not green box

measures that fully conform to paragraph 6(a) of Annex 2 of the *Agreement on Agriculture* and, therefore, that these measures are not exempt from actions based on Article XVI of the *GATT 1994* and Part III of the *SCM Agreement* by virtue of Article 13(a)(ii) of the *Agreement on Agriculture*, because they are not determined by clearly-defined criteria in a *defined and fixed base period*¹⁷⁹; and

- (ii) in relation to Article 13(b)(ii), whether the Panel erred in finding, in paragraphs 7.608 and 8.1(c) of the Panel Report, that user marketing (Step 2) payments ("Step 2 payments") to domestic users, marketing loan program payments, production flexibility contract payments, market loss assistance payments, direct payments, counter-cyclical payments, crop insurance payments, and cottonseed payments (the "challenged domestic support measures") granted, in the years 1999, 2000, 2001, and 2002, support to a specific commodity, namely, upland cotton, in excess of that decided during the 1992 marketing year and, therefore, that these measures are not exempt from actions based on Articles 5 and 6 of the *SCM Agreement* and Article XVI:1 of the *GATT 1994* by virtue of Article 13(b)(ii) of *Agreement on Agriculture*, based on its findings:

- in paragraph 7.494 of the Panel Report, that the phrase "grant support to a specific commodity" in Article 13(b)(ii) refers to all non-green box support measures that clearly or explicitly define a commodity as one to which they bestow or confer support and does not mean "product-specific domestic support";
- in paragraphs 7.518 and 7.520 of the Panel Report, that the challenged domestic support measures are non-green box support measures that clearly or explicitly define a commodity, namely, upland cotton, as one to which they bestow or confer support; and
- in paragraphs 7.561 and 7.562 of the Panel Report, that an appropriate comparison between the level at which measures "grant support" in the implementation period and that "decided during

¹⁷⁹Brazil's appeal is conditional on the Appellate Body reversing the finding of the Panel that "direct payments, production flexibility contract payments, and the legislative and regulatory provisions that establish and maintain the direct payment program" do not fully conform to paragraph 6(b) of Annex 2 and, consequently, do not satisfy the condition in paragraph (a) of Article 13 of the *Agreement on Agriculture*.

the 1992 marketing year" may be achieved, with respect to marketing loan program payments and deficiency payments, through the use of a methodology other than the price gap methodology described in paragraph 10 of Annex 3 of the *Agreement on Agriculture*;

- (c) as regards serious prejudice:
 - (i) in relation to Article 6.3(c) of the *SCM Agreement*:
 - whether the Panel erred in finding, in paragraphs 7.1416 and 8.1(g)(i) of the Panel Report, that the effect of the marketing loan program payments, Step 2 payments, market loss assistance payments, and counter-cyclical payments (the "price-contingent subsidies") is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*, based on its findings:
 - (A) regarding the "market" and "price" in assessing whether "the effect of the subsidy is ... significant price suppression ... in the same market" within the meaning of Article 6.3(c) of the *SCM Agreement*:
 - in paragraphs 7.1238-7.1240 of the Panel Report, that the "same market" may be a "world market";
 - in paragraph 7.1247 of the Panel Report, that a "world market" for upland cotton exists; and
 - in paragraph 7.1274 of the Panel Report, that "the A-Index can be taken to reflect a world price in the world market for upland cotton"; and
 - (B) regarding the "effect" of the price-contingent subsidies under Article 6.3(c) of the *SCM Agreement*:
 - in paragraphs 7.1312 and 7.1333 of the Panel Report, that "significant price suppression" occurred within the meaning of Article 6.3(c);

- in paragraphs 7.1355 and 7.1363 of the Panel Report, that "a causal link exists" between the price-contingent subsidies and the significant price suppression found by the Panel under Article 6.3(c) and that this link is not attenuated by other factors raised by the United States;
- in paragraphs 7.1173, 7.1186, and 7.1226 of the Panel Report, that it was not required to quantify precisely the benefit conferred on upland cotton by the price-contingent subsidies and, consequently, not identifying the precise amount of counter-cyclical payments and market loss assistance payments that benefited upland cotton; and
- in paragraph 7.1416 of the Panel Report, that the effect of the price-contingent subsidies for marketing years 1999 to 2002 "is significant price suppression ... in the period MY 1999-2002"; and
- whether the Panel, contrary to Article 12.7 of the DSU, failed to set out the findings of fact, the applicability of relevant provisions, or the basic rationale behind its finding, in paragraphs 7.1416 and 8.1(g)(i) of the Panel Report, that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*; and
- (ii) in relation to Article 6.3(d) of the *SCM Agreement*:
 - whether the Panel erred in finding, in paragraph 7.1464 of the Panel Report, that the words "world market share" in Article 6.3(d) of the *SCM Agreement* refer to the "share of the world market supplied by the subsidizing Member of the product concerned"; and
 - whether the Appellate Body should complete the analysis of whether the effect of the price-contingent subsidies is an increase in the

United States' world market share of exports in upland cotton within the meaning of Article 6.3(d) of the *SCM Agreement*¹⁸⁰,

- (d) as regards user marketing (Step 2) payments, whether the Panel erred:
 - (i) in finding, in paragraphs 7.1088, 7.1097-7.1098, and 8.1(f) of the Panel Report, that Step 2 payments to *domestic users* of United States upland cotton, under Section 1207(a) of the FSRI Act of 2002, are subsidies contingent upon the use of domestic over imported goods that are inconsistent with Articles 3.1(b) and 3.2 of the *SCM Agreement*; and
 - (ii) in finding, in paragraphs 7.748-7.749, 7.760-7.761, and 8.1(e) of the Panel Report, that Step 2 payments to *exporters* of United States upland cotton, pursuant to Section 1207(a) of the FSRI Act of 2002, are subsidies contingent upon export performance within the meaning of Article 9.1(a) of the *Agreement on Agriculture* that are inconsistent with Articles 3.3 and 8 of that Agreement and Articles 3.1(a) and 3.2 of the *SCM Agreement*;
- (e) as regards export credit guarantee programs, whether the Panel erred:
 - (i) in finding, in paragraphs 7.901, 7.911, and 7.932 of the Panel Report, that Article 10.2 of the *Agreement on Agriculture* does not exempt export credit guarantees from the export subsidy disciplines in Article 10.1 of that Agreement;
 - (ii) in the manner that it applied the burden of proof in finding that the United States' export credit guarantee programs are prohibited export subsidies under Articles 3.1(a) and 3.2 of the *SCM Agreement*;
 - (iii) by failing to make the necessary findings of fact in assessing whether the United States' export credit guarantee programs are provided at premium rates that are inadequate to cover long-term operating costs and losses within the meaning of item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement*;

¹⁸⁰Brazil's request for the Appellate Body to complete the analysis of this issue is conditional on the Appellate Body reversing the finding of the Panel that the effect of the price-contingent subsidies was significant price suppression in terms of Article 6.3(c) of the *SCM Agreement*.

- (iv) in finding, in paragraphs 7.947 and 7.948 of the Panel Report, that the United States' export credit guarantee programs are prohibited export subsidies under Article 3.1(a) of the *SCM Agreement* and are consequently inconsistent with Article 3.2 of that Agreement; and
- (v) by exercising judicial economy, as noted in paragraph 6.31 of the Panel Report, in respect of Brazil's claim that the United States' export credit guarantee programs are export subsidies within the meaning of Articles 1.1 and 3.1(a) of the *SCM Agreement*, having already found that these measures were export subsidies covered by item (j) of the Illustrative List of Export Subsidies and, therefore, were inconsistent with Articles 3.1(a) and 3.2 of the *SCM Agreement*;
- (f) as regards circumvention of export subsidy commitments, whether the Panel erred:
 - (i) in the application of Article 10.1 of the *Agreement on Agriculture* and by failing to meet the requirements of Article 11 of the DSU, in finding, in paragraph 7.881 of the Panel Report, that Brazil did not establish that the United States' export credit guarantees are "applied in a manner that results in ... circumvention" of the United States' export subsidy commitments with respect to pig meat and poultry meat in 2001¹⁸¹;
 - (ii) in paragraphs 7.882-7.883 and 7.896 of the Panel Report, in interpreting and applying the phrase "threatens to lead to ... circumvention" in Article 10.1 of the *Agreement on Agriculture*; and
 - (iii) in paragraph 7.882 and footnote 1061 of the Panel Report, by confining its examination of threat of circumvention to scheduled products other than rice and unsupported unscheduled products;
 - (g) as regards the FSC Repeal and Extraterritorial Income Exclusion Act of 2000 (the "ETI Act of 2000"), whether the Panel erred in finding that Brazil did not establish a *prima facie* case that the ETI Act of 2000 and the subsidies granted

¹⁸¹At the oral hearing, Brazil indicated that it was not pursuing this claim in respect of vegetable oil.

thereunder are inconsistent with Articles 8 and 10.1 of the *Agreement on Agriculture* and Articles 3.1 and 3.2 of the *SCM Agreement*, in respect of upland cotton; and

(h) as regards Article XVI:3 of the GATT 1994:

- (i) whether the Panel erred in finding, in paragraph 7.1016 of the Panel Report, that Article XVI:3 of the GATT 1994 "applies only to export subsidies as that term is now defined in the *Agreement on Agriculture* and the *SCM Agreement*"; and
- (ii) whether the Appellate Body should complete the analysis of whether the price-contingent subsidies caused the United States to have "more than an equitable share of world export trade" in upland cotton, in violation of the second sentence of Article XVI:3 of the GATT 1994.¹⁸²

IV. Preliminary Issues

A. *Terms of Reference – Expired Measures*

1. Introduction

250. The United States appeals the Panel's finding that two subsidy measures, namely, production flexibility contract payments with the exception of those made in the 2002 marketing year and market loss assistance payments, can be the subject of consultations under the DSU and hence fell within the Panel's terms of reference, notwithstanding the fact that the legislative basis for these payments had expired at the time those terms of reference were set.¹⁸³

251. Production flexibility contract payments were a form of income support under the Federal Agriculture Improvement and Reform Act of 1996 (the "FAIR Act of 1996"); they were discontinued with the passage of the Farm Security and Rural Investment Act of 2002 (the "FSRI Act of 2002") in May 2002. The last production flexibility contract payments were scheduled to be made "not later

¹⁸²Brazil's request for the Appellate Body to complete the analysis of this issue is conditional on two events: (i) the Appellate Body reversing the finding of the Panel that the effect of the price-contingent subsidies was significant price suppression in terms of Article 6.3(c) of the *SCM Agreement*; and, (ii) the Appellate Body declining Brazil's request for a ruling that the United States' measures at issue resulted in an increase in the United States' world market share in upland cotton in terms of Article 6.3(d) of the *SCM Agreement*.

¹⁸³Notwithstanding paragraph 9 of the United States' Notice of Appeal, the United States explained during the oral hearing that it does not appeal the Panel's findings, in paragraph 7.132 of the Panel Report, that payments with respect to non-upland cotton base acres were within its terms of reference.

than" 30 September 2002¹⁸⁴, in connection with the 2002 crop. Market loss assistance payments were *ad hoc* annual payments made through legislation enacted by the United States Congress between 1998 and 2001. Each such payment was made through a separate piece of legislation, the last of which was enacted on 13 August 2001, for the marketing year 2001 (1 August 2001 – 31 July 2002) crop.¹⁸⁵

252. Before the Panel, the United States argued that production flexibility contract payments and market loss assistance payments could not be within the terms of reference because they had expired prior to Brazil's request for consultations. The United States argued that Article 4.2 of the DSU provides that consultations may cover only "measures affecting" the operation of a covered agreement, and that expired measures are not "measures affecting" the operation of a covered agreement.¹⁸⁶ Brazil asked the Panel to reject the United States' request, submitting that a panel is required to examine the effects flowing from expired measures in order to conduct an objective assessment of a serious prejudice claim.¹⁸⁷

253. The Panel noted that Brazil had not pursued claims with respect to the legislation underlying the programs; instead, Brazil's claim was limited to the WTO-consistency of the payments made under those programs.¹⁸⁸ In its reasoning, the Panel said it did:

... not consider that Article 4.2 [of the DSU] supports an interpretation that a request for consultations cannot concern measures that have expired, or payments made under programmes that are no longer in effect, where the Member requesting consultations represents that benefits accruing to it directly or indirectly under the covered agreements are being impaired by those measures.¹⁸⁹

254. It added that "the Panel's terms of reference refer to Brazil's request for establishment of a panel, not its request for consultations."¹⁹⁰ The Panel also recalled that "Article 6.2 of the *DSU* provides that a request for establishment of a panel should identify the 'specific measures at issue' and

¹⁸⁴See Panel Report, paras. 7.107 and 7.212-7.215. See also "Answers of the United States to the Panel's Questions Posed Following the First Session of the First Substantive Panel Meeting" (11 August 2003), Panel Report, p. I-84, para. 35.

¹⁸⁵For further discussion of the nature of production flexibility contract payments and market loss assistance payments, insofar as they are relevant to this issue, see Panel Report, paras. 7.107 and 7.212-7.217.

¹⁸⁶See Panel Report, paras. 7.104 and 7.113.

¹⁸⁷See Panel Report, para. 7.105.

¹⁸⁸*Ibid.*, para. 7.108.

¹⁸⁹*Ibid.*, para. 7.118.

¹⁹⁰*Ibid.*, para. 7.121.

does not address the issue of the status of the measures at all.¹⁹¹ On this basis, the Panel indicated that it did not believe that:

Article 4.2, and hence Article 6.2, of the *DSU* excludes expired measures from the potential scope of a request for establishment of a panel.¹⁹²

255. In the light of this finding (and having rejected a further claim by the United States that market loss assistance payments were not identified with adequate specificity in Brazil's request for establishment of a panel¹⁹³), the Panel concluded:

Therefore, in light of our conclusion at paragraph 7.122, ... the Panel rules that PFC and MLA payments, as addressed in document WT/DS267/7, fall within its terms of reference.¹⁹⁴

2. Appeal by the United States

256. The United States claims that the Panel erred in reaching this conclusion and requests the Appellate Body to reverse the Panel's finding that Articles 4.2 and 6.2 of the DSU do not exclude expired measures from the potential scope of consultations or a request for establishment of a panel.¹⁹⁵ It also asserts that the Panel failed to set out the findings of fact, the applicability of relevant provisions, and the basic rationale behind this finding, as required by Article 12.7 of the DSU.¹⁹⁶ The United States submits that it was undisputed that the legislation authorizing both of these types of payments had expired before Brazil submitted its request for consultations.¹⁹⁷

257. The United States observes that Article 4.2 of the DSU provides that consultations may cover "any representations made by another Member *concerning measures affecting the operation of any covered agreement* taken within the territory of the former".¹⁹⁸ The United States focuses on the present tense of the verb "affecting" in this Article and contends that expired measures cannot be

¹⁹¹Panel Report, para. 7.121.

¹⁹²*Ibid.*, para. 7.122.

¹⁹³*Ibid.*, para. 7.127. This finding has not been appealed.

¹⁹⁴*Ibid.*, para. 7.128. This final finding was reiterated in paragraph 7.194(ii) of the Panel Report.

¹⁹⁵United States' Notice of Appeal, *supra*, footnote 17, para. 14; United States' appellant's submission, para. 515.

¹⁹⁶United States' appellant's submission, para. 150.

¹⁹⁷*Ibid.*, para. 500.

¹⁹⁸United States' appellant's submission, para. 501 (quoting Article 4.2 of the DSU). (emphasis added by the United States)

measures "affecting", in the present, the operation of a covered agreement.¹⁹⁹ Thus, according to the United States, production flexibility contract and market loss assistance payments cannot be said to be currently "affecting" the operation of any covered agreement. Consequently, they cannot be measures falling within the scope of "specific measures at issue" in terms of Article 6.2 of the DSU.²⁰⁰

258. Brazil responds that neither Article 4.2 nor Article 6.2 of the DSU precludes a panel from analyzing payments made in the past in the context of serious prejudice claims. Brazil focuses on the context provided by Article 3.3 of the DSU, which states that a purpose of dispute settlement is the "prompt settlement of situations in which a Member considers that any benefits accruing to it ... are being impaired by measures taken by another Member". For Brazil, as long as the impairment is *current*, the status in domestic law of the measure causing that impairment is irrelevant. Brazil notes that the present dispute involves allegations of "adverse effects" and "serious prejudice" under the provisions of the *SCM Agreement* and the GATT 1994. A breach of the relevant provisions of these Agreements does not occur when an actionable subsidy is granted, but rather when the adverse effects arise. Brazil finds support for its position in the view of the panel in *Indonesia – Autos*, which found that past, present, and future subsidies can be the subject of dispute settlement, as the effect of such measures may be serious prejudice to the interests of a Member.²⁰¹

3. Scope of Consultations under Article 4.2 of the DSU

259. Article 4.2 of the DSU governs what measures may be the subject of consultations and provides as follows:

Each Member undertakes to accord sympathetic consideration to and afford adequate opportunity for consultation regarding any representations made by another Member concerning measures affecting the operation of any covered agreement taken within the territory of the former. (footnote omitted)

260. It is clear from Article 4.2 that, although a requested Member is under an obligation to engage in "consultation" on "any" representations made by another Member, such representations must pertain to "measures affecting the operation of any covered agreement". The United States argues that Article 4.2 of the DSU limits the obligation of the requested Member to representations concerning measures that are actually "*affecting*" the operation of any covered agreement. The United States stresses the temporal significance of the present tense of the word "affecting" and asserts that

¹⁹⁹*Ibid.*, para. 501.

²⁰⁰United States' appellant's submission, paras. 502 and 512.

²⁰¹Brazil's appellee's submission, para. 256 (referring to Panel Report, *Indonesia – Autos*, para. 14.206).

"[m]easures that have expired before a request for consultations *cannot* be measures 'affecting the operation of any covered agreement' at the time the request is made".²⁰²

261. We agree with the Panel that the word "affecting" refers primarily to "the way in which [measures] relate to a covered agreement".²⁰³ As the Appellate Body stated in *EC – Bananas III*, "[t]he ordinary meaning of the word 'affecting' implies a measure that has 'an effect on'" something else.²⁰⁴ At the same time, we also concur with the United States that the ordinary meaning of the word "affecting" suggests a temporal connotation. As the United States submits, the present tense of the phrase "affecting the operation of any covered agreement" denotes that the effects of such measures must relate to the present impact of those measures on the operation of a covered agreement. It is not sufficient that a Member alleges that challenged measures affected the operation of a covered agreement in the past; the representations of the Member requesting consultations must indicate that the effects are occurring in the present.²⁰⁵

262. Whether or not a measure is still in force is not dispositive of whether that measure is currently affecting the operation of any covered agreement. Therefore, we disagree with the United States' argument that measures whose legislative basis has expired are incapable of affecting the operation of a covered agreement in the present and that, accordingly, expired measures *cannot* be the subject of consultations under the DSU.²⁰⁶ In our view, the question of whether measures whose legislative basis has expired affect the operation of a covered agreement currently is an issue that must be resolved on the facts of each case. The outcome of such an analysis cannot be prejudged by excluding it from consultations and dispute settlement proceedings altogether.

263. We consider that requesting Members should enjoy a degree of discretion to identify, in their request for consultations under Article 4.2, matters relating to the covered agreements for discussion in consultations. As the Appellate Body observed in *Mexico – Corn Syrup (Article 21.5 – US)*, consultations present an opportunity for clarifying factual and legal issues, and for narrowing the scope of a dispute, and for resolving differences between WTO Members.²⁰⁷ We do not think it would advance the purpose of consultations if Article 4.2 were interpreted as excluding *a priori* measures whose legislative basis may have expired, but whose effects are alleged to be impairing the benefits accruing to the requesting Member under a covered agreement. Nor, indeed, do we find

²⁰²United States' appellant's submission, para. 501. (emphasis added)

²⁰³Panel Report, para. 7.115.

²⁰⁴Appellate Body Report, *EC – Bananas III*, para. 220.

²⁰⁵This does not exclude the possibility that the effects of a measure may occur in future.

²⁰⁶United States appellant's submission, para. 501.

²⁰⁷Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 54.

textual support in the provision itself for doing so. Thus, we do not read Article 4.2 of the DSU as precluding a Member from making representations on measures whose legislative basis has expired, where that Member has reason to believe that such measures are still "affecting" the operation of a covered agreement.

264. We find contextual support for this interpretation in Article 3.3 of the DSU²⁰⁸, which underscores the importance of the "prompt settlement" of certain situations that, in the absence of settlement, could undermine the effective functioning of the WTO and the maintenance of a proper balance between the rights and obligations of Members. We note, first, that Article 3.3 focuses not upon "existing" measures, or measures that are "currently in force" but, rather, upon "measures taken" by a Member, which includes measures taken in the past.²⁰⁹ We also observe that Article 3.3 envisages that disputes arise when a Member "considers" that benefits accruing to it are being impaired by measures taken by another Member. By using the word "considers", Article 3.3 focuses on the perception or understanding of an aggrieved Member. This does not exclude the possibility that a Member requesting consultations may have reason to believe that a measure is still impairing benefits even though its legislative basis has expired.²¹⁰

265. We recall that the Panel observed that:

Brazil's request for consultations alleges that the use of the measures specified in the request "causes adverse effects, i.e. serious prejudice" to its interests. We note the present tense of this allegation. The request concerns the way in which measures were affecting the operation of a covered agreement at the time of consultations, and it states that Brazil had reason to believe that these subsidies were resulting in serious prejudice at that time.²¹¹

²⁰⁸Article 3.3 of the DSU provides:

The prompt settlement of situations in which a Member considers that any benefits accruing to it directly or indirectly under the covered agreements are being impaired by measures taken by another Member is essential to the effective functioning of the WTO and the maintenance of a proper balance between the rights and obligations of Members.

²⁰⁹Indeed, as the Panel noted, in the sense that "PFC and MLA payments had already been made at the date of the establishment of the Panel", "they had not expired, but had simply occurred in the past". (Panel Report, para. 7.110)

²¹⁰Whether the Member's belief proves to be correct is a substantive matter to be addressed in the consultations, or—if consultations fail—before a panel. We note that Brazil's request for consultations in regard to this matter was based not only on Article 4 of the DSU, but also on Article 7.1 of the *SCM Agreement* (as well as Article XXII of the GATT 1994). (See Request for Consultations by Brazil, WT/DS267/1, 3 October 2002, p. 1.) Article 7.1 authorizes a Member to request consultations whenever it "has reason to believe" that any subsidy referred to in Article 1 "results in" certain effects listed in that provision. Article 7.1 thus recognizes that questions regarding the results of subsidization are potentially contentious matters.

²¹¹Panel Report, para. 7.119.

266. For the Panel, these aspects of the request for consultations were sufficient for Brazil to meet the requirements of Article 4.2 of the DSU. We see no error in the Panel's approach to this question. Whether or not a subsidy program is still in force at the time consultations were requested does not answer the question whether any payments previously made under that program are currently affecting the operation of a covered agreement in the sense of Article 4.2. Brazil, in these proceedings, represented in its request for consultations that payments under the production flexibility contract and market loss assistance programs continued to affect its rights under the *SCM Agreement*. In our view, this was sufficient to meet the requirements of Article 4.2 of the DSU.

4. Measure at Issue under Article 6.2 of the DSU

267. In addition to its arguments under Article 4.2 of the DSU, the United States contends that an expired measure cannot be a measure that is "at issue" in terms of Article 6.2 of the DSU. The United States also argues that a finding to the contrary would be difficult to reconcile with the terms of Articles 3.7 and 19.1 of the DSU, which contemplate the "withdrawal" of a measure found to be inconsistent with the covered agreements, or a recommendation that a measure found to be inconsistent with a covered agreement be brought into conformity. The United States argues that the remedies described in Articles 3.7 and 19.1 are essentially prospective in nature.

268. We understand these arguments by the United States to be largely dependent upon its arguments regarding Article 4.2 of the DSU: if, as the United States contends, a measure may not be the subject of consultations then, *ipso facto*, it may not be a measure "at issue" in the sense of Article 6.2. Having rejected the United States' arguments regarding Article 4.2, we do not find the United States' additional arguments under Article 6.2 compelling.

269. The only temporal connotation contained in the ordinary meaning of the expression "at issue", as used in Article 6.2 of the DSU, is expressed by its present tense: measures must be "at issue"—or, putting it another way, "in dispute"—at the time the request is made. Certainly, nothing inherent in the term "at issue" sheds light on whether measures at issue must be currently in force, or whether they may be measures whose legislative basis has expired.

270. The relevant context for Article 6.2 in this regard includes Articles 3.3 and 4.2 of the DSU. As we have concluded above, those provisions do not preclude a Member from making representations with respect to measures whose legislative basis has expired, if that Member considers, with reason, that benefits accruing to it under the covered agreements are still being impaired by those measures. If the effect of such measures remains in dispute following consultations, the complaining party may, according to Article 4.7 of the DSU, request the

establishment of a panel, and the text of Article 6.2 does not suggest that such measures could not be the subject of a panel request as "specific measures at issue".

271. The United States purports to find support for its position in the ruling of the Appellate Body in *US – Certain EC Products*, where the Appellate Body reversed the panel's decision to make a recommendation under Article 19.1 of the DSU that the United States bring the measure at issue in that case (the "3 March Measure") into conformity with the covered agreements, on the grounds that the panel had already found that the measure had expired. However, that case involved a situation different from the present one. There, the 3 March Measure had been the subject of consultations, but had expired. The expiry of the 3 March Measure did not prevent it being a "measure at issue" for purposes of Article 6.2 of the DSU. Indeed, neither the panel nor the Appellate Body found that the 3 March Measure was outside the panel's terms of reference, and both the panel and Appellate Body addressed that measure in their rulings.²¹²

272. The question whether an expired measure is susceptible to a recommendation under Article 19.1 of the DSU is a different matter. The Appellate Body in *US – Certain EC Products* confirmed that the 3 March Measure had ceased to exist. It noted that there was an obvious inconsistency between the finding of the panel that "the 3 March Measure is no longer in existence" and the panel's subsequent recommendation that the Dispute Settlement Body (the "DSB") request the United States to bring the 3 March Measure into conformity with its WTO obligations.²¹³ Thus, the fact that a measure has expired may affect what recommendation a panel may make. It is not, however, dispositive of the preliminary question of whether a panel can address claims in respect of that measure.²¹⁴

²¹²This contrasts with the treatment of the other measure raised in that proceeding (the "19 April action"). It was in force, but had not been the subject of consultations. The panel and Appellate Body both ruled that the absence of consultations on the 19 April action required its exclusion from the terms of reference. (Appellate Body Report, *US – Certain EC Products*, para. 82; Panel Report, *US – Certain EC Products*, paras. 6.89 and 6.128)

²¹³Appellate Body Report, *US – Certain EC Products*, paras. 81-82.

²¹⁴This conclusion is consistent with the approach taken by GATT and WTO panels to questions relating to the expiry of measures after the initiation of dispute settlement proceedings, but before those proceedings have been completed. See, for example, GATT Panel Report, *EEC – Apples I (Chile)*, paras. 2.4 and 4.1 ff; Panel Report, *India – Autos*, para. 7.29. GATT and WTO panels have frequently made findings with respect to measures withdrawn after the establishment of the panel. See, for example, GATT Panel Report, *EEC – Animal Feed Proteins*, para. 2.4; GATT Panel Report, *US – Canadian Tuna*, para. 4.3; Panel Report, *US – Wool Shirts and Blouses*, para. 6.2; and Panel Report, *Indonesia – Autos*, para. 14.9. Even in cases where a panel has chosen not to rule on measures that had been terminated during the course of proceedings, panels have recognized that "[o]n several occasions, panels have considered measures that were no longer in force". (Panel Report, *Argentina – Textiles and Apparel*, para. 6.12. (footnote omitted)) In none of these cases has a panel or the Appellate Body premised its decision on the view that, *a priori*, an expired measure could not be within a panel's terms of reference.

273. It is important to recognize the particular characteristics of *subsidies* and the nature of Brazil's claims against the production flexibility contract and market loss assistance subsidy payments. Article 7.8 of the *SCM Agreement* provides that, where it has been determined that "any subsidy has *resulted* in adverse effects to the interests of another Member", the subsidizing Member must "take appropriate steps to *remove the adverse effects* or ... withdraw the subsidy". (emphasis added) The use of the word "resulted" suggests that there could be a time-lag between the payment of a subsidy and any consequential adverse effects.²¹⁵ If expired measures underlying past payments could not be challenged in WTO dispute settlement proceedings, it would be difficult to seek a remedy for such adverse effects. Further—in contrast to Articles 3.7 and 19.1 of the DSU—the remedies under Article 7.8 of the *SCM Agreement* for adverse effects of a subsidy are (i) the withdrawal of the subsidy or (ii) the removal of adverse effects. Removal of adverse effects through actions other than the withdrawal of a subsidy could not occur if the expiration of a measure would automatically exclude it from a panel's terms of reference.

274. For these reasons, we find the United States' reliance upon the prospective character of the remedies described in Articles 3.7 and 19.1 of the DSU unconvincing. We therefore *reject* the United States' argument that production flexibility contract payments and market loss assistance payments were outside the Panel's terms of reference by virtue of Article 6.2 of the DSU.

5. Article 12.7 of the DSU

275. The United States also alleges that, contrary to Article 12.7 of the DSU, the Panel failed to set out the findings of fact, the applicability of relevant provisions, and the basic rationale behind its finding that Articles 4.2 and 6.2 of the DSU do not exclude expired measures from the potential scope of a request for the establishment of a panel.

276. The Appellate Body stated in *Mexico – Corn Syrup (Article 21.5 – US)*:

²¹⁵We observe, in this regard, that the United States concedes that at least *some* subsidies can have effects for years after the date on which they are paid. Thus, the United States distinguishes between "non-recurring" subsidies and "recurring" subsidies. Although the United States believes that the effects of recurring subsidies are limited to the year for which they are paid, the United States *accepts* that the effects of non-recurring subsidies may spread out well into the future. (United States' appellant's submission, para. 508)

Article 12.7 establishes a minimum standard for the reasoning that panels must provide in support of their findings and recommendations. Panels must set forth explanations and reasons sufficient to disclose the essential, or fundamental, justification for those findings and recommendations.²¹⁶

The Appellate Body clarified:

[w]hether a panel has articulated adequately the "basic rationale" for its findings and recommendations must be determined on a case-by-case basis, taking into account the facts of the case, the specific legal provisions at issue, and the particular findings and recommendations made by a panel. Panels must identify the relevant facts and the applicable legal norms. In applying those legal norms to the relevant facts, the reasoning of the panel must reveal how and why the law applies to the facts. In this way, panels will, in their reports, disclose the essential or fundamental justification for their findings and recommendations.²¹⁷

The Appellate Body also explained that this "does not, however, necessarily imply that Article 12.7 requires panels to expound at length on the reasons for their findings and recommendations."²¹⁸

277. We note that compliance with Article 12.7 of the DSU is to be determined on a case-by-case basis. With regard to the current proceedings, as discussed above, we see no error in the Panel's conclusion regarding its ability to make findings with respect to subsidies whose legislative basis had expired at the time of panel establishment. Although the Panel's reasoning with respect to this issue may be brief, the Panel set out the necessary findings of fact, the applicability of relevant provisions, and the basic rationale behind its findings. The Panel noted that the parties agreed on the key factual element that was relevant to this part of its analysis, namely, that the legislation under which production flexibility contract and market loss assistance payments were made had expired, and went

²¹⁶Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 106. It also noted that:

... the duty of panels under Article 12.7 of the DSU to provide a "basic rationale" reflects and conforms with the principles of fundamental fairness and due process that underlie and inform the provisions of the DSU. In particular, in cases where a Member has been found to have acted inconsistently with its obligations under the covered agreements, that Member is entitled to know the reasons for such finding as a matter of due process. In addition, the requirement to set out a "basic rationale" in the panel report assists such Member to understand the nature of its obligations and to make informed decisions about: (i) what must be done in order to implement the eventual rulings and recommendations made by the DSB; and (ii) whether and what to appeal.

(*Ibid.*, para. 107) (footnote omitted)

²¹⁷*Ibid.*, para. 108.

²¹⁸*Ibid.*, para. 109.

on to discuss relevant factual aspects.²¹⁹ The Panel cited and discussed Article 4.2, in particular the meaning and significance of the term "affecting" in that provision.²²⁰ As we have done, the Panel interpreted Article 4.2 in the light of the context provided by Article 3.3 of the DSU.²²¹ It addressed Article 6.2 of the DSU²²², and also situated the question of "expired measures" in the context of the actionable subsidies claims made by Brazil in this case.²²³ Given these inquiries and considerations by the Panel, we see no reason to find that the Panel failed to meet the requirements of Article 12.7 of the DSU in relation to whether the expired production flexibility contract and market loss assistance payments fell within its terms of reference.

B. *Terms of Reference – Export Credit Guarantees*

1. Introduction

278. We turn now to the United States' claim that the Panel erred in finding that its terms of reference were not limited to export credit guarantees to upland cotton, but also included export credit guarantees to other eligible United States agricultural commodities.²²⁴

279. The United States requested the Panel to "rule that export credit guarantee measures relating to eligible United States agricultural commodities (other than upland cotton) are not within its terms of reference because this 'measure' was not the subject of Brazil's request for consultations".²²⁵ Brazil responded that "both its request for consultations and the accompanying statement of available evidence, as well as the questions it posed to the United States during consultations, revealed that they covered export credit guarantee measures relating to *all* eligible United States agricultural commodities".²²⁶

²¹⁹Panel Report, para. 7.108.

²²⁰*Ibid.*, paras. 7.112-7.115.

²²¹*Ibid.*, para. 7.116-7.117.

²²²*Ibid.*, para. 7.121.

²²³*Ibid.*, paras. 7.109-7.110.

²²⁴We note that, during the interim review, Brazil requested the Panel "to conclude that GSM 102, GSM 103 and SCGP also constitute prohibited export subsidies within the meaning of item (j) and Article 3.1(a) of the *SCM Agreement*, for all products not covered by the *Agreement on Agriculture*". The Panel rejected Brazil's request, explaining that its "terms of reference include[d] export credit guarantees to facilitate the export of United States upland cotton and other eligible *agricultural* commodities as addressed in document WT/DS267/7". (Panel Report, para. 6.37. (original emphasis))

²²⁵Panel Report, para. 7.55. (footnote omitted)

²²⁶*Ibid.*, para. 7.57. (footnote omitted; emphasis added)

280. The Panel found that "the *actual* consultations did include export credit guarantee measures relating to all eligible agricultural commodities".²²⁷ The Panel then examined the text of Brazil's request for consultations, "[a]ssuming *arguendo* that the scope of the written request for consultations is determinative, rather than the scope of the actual consultations".²²⁸ It found "that export credit guarantee measures relating to all eligible agricultural commodities were included in Brazil's request for consultations, based on its reading of the text of the request itself".²²⁹ Accordingly, the Panel made the following ruling in response to the United States' request:

[T]he Panel rules that export credit guarantees to facilitate the export of United States upland cotton, and other eligible agricultural commodities as addressed in document WT/DS267/7, are within its terms of reference.²³⁰

2. Arguments on Appeal

281. On appeal, the United States asserts that the Panel erred in finding that export credit guarantee measures relating to all eligible agricultural commodities were included in Brazil's request for consultations.²³¹ In addition, the United States takes issue with the Panel's finding that consultations were *actually* held on the export credit guarantee programs relating to agricultural commodities including, but not limited to, upland cotton.²³² The United States argues, in this regard, that the fact that Brazil posed written questions on the export credit guarantees relating to agricultural commodities including, but not limited to, upland cotton does not mean that consultations were *actually* held on all those products, especially considering that the United States objected to discussing them during the consultations on the basis that they were not included in the request for consultations.²³³

282. Brazil requests that we reject the United States' appeal. It contends that its request for consultations identified three United States export credit programs, namely, the General Sales Manager 102 ("GSM 102") and General Sales Manager 103 ("GSM 103") programs and the Supplier

²²⁷Panel Report, para. 7.61. (original italics; underlining added)

²²⁸*Ibid.*, para. 7.62.

²²⁹*Ibid.*, para. 7.65. The Panel explained that the title of this dispute, "United States – Subsidies on Upland Cotton", "did not appear in the original communication sent from the Permanent Mission of Brazil to the Permanent Mission of the United States", but rather "was added by the [WTO] Secretariat when it circulated a copy of the request for consultations to Members". Consequently, the Panel did not consider the title to be "a legally relevant consideration here". (*Ibid.*, footnote 131 to para. 7.64)

²³⁰Panel Report, para. 7.69. (footnote omitted)

²³¹United States' appellant's submission, para. 474.

²³²*Ibid.*, para. 471.

²³³*Ibid.*, paras. 471-472.

Credit Guarantee Program (the "SCGP").²³⁴ By their own terms, each of these measures applies to all eligible products.²³⁵ Therefore, there was no need to specify the product scope of these measures.²³⁶ Brazil submits that, in any event, its request for consultations in fact identified the export credit guarantee programs in connection with all eligible commodities, without any limitation to upland cotton.²³⁷ Finally, Brazil asserts that, irrespective of the measures identified in Brazil's request for consultations, the Panel found, as a matter of fact, that "consultations were held" on the export credit guarantee programs in connection with all eligible commodities, as required by Article 6.2 of the DSU.²³⁸

3. Did the Panel's Terms of Reference Include Other Eligible Agricultural Commodities?

283. The United States claims on appeal that the Panel's terms of reference were limited to export credit guarantees to upland cotton, and did not include export credit guarantees to other eligible agricultural commodities. This claim is premised on the allegation that, in its request for the establishment of a panel, Brazil expanded the product scope in respect of which it challenges the United States' export credit guarantee programs to include other eligible agricultural products in addition to upland cotton. The United States submits that the request for consultations and the consultations themselves, however, were limited to export credit guarantees to upland cotton. Brazil contends that its request for consultations and the consultations held covered *all* agricultural products eligible for export credit guarantees.²³⁹

284. Before addressing the question of whether Brazil expanded, in its panel request, the scope of products in respect of which it challenged the United States' export credit guarantee programs, we note that the Appellate Body has explained previously that, "pursuant to Article 7 of the DSU, a

²³⁴These programs are described *infra*, paras. 586-589.

²³⁵See Panel Report, footnote 1056 to para. 7.875.

²³⁶Brazil's appellee's submission, para. 195.

²³⁷*Ibid.*, para. 202.

²³⁸Brazil's appellee's submission, paras. 208-209. Brazil reads the Appellate Body Report in *Brazil – Aircraft* as meaning that as long as "consultations were held" on a measure included in a request for establishment of a panel, that measure is properly within a panel's terms of reference, irrespective of whether the measure was included in the request for consultations. (*Ibid.*, para. 213 (referring to Appellate Body Report, *Brazil – Aircraft*, paras. 132-134)) Brazil adds that this is consistent with the purpose of consultations. (*Ibid.*, para. 214)

²³⁹In addition, Brazil submits that the Panel's terms of reference are determined by the panel request, and that its panel request referred to all agricultural products eligible for the United States' export credit guarantees.

panel's terms of reference are governed by the request for establishment of a panel".²⁴⁰ However, the Appellate Body has also explained that "as a general matter, consultations are a prerequisite to panel proceedings"²⁴¹ and has underscored the importance and benefits of consultations:

We agree ... on the importance of consultations. Through consultations, parties exchange information, assess the strengths and weaknesses of their respective cases, narrow the scope of the differences between them and, in many cases, reach a mutually agreed solution in accordance with the explicit preference expressed in Article 3.7 of the DSU. Moreover, even where no such agreed solution is reached, consultations provide the parties an opportunity to define and delimit the scope of the dispute between them. Clearly, consultations afford many benefits to complaining and responding parties, as well as to third parties and to the dispute settlement system as a whole.²⁴²

285. The requirements that apply to a request for consultations are set out in Article 4.4 of the DSU, which provides, in relevant part:

Any request for consultations shall be submitted in writing and shall give the reasons for the request, including identification of the measures at issue and an indication of the legal basis for the complaint.

The Appellate Body has stated that "Articles 4 and 6 of the DSU ... set forth a process by which a complaining party must request consultations, and consultations must be held, before a matter may be referred to the DSB for the establishment of a panel".²⁴³ At the same time, however, the Appellate Body has said that it does not believe that "Articles 4 and 6 of the DSU ... require a *precise and exact identity* between the specific measures that were the subject of consultations and the specific

²⁴⁰Appellate Body Report, *US – Carbon Steel*, para. 124. Article 7.1 of the DSU provides:

Panels shall have the following terms of reference unless the parties to the dispute agree otherwise within 20 days from the establishment of the panel:

To examine, in the light of the relevant provisions in (name of the covered agreement(s) cited by the parties to the dispute), the matter referred to the DSB by (name of party) in document ... and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in that/those agreement(s).

The United States does not dispute that Brazil's request for the establishment of a panel included export credit guarantees to eligible agricultural commodities including, but not limited to, upland cotton.

²⁴¹Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 58.

²⁴²*Ibid.*, para. 54.

²⁴³Appellate Body Report, *Brazil – Aircraft*, para. 131.

measures identified in the request for the establishment of a panel".²⁴⁴ We need not elaborate further on the relationship between a panel's terms of reference and the requirement that "consultations were held", because, as we explain below, we are satisfied that, in this case, the Panel had a reasonable basis to conclude that the request for consultations included export credit guarantees to eligible agricultural commodities including, but not limited to, upland cotton.

286. In reviewing the Panel's analysis, we are faced with the question whether the scope of the consultations is determined by the written request for consultations or by what actually happens in the consultations. The Panel looked first at what actually happened during the consultations. It observed that Brazil submitted in writing to the United States 21 questions regarding export credit guarantee programs, seeking information on, *inter alia*, the total volume and value of exports of United States agricultural goods guaranteed by these programs.²⁴⁵ According to the Panel, "[t]his shows that the actual consultations did include export credit guarantee measures relating to all eligible agricultural commodities".²⁴⁶ The Panel then examined the text of Brazil's request for consultations, "[a]ssuming *arguendo* that the scope of the written request for consultations is determinative, rather than the scope of the actual consultations".²⁴⁷

287. We believe that the Panel should have limited its analysis to the request for consultations because we are inclined to agree with the panel in *Korea – Alcoholic Beverages*, which stated that "[t]he only requirement under the DSU is that consultations were in fact held ... [w]hat takes place in those consultations is not the concern of a panel".²⁴⁸ Examining what took place in the consultations would seem contrary to Article 4.6 of the DSU, which provides that "[c]onsultations shall be confidential, and without prejudice to the rights of any Member in any further proceedings." Moreover, it would seem at odds with the requirements in Article 4.4 of the DSU that the request for

²⁴⁴Appellate Body Report, *Brazil – Aircraft*, para. 132. (original emphasis) The Appellate Body found, in that case, that certain measures that came into effect after consultations were held were nevertheless within the Panel's terms of reference, emphasizing that the measures did not change the essence of the challenged export subsidies. In *US – Certain EC Products*, the Appellate Body found that one of the measures challenged by the European Communities was not properly before the Panel. The Appellate Body explained that, although the panel request referred to the measure, it was not possible for it to conclude "on this basis *alone*" that the measure was within the Panel's terms of reference. It noted that the European Communities' request for consultations did not refer to the measure and that the European Communities acknowledged that the measure was not the subject of the consultations. In its ruling, the Appellate Body also emphasized that the particular measure was "separate" and "legally distinct" from another measure challenged by the European Communities. (Appellate Body Report, *US – Certain EC Products*, paras. 69-75) (original emphasis)

²⁴⁵The United States acknowledged that Brazil posed questions during the consultations that went beyond upland cotton. (Panel Report, para. 7.61) According to the Panel, the United States declined to respond to these questions during the consultations. (Panel Report, 7.67)

²⁴⁶Panel Report, para. 7.61. (original emphasis)

²⁴⁷*Ibid.*, para. 7.62.

²⁴⁸Panel Report, *Korea – Alcoholic Beverages*, para. 10.19.

consultations be made in writing and that it be notified to the DSB. In addition, there is no public record of what actually transpires during consultations and parties will often disagree about what, precisely, was discussed. Ultimately, however, it is not necessary for us to inquire into this part of the Panel's analysis because the Panel also found "that export credit guarantee measures relating to all eligible agricultural commodities were included in Brazil's request for consultations, based on its reading of the text of the request itself".²⁴⁹ We turn, therefore, to examine whether there is a sufficient basis for the Panel's conclusion in this regard.

288. Brazil's request for consultations states, in relevant part²⁵⁰:

The measures that are the subject of this request are prohibited and actionable subsidies provided to US producers, users and/or exporters of upland cotton', as well as legislation, regulations, statutory instruments and amendments thereto providing such subsidies (including export credits), grants, and any other assistance to the US producers, users and exporters of upland cotton ("US upland cotton industry"). The measures include the following:

...

- Export subsidies, exporter assistance, export credit guarantees, export and market access enhancement to facilitate the export of US upland cotton provided under the Agricultural Trade Act of 1978, as amended, and other measures such as the GSM-102, GSM-103, and SCGP programs ...

...

Regarding export credit guarantees, export and market access enhancement provided under the Agricultural Trade Act of 1978, as amended, and other measures such as the GSM-102, GSM-103, and SCGP programs, Brazil is of the view that these programs, as applied and as such, violate Articles 3.3, 8, 9.1, and 10.1 of the Agreement on Agriculture and are prohibited export subsidies under Article 3.1(a) and item (j) of the Illustrative List of Export Subsidies included as Annex I to the SCM Agreement. Subsidies provided under these programs are also actionable subsidies for the purpose of Brazil's claims under Article 6.3 of the SCM Agreement.

¹ Except with respect to export credit guarantee programs as explained below.

289. According to the Panel, footnote 1 to Brazil's request for consultations "should have indicated to the careful reader that the subject of the request for consultations, with respect to export credit

²⁴⁹Panel Report, para. 7.65.

²⁵⁰Request for Consultations by Brazil, *supra*, footnote 26, pp. 1-2 and 4.

guarantee measures only, was different from those provided to US producers, users and/or exporters of upland cotton".²⁵¹ The Panel also observed that the second paragraph after the footnote dealing with export credit guarantee programs referred to the programs as applied and as such, and it did not refer specifically to upland cotton. The Panel therefore concluded that "export credit guarantee measures relating to all eligible agricultural commodities were included in Brazil's request for consultations, based on its reading of the text of the request itself."²⁵²

290. The United States contends that the Panel ignored the first paragraph after the footnote and drew the wrong conclusion from the second paragraph. According to the United States, "it is simply not the case that a 'plain reading' of the [second] paragraph 'includes all eligible agricultural commodities'." Rather, it "shows that the [second] paragraph mentions *no* commodities at all".²⁵³ The United States also asserts that the Panel "overlooked the context that th[e] first paragraph provided for the second".²⁵⁴ The first paragraph, the United States points out, refers to exports subsidies, exporter assistance, and export credit guarantees to facilitate the export of *upland cotton* under a series of listed measures. A comparison of the first and second paragraphs shows that "the second did not describe measures, but, rather, described the *legal basis* for Brazil's complaint".²⁵⁵

The United States submits that the Panel should therefore have concluded that "the two paragraphs complemented one another" and, "[t]hat being the case, there is no reason to believe (and certainly the Panel gave none) that the product scope of the second paragraph was broader than the 'upland cotton' mentioned in the first paragraph".²⁵⁶ Finally, the United States argues that, "[e]ven assuming that the omission of the words 'upland cotton' from the second paragraph had some significance", the Panel gave no explanation as to "why the omission of those words should extend the product scope to 'all eligible agricultural commodities' rather than some other product scope".²⁵⁷

²⁵¹ Panel Report, para. 7.63.

²⁵² *Ibid.*, para. 7.65.

²⁵³ United States' appellant's submission, para. 476 (quoting Panel Report, para. 7.64). (original emphasis)

²⁵⁴ *Ibid.*, para. 477.

²⁵⁵ *Ibid.*, (original emphasis)

²⁵⁶ *Ibid.*, para. 477.

²⁵⁷ *Ibid.*, para. 479.

291. We have examined carefully Brazil's request for consultations and we find that it provides a sufficient basis for the Panel to have concluded that the request included export credit guarantees to eligible agricultural commodities including, but not limited to, upland cotton. Footnote 1 of the request for consultations, which states "Except with respect to export credit guarantee programs as provided below", alerts the reader that there is something different about Brazil's claims relating to the United States' export credit guarantee programs. Furthermore, the fact that the footnote follows immediately after the term "upland cotton" suggests that this difference relates to the product scope. It was not unreasonable, therefore, for the Panel to conclude that footnote 1 "should have indicated to the careful reader that the subject of consultations, with respect to export credit guarantee measures only, was different from those provided to US producer, users and/or exporters of upland cotton".²⁵⁸ In addition, in the second paragraph dealing with export credit guarantees after the footnote, Brazil refers to the programs "as such", which suggests a broad challenge, rather than one limited to a specific agricultural commodity. In our view, therefore, the footnote, together with the reference to the programs "as such" in the second paragraph, provide a reasonable basis for the Panel's conclusion "that export credit guarantee measures relating to all eligible agricultural commodities were included in Brazil's request for consultations, based on its reading of the text of the request itself."²⁵⁹

292. The United States also cites the lack of any reference to agricultural commodities other than upland cotton in the statement of available evidence that is annexed to Brazil's request for consultations as "further proof that the request did not extend beyond export credit guarantees for upland cotton".²⁶⁰ The United States raised this point as a separate claim on appeal and, therefore, we deal with this allegation in the next section of this Report. Below we uphold the Panel's finding that Brazil provided a statement of available evidence with respect to the United States' export credit guarantee programs as they relate to eligible agricultural products including, but not limited to, upland cotton²⁶¹ and, consequently, this argument does not support the United States' position on this issue.

²⁵⁸ Panel Report, para. 7.63.

²⁵⁹ *Ibid.*, para. 7.65. The facts of this case differ from those in *US – Certain EC Products*, on which the United States relies. In that case, the measure was not mentioned in the request for consultations because it was not even in existence at the time. (Appellate Body Report, *US – Certain EC Products*, para. 70)

²⁶⁰ United States' appellant's submission, para. 461.

²⁶¹ See *infra*, para. 309.

293. We emphasize that consultations are but the first step in the WTO dispute settlement process. They are intended to "provide the parties an opportunity to define and delimit the scope of the dispute between them".²⁶² We also note that Article 4.2 of the DSU calls on a WTO Member that receives a request for consultations to "accord sympathetic consideration to and afford adequate opportunity for consultation regarding any representations made by another Member". As long as the complaining party does not expand the scope of the dispute, we hesitate to impose too rigid a standard for the "precise and exact identity"²⁶³ between the scope of consultations and the request for the establishment of a panel, as this would substitute the request for consultations for the panel request. According to Article 7 of the DSU, it is the request for the establishment of a panel that governs its terms of reference, unless the parties agree otherwise.²⁶⁴

294. For these reasons, we uphold the Panel's ruling, in paragraph 7.69 of the Panel Report, that "export credit guarantees to facilitate the export of United States upland cotton, and other eligible agricultural commodities ... are within its terms of reference".

C. *Statement of Available Evidence – Export Credit Guarantees*

1. Introduction

295. We now examine the United States' claim that the Panel erred in finding that Brazil's statement of available evidence was not limited to the United States' export credit guarantees to upland cotton, but also included export credit guarantee measures relating to other eligible United States agricultural products, as required by Article 4.2 of the *SCM Agreement*.

296. The United States requested the Panel to rule that Brazil "could not advance claims under ... Article 4 ... of the *SCM Agreement* with respect to export credit guarantee measures on eligible agricultural commodities other than upland cotton because it did not include a statement of available

evidence with respect to such export credit guarantees in accordance with Article 4.2 ... of that Agreement".²⁶⁵

297. In examining the United States' request, the Panel noted that Brazil's statement of available evidence contained two paragraphs specifically referring to the United States' export credit guarantee programs²⁶⁶, and observed that the first paragraph is "textually limited to upland cotton", while the second paragraph "is not so limited".²⁶⁷ The Panel then rejected the United States' contention that the lack of a reference to upland cotton in the second paragraph could not expand the scope of the statement of available evidence.²⁶⁸ According to the Panel, when the second "paragraph is read in light of footnote 1 of the request for consultations, a careful reader should have been alerted to the fact that this paragraph referred to alleged subsidies arising from export credit guarantees under the challenged programmes, without any limitation to upland cotton or any other particular product or products".²⁶⁹ Furthermore, the Panel stated that Brazil's statement of evidence referred to a website of the United States Congressional Budget Office, which includes data pertaining to the spending and

²⁶⁵Panel Report, para. 7.70. The Panel explained that the United States initially argued that Brazil's statement of available evidence as regards export credit guarantees was limited to upland cotton and did not extend to other eligible agricultural commodities, demonstrating that Brazil's request for consultations was limited to export credit guarantees relating to upland cotton. The request for a specific ruling on the adequacy of the statement of available evidence was made by the United States in its submission of 30 September 2003. (Panel Report, para. 7.71)

In addition, the Panel noted that the United States had made allegations under both Articles 4.2 and 7.2 of the *SCM Agreement*. The Panel observed that Article 4.2 relates to prohibited subsidies and Article 7.2 relates to claims against actionable subsidies. Then, the Panel stated that it was not necessary for it to rule on the United States' claim relating to Article 7.2 because: (i) Brazil challenged only one United States export credit guarantee program—GSM 102—as an actionable subsidy that caused serious prejudice; (ii) this allegation was limited to upland cotton; and (iii) the Panel had exercised judicial economy with respect to the claim. Thus, the Panel limited its examination to "whether Brazil included a statement of available evidence with respect to export credit guarantees on other eligible agricultural products in accordance with the requirement pertaining to its *export* subsidy allegations in Article 4.2 of the *SCM Agreement*". (Panel Report, paras. 7.73-7.74, 7.76, and 7.78-7.79) (original emphasis)

In its Notice of Appeal, the United States asserted that, in the event that Brazil appealed the Panel's exercise of judicial economy with respect to Brazil's claims concerning the compatibility of the United States' export credit guarantee measures with Part III of the *SCM Agreement*, the United States would conditionally request the Appellate Body to find that Brazil also failed to provide a statement of available evidence as required by Article 7.2 of the *SCM Agreement* and, accordingly, Brazil's claims concerning these measures were not within the Panel's terms of reference. (Notice of Appeal, *supra*, footnote 17, para. 13) The United States did not pursue this claim further in its appellant's submission. In any event, the condition on which the United States' appeal was based was not met, as Brazil did not appeal the Panel's exercise of judicial economy concerning the compatibility of the United States' export credit guarantee measures with Part III of the *SCM Agreement*.

²⁶⁶Panel Report, para. 7.83.

²⁶⁷*Ibid.*, para. 7.84.

²⁶⁸*Ibid.*, para. 7.84.

²⁶⁹*Ibid.*, para. 7.85. (footnoted omitted) Footnote 1 of Brazil's request for consultations reads: "Except with respect to export credit guarantee programs as explained below". See *supra*, para. 288.

²⁶²Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 54.

²⁶³Appellate Body Report, *Brazil – Aircraft*, para. 132. (emphasis omitted)

²⁶⁴Appellate Body Report, *US – Carbon Steel*, para. 124.

offsetting receipts of the Commodity Credit Corporation (the "CCC"). Neither the reference to the website nor the data on the website "contain any indication of limitation of Brazil's allegations concerning the export credit guarantee programmes to any specific product, such as, for example, upland cotton".²⁷⁰

298. Therefore, the Panel found:

[A]ssuming *arguendo* that the United States' request was timely²⁷¹, the Panel rules that Brazil provided a statement of available evidence with respect to export credit guarantee measures relating to upland cotton and eligible United States agricultural products other than upland cotton, as required by Article 4.2 of the *SCM Agreement*.²⁷²

299. On appeal, the United States argues that the Panel's ruling is erroneous. The United States submits that Brazil's statement of evidence contains two paragraphs specifically referring to the United States' export credit guarantee programs.²⁷³ The first paragraph is textually limited to upland cotton, as the Panel correctly found. Although the second paragraph does not refer to upland cotton, it contains no suggestion that it expands on the programs described in the preceding paragraph.²⁷⁴ The United States further submits that, even if the second paragraph were construed to refer to programs that provide benefits to products other than upland cotton, it is "difficult to see" how that paragraph meets the requirements of Article 4.2 of the *SCM Agreement*, as it does not provide information about the "existence" or "nature" of the subsidies allegedly provided by the export credit guarantee programs to products in addition to upland cotton.²⁷⁵

300. Brazil submits that its statement of available evidence not only identifies the measures at issue—the United States' export credit guarantee programs—but also indicates the characteristics of those measures that had led Brazil to suspect that they constituted export subsidies, as required by the Appellate Body in *US – FSC*.²⁷⁶ Specifically, Brazil's statement describes the failure of the export credit guarantee programs to establish premium rates that cover long-term operating costs and losses,

²⁷⁰Panel Report, paras. 7.92-7.93.

²⁷¹Brazil had argued that the United States' request was untimely. The Panel found it unnecessary to rule on the timeliness of the United States' request, in the light of its ruling on the substantive question. (Panel Report, footnote 160 to para. 7.103)

²⁷²Panel Report, para. 7.103. (footnotes omitted)

²⁷³United States' appellant's submission, para. 494.

²⁷⁴*Ibid.*, paras. 495-496.

²⁷⁵United States' appellant's submission, para. 497.

²⁷⁶Brazil's appellee's submission, paras. 228-229 (referring to Appellate Body Report, *US – FSC*, para. 161).

which are central elements in a determination of whether a program constitutes an export subsidy under item (j) of the Illustrative List of Export Subsidies included as Annex I to the *SCM Agreement*.²⁷⁷ Furthermore, the Panel made a factual finding that the documentary evidence cited by Brazil to support its preliminary view included a link to a United States government website with data showing that revenues for the export credit guarantee programs do not cover long-term operating costs and losses, which addressed the programs overall, rather than in connection with only upland cotton.²⁷⁸ Thus, according to Brazil, its statement of available evidence met the requirements of Article 4.2, by identifying the export credit guarantee measures, and providing and describing available evidence of "the character of" those measures, across all eligible commodities, as export subsidies.²⁷⁹

2. Did Brazil's Statement of Available Evidence Include Export Credit Guarantees to Other Eligible Agricultural Commodities?

301. The issue raised on appeal is whether the Panel correctly concluded that Brazil's statement of available evidence was not limited to export credit guarantees to upland cotton and included export credit guarantees to other eligible agricultural commodities.²⁸⁰ The requirement that a party challenging a prohibited subsidy provide a statement of available evidence is set out in Article 4.2 of the *SCM Agreement*, which provides:

A request for consultations under paragraph 1 shall include a statement of available evidence with regard to the existence and nature of the subsidy in question.

Article 4.2 is included in Appendix 2 of the DSU as a special or additional rule on dispute settlement.

302. The Appellate Body has stated that Article 4.2 of the *SCM Agreement* must be read and applied together with Article 4.4 of the DSU, which sets out the requirements for the request for consultations, "so that a request for consultations relating to a prohibited subsidy claim under the *SCM Agreement* must satisfy the requirements of both provisions".²⁸¹ It has also explained that the

²⁷⁷Brazil's appellee's submission, para. 230.

²⁷⁸*Ibid.*, paras. 231-232 (referring to Panel Report, paras. 7.92-7.93).

²⁷⁹*Ibid.*, para. 233.

²⁸⁰The United States does not contest that Brazil submitted a statement of available evidence together with its request for consultations. Nor does the United States contest that Brazil's statement of available evidence referred to the United States' export credit guarantees as they relate to upland cotton.

²⁸¹Appellate Body Report, *US – FSC*, para. 159.

"additional requirement of 'a statement of available evidence' under Article 4.2 of the *SCM Agreement* is distinct from—and not satisfied by compliance with—the requirements of Article 4.4 of the DSU".²⁸²

303. Brazil's statement of available evidence is annexed to its request for consultations. As the Panel noted²⁸³, the statement contains the following two paragraphs referring specifically to the United States' export credit guarantee programs:

US export credit guarantee programs have caused serious prejudice to Brazilian upland cotton producers by providing below-market financing benefits for the export of competing US upland cotton;

US export credit guarantee programs, since their origin in 1980 and up [to] the present, provide premium rates that are inadequate to cover the long-term operating costs and losses of the programs; in particular there were losses caused by large-scale defaults totalling billions of dollars that have not been reflected in increased premiums to cover such losses[.]²⁸⁴

304. The United States asserts that Brazil's statement of evidence does not mention any agricultural commodity other than upland cotton when it refers to the United States' export credit guarantee programs. This is correct. At the same time, however, we observe that the second paragraph is not expressly limited to upland cotton. Rather, that paragraph refers to the United States' export credit guarantee programs in a general way, suggesting that the reference is to the programs as a whole and not just as they relate to one specific agricultural commodity. The allegation in that paragraph that the premium rates are inadequate to cover the long-term operating costs and losses of the programs is equally broad and does not suggest that it is only with respect to upland cotton that premiums are insufficient to offset costs and losses. As the Panel explained, when the second "paragraph is read in light of footnote 1 of the request for consultations, a careful reader should have been alerted to the fact that this paragraph referred to alleged subsidies arising from export credit guarantees under the challenged programmes, without any limitation to upland cotton or any other particular product or products".²⁸⁵ Thus, we do not find that it was unreasonable for the Panel to have "read Brazil's statement of available evidence, insofar as Brazil's export subsidy claims are concerned, to refer to

²⁸² Appellate Body Report, *US – FSC*, para. 161.

²⁸³ Panel Report, para. 7.83.

²⁸⁴ Statement of available evidence annexed to the Request for Consultations by Brazil, *supra*, footnote 26, para. 3.

²⁸⁵ Panel Report, para. 7.85. (footnote omitted) The text of footnote 1 is reproduced, *supra*, footnote 269.

each of the three challenged United States export subsidy programmes as they relate to upland cotton and other eligible agricultural products".²⁸⁶

305. The United States submits that, even if the second paragraph were construed to refer to programs that provide benefits to products in addition to upland cotton, it is "difficult to see"²⁸⁷ how that paragraph meets the requirements of Article 4.2 of the *SCM Agreement*, as it does not provide information about the "existence" or "nature" of the subsidies allegedly provided by the export credit guarantee programs to products in addition to upland cotton. The Panel rejected the United States' argument because it considered that:

Brazil's statement of available evidence indicates Brazil's view that the character of the alleged subsidy lay in the provision of export credit guarantees under programmes "at premium rates that are inadequate to cover the long-term operating costs and losses of the programs; in particular there were losses caused by large-scale defaults totalling billions of dollars that have not been reflected in increased premiums to cover such losses."²⁸⁸

From this, the Panel concluded that Brazil "had evidence available to it at that time which led it to conclude that the United States was providing a prohibited export subsidy of this nature and character under the three identified export subsidy programmes, without any limitation to a particular product or products".²⁸⁹

306. We recall that Article 4.2 requires that the request for consultations "include a statement of available evidence with regard to the existence and nature of the subsidy in question". In *US – FSC*, the Appellate Body explained that this means that "it is available evidence of the character of the measure as a 'subsidy' that must be indicated, and not merely evidence of the existence of the measure".²⁹⁰ We observe that, in Brazil's statement of available evidence, the second paragraph that deals specifically with the United States' export credit guarantee programs does not simply refer to their existence. In that paragraph, Brazil indicates that the export credit guarantees have the

²⁸⁶ Panel Report, para. 7.86.

²⁸⁷ United States' appellant's submission, para. 497.

²⁸⁸ Panel Report, para. 7.89 (quoting statement of available evidence, *supra*, footnote 284, para. 3).

²⁸⁹ *Ibid.*, para. 7.90.

²⁹⁰ Appellate Body Report, *US – FSC*, para. 161. In that case, the European Communities did not provide a separate statement of available evidence, but argued that such a statement was contained in the request for consultations itself. The Panel found that the consultations request may have contained a statement of available evidence. The Appellate Body noted that it "would have preferred that the Panel give less relaxed treatment to this important distinction" between the existence and the character of the measure as a subsidy, but it ultimately ruled that the United States' objection to the request for consultations had been untimely and therefore it did not rule on whether the consultations request included a statement of available evidence. (*Ibid.*, paras. 155, 161, and 165)

"character" of a subsidy because the premiums charged are insufficient to cover the long-term operating costs and losses. Brazil goes further by stating that this situation is especially due to the fact that the premiums have not increased despite "large-scale defaults totalling billions of dollars".²⁹¹

307. In addition, as the Panel pointed out, Brazil referred to a website of the United States Congressional Budget Office. This website includes projections of the mandatory spending of the United States federal government. One of the tables provided on the website contains a line-item that specifically refers to spending by the CCC, which, according to the title of the table, already takes into account offsetting receipts. Thus, by referring to this website, Brazil's statement of evidence was also indicating that the export credit guarantees have the "character" of a subsidy because the premiums charged are insufficient to cover the long-term operating costs and losses. Therefore, the Panel had a reasonable basis to conclude that Brazil's statement of evidence met the requirements of Article 4.2 of the *SCM Agreement*.

308. We recognize that the statement of available evidence plays an important role in WTO dispute settlement. The adequacy of the statement of available evidence must be determined on a case by case basis. As the Panel stated, moreover, the "statement of available evidence ... is the starting point for consultations, and for the emergence of more evidence concerning the measures by reason of the clarification of the 'situation'".²⁹² It is, therefore, important to bear in mind that the requirement to submit a statement of available evidence applies in the earliest stages of WTO dispute settlement, and that the requirement is to provide a "statement" of the evidence and not the evidence itself.²⁹³

309. For these reasons, we *uphold* the Panel's ruling, in paragraph 7.103 of the Panel Report, that "Brazil provided a statement of available evidence with respect to export credit guarantee measures relating to upland cotton and eligible United States agricultural products other than upland cotton, as required by Article 4.2 of the *SCM Agreement*". (footnote omitted)

²⁹¹Statement of available evidence annexed to the Request for Consultations by Brazil, *supra*, footnote 26, para. 3.

²⁹²Panel Report, para. 7.100.

²⁹³Panel Report, *Australia – Automotive Leather II*, para. 9.19.

V. Domestic Support

A. Article 13(a) of the Agreement on Agriculture – Planting Flexibility Limitations

1. Introduction

310. We turn now to consider appeals by the United States and Brazil regarding the application of Article 13 of the *Agreement on Agriculture* (often referred to as the "peace clause"). We first address the issue of whether two types of payment—production flexibility contract payments and direct payments—are entitled to the exemption from action established by paragraph (a) of Article 13.

311. Production flexibility contract payments were introduced by the FAIR Act of 1996 for the 1996-2002 marketing years, and were made to certain historical producers of seven eligible commodities, including upland cotton. Historical producers could enroll acres upon which upland cotton had been grown during a base period and were allocated upland cotton "base acres" (as well as a farm-specific yield per acre), for which payment would be made at a rate specified each year for upland cotton. The production flexibility contract program dispensed with the requirement that producers continue to plant upland cotton in order to receive payments; instead, payments would generally be made regardless of what the producer chose to grow, and whether or not the producer chose to produce anything at all. However, there were limits to this planting flexibility. Specifically, payments were reduced or eliminated if fruits and vegetables (other than lentils, mung beans, and dry peas) were planted on upland cotton base acres, subject to certain other exceptions.²⁹⁴

312. Direct payments were introduced by the FSRI Act of 2002 for the 2002-2007 marketing years. They essentially replaced production flexibility contract payments under the FAIR Act of 1996, while also expanding the program to take in historical production of some additional commodities.²⁹⁵ Both production flexibility contract payments and direct payments were available for the 2002 crop, but production flexibility contract payments made for that crop were deducted from direct payments made for that crop.²⁹⁶ Like production flexibility contract payments for upland cotton, direct payments for upland cotton were dependent on base acres allocated by reference to the

²⁹⁴Panel Report, paras. 7.212-7.215 and 7.376-7.378. The exceptions from planting flexibility limitations related to regions with a history of double cropping or farms with a history of planting fruits or vegetables on contract acreage. (*Ibid.*, para. 7.378)

²⁹⁵*Ibid.*, paras. 7.218-7.219 and 7.397. The Panel discusses similarities and differences between the production flexibility contract program and the direct payment program in paragraphs 7.398-7.399.

²⁹⁶*Ibid.*, para. 7.220.

production of upland cotton during certain base periods.²⁹⁷ The payments were made each year at a rate fixed for the entire 2002-2007 period at 6.67 cents per pound of upland cotton. As was the case under the production flexibility contract program, producers were not required to grow any particular crop in order to receive direct payments, and could choose to grow nothing at all. In addition to fruits and vegetables (other than lentils, mung beans, and dry peas), wild rice was added to the planting flexibility limitations.²⁹⁸

313. The Panel found that the amount of payments under the production flexibility contract program and the direct payment program is "related to the type of production undertaken by the producer after the base period."²⁹⁹ On this basis, the Panel found that these payments and "the legislative and regulatory provisions that provide for the planting flexibility limitations in the DP programme" do not fully conform to paragraph 6(b) of Annex 2 of the *Agreement on Agriculture*.³⁰⁰ The Panel concluded that these measures are thus not green box measures³⁰¹, and added that these measures "do not comply with the condition in paragraph (a) of Article 13 of the *Agreement on Agriculture*" and are therefore "non-green box measures covered by paragraph (b) of Article 13."³⁰²

2. Appeal by the United States

314. The United States appeals the Panel's finding that direct payments, production flexibility contract payments, and the legislative and regulatory provisions that establish and maintain the direct payments program, are not green box measures sheltered from challenge by virtue of Article 13(a) of the *Agreement on Agriculture*. The United States does not dispute that the amount of payments under the production flexibility contract and direct payment programs depended upon a formula that centred on "base acres" tied to the historical production of upland cotton.³⁰³ Nor does the United States dispute that there are limitations on producers' ability to plant any product, if those producers wish to

²⁹⁷There was a limited opportunity for producers to elect a different base period for the calculation of upland cotton base acres for direct payments under the FSRI Act of 2002 from that prevailing for production flexibility contract payments under the FAIR Act of 1996. (Panel Report, paras. 7.220-7.221) Brazil has conditionally appealed the Panel's exercise of judicial economy in respect of Brazil's claim that this "updating" of base acres contravenes paragraph 6(a) of Annex 2 of the *Agreement on Agriculture*. We address this conditional appeal below at section V.B of this Report.

²⁹⁸Panel Report, paras. 7.220, 7.222, and 7.379-7.381. As was the case under the production flexibility contract program, there were limited exceptions to the planting flexibility limitations.

²⁹⁹*Ibid.*, para. 7.385.

³⁰⁰*Ibid.*, para. 7.388.

³⁰¹*Ibid.*, para. 7.413.

³⁰²*Ibid.*, para. 7.414.

³⁰³United States' appellant's submission, para. 17.

receive production flexibility or direct payments with respect to upland cotton base acres.³⁰⁴ In the case of production flexibility contract payments, these limitations related to the growing of fruits and vegetables. In the case of direct payments, the limitations extended to wild rice as well.³⁰⁵ Beyond these limitations, however, the United States stresses that a producer can receive production flexibility contract payments or direct payments regardless of the agricultural products that the producer chooses to grow and irrespective of whether it chooses to produce any product at all.³⁰⁶

315. The United States takes issue with the Panel's finding that the planting flexibility limitations mean that the "amount of payments" under the production flexibility contract and direct payment programs is "related to the type of production undertaken by the producer after the base period", within the meaning of paragraph 6(b) of Annex 2 to the *Agreement on Agriculture*.³⁰⁷ According to the United States, a *negative* direction in respect of production of certain goods—that is, conditioning payment on a producer's *non*-production of certain goods—does not make the amount of payments "related to the type of production". The United States submits that this interpretation serves the "fundamental requirement" found in paragraph 1 of Annex 2 that green box measures "have no, or at most minimal, trade-distorting effects or effects on production".

316. Brazil requests that the Appellate Body uphold the Panel's finding, under paragraph 6(b) of Annex 2 of the *Agreement on Agriculture*, that production flexibility contract and direct payments relate "the amount of" the payment to "the type of production undertaken" by recipients.³⁰⁸ The grounds for the Panel's finding are that production flexibility contract and direct payments are made solely if production is undertaken of crops other than fruits and vegetables (and, in the case of direct payments, wild rice as well). Brazil agrees with the Panel that this relates the amount of payments to production of the "permitted" crops. As the Panel found, if "permitted" crops alone are produced, a full payment is made. If a small quantity of "prohibited" crops is produced, the "amount of payment" is reduced. If a larger quantity of "prohibited" crops is produced, no payment is made.³⁰⁹

317. Brazil submits that the distinction drawn by the United States between "permitted" (or positive) and "prohibited" (or negative) categories of crops is artificial because the effect of both

³⁰⁴See, for example, United States' appellant's submission, paras. 17 ff.

³⁰⁵United States' appellant's submission, para. 18.

³⁰⁶*Ibid.*

³⁰⁷Panel Report, para. 7.385; United States' appellant's submission, paras. 22 ff.

³⁰⁸Panel Report, para. 7.385; Brazil's appellee's submission, paras. 260 ff.

³⁰⁹Brazil's appellee's submission, para. 285 (referring to Panel Report, paras. 7.382-7.383). The participants, like the Panel, refer to "permitted" and "prohibited" crops, in the sense that crops not subject to planting flexibility limitations are eligible to receive payments, while fruits and vegetables (and wild rice) are not eligible to receive payments. We generally prefer to refer to these categories as "covered" or "eligible" crops, on the one hand, and "excluded" crops on the other.

categories is identical: in both cases, production is channelled *away from* certain "prohibited" crops (for which no payments are made) and *towards* other "permitted" crops (for which payments are made). Thus, the incentives and disincentives are precisely the same. In both cases, "the amount of" the payment is intrinsically "related to" undertaking production of the "permitted" crops, and not undertaking production of the "prohibited" crops. According to Brazil, the Panel's factual findings support this view because it found that the prohibition on fruits and vegetables (and wild rice in respect of direct payments) imposes "significant constraints" on production decisions and creates incentives for the production of eligible crops rather than those crops that are prohibited.³¹⁰

3. Analysis

318. Article 13 of the *Agreement on Agriculture*, entitled "Due Restraint", provides in relevant part that:

During the implementation period, notwithstanding the provisions of GATT 1994 and the Agreement on Subsidies and Countervailing Measures (referred to in this Article as the "Subsidies Agreement"):

- (a) domestic support measures that conform fully to the provisions of Annex 2 to this Agreement shall be: ...
- (ii) exempt from actions based on Article XVI of GATT 1994 and Part III of the Subsidies Agreement; ...

319. Accordingly, domestic support that conforms fully to the provisions of Annex 2—that is "green box" support, which is exempt from the domestic support reduction obligations of the *Agreement on Agriculture*—is also exempt, during the implementation period³¹¹, from actions based on Article XVI of GATT 1994 and the actionable subsidies provisions of Part III of the *SCM Agreement*.

320. The United States claims that production flexibility contract payments and direct payments are domestic support that conforms fully to the provisions of Annex 2 because they are "[d]ecoupled income support" within the meaning of paragraph 6 of that Annex. Annex 2 is entitled "Domestic

³¹⁰Brazil's appellee's submission, paras. 285-286 (quoting Panel Report, para. 7.386).

³¹¹The "implementation period" during which Article 13 applies is defined in Article 1(f) of the *Agreement on Agriculture* as "the nine-year period commencing in 1995", "Year", for purposes of Article 1(f) "and in relation to the specific commitments of a Member" is defined in Article 1(f) and is "the calendar, financial or marketing year specified in the Schedule relating to that Member".

Support: The Basis for Exemption from the Reduction Commitments" and provides, in relevant part, as follows:

1. Domestic support measures for which exemption from the reduction commitments is claimed shall meet the *fundamental requirement* that they have *no, or at most minimal, trade-distorting effects or effects on production*. Accordingly, all measures for which exemption is claimed shall conform to the following basic criteria:

- (a) the support in question shall be provided through a publicly-funded government programme (including government revenue foregone) not involving transfers from consumers; and,
- (b) the support in question shall not have the effect of providing price support to producers;

plus policy-specific criteria and conditions as set out below.

5. *Direct payments to producers*

Support provided through direct payments (or revenue foregone, including payments in kind) to producers for which exemption from reduction commitments is claimed shall meet the basic criteria set out in paragraph 1 above, plus specific criteria applying to individual types of direct payment as set out in paragraphs 6 through 13 below. ...

6. *Decoupled income support*

- (a) Eligibility for such payments shall be determined by *clearly-defined criteria* such as income, status as a producer or landowner, factor use or production level in a *defined and fixed base period*.
- (b) *The amount of such payments in any given year shall not be related to, or based on, the type or volume of production* (including livestock units) undertaken by the producer in any year *after* the base period.
- (c) *No production shall be required* in order to receive such payments. (emphasis added)

321. Paragraph 6, entitled, "[d]ecoupled income support" applies to one type of "direct payment" to producers that may benefit from exemption from reduction commitments and protection under the peace clause. Paragraph 6(a) sets forth that eligibility for payments under a decoupled income support program must be determined by reference to certain "clearly-defined criteria" in a "defined

and fixed base period". Paragraph 6(b) requires the severing of any link between the *amount of payments* under such a program and the *type or volume of production* undertaken by recipients of payments under that program in any year after the base period. Paragraphs 6(c) and 6(d) serve to require that payments are also decoupled from *prices* and *factors of production employed* after the base period. Paragraph 6(e) makes it clear that "[n]o production shall be required in order to receive ... payments" under a decoupled income support program.

322. As we noted above³¹², there is no disagreement between the participants that the amount of payments under the production flexibility contract and direct payment programs depended upon a formula that centred on "base acres", which were established on the basis of the historical production of upland cotton. Nor does the United States dispute that there are limitations on producers' ability to produce certain products, while also receiving production flexibility contract payments or direct payments with respect to upland cotton base acres. Therefore, the question before us regarding the consistency of production flexibility contract payments and direct payments with paragraph 6(b) of Annex 2 is a limited one. It does not concern a measure *requiring* producers to grow certain crops in order to receive payments; it also does not concern a measure with complete planting *flexibility* that provides payments without regard whatsoever to the crops that are grown. Indeed, it does not concern a measure that requires the production of any crop at all; nor does it involve a measure that totally *prohibits* the growing of any crops as a condition for payments. The question before us in this appeal thus concerns a measure with a *partial* exclusion combining planting flexibility and payments with the reduction or elimination of the payments when the excluded crops are produced, while providing payments even when no crops are produced at all.

323. In addressing the question of the consistency of such a measure with paragraph 6(b), we note that under this provision, for income support to be *decoupled*, the "amount of such payments ... shall not be related to ... the type or volume of production ... undertaken by the producer in any year after the base period". It is uncontested that the amount of payments under the production flexibility contract and direct payment programs may be affected, depending upon whether a producer plants a crop that is permitted under the production flexibility contract or direct payment programs, or a crop that is covered by the planting flexibility limitations.³¹³ The United States focuses on the term "related to" and contends that the amount of payments under the production flexibility contract and direct payment programs is not "related to" the type of production as proscribed by paragraph 6(b).

³¹² *Supra*, para. 314.

³¹³ United States' appellant's submission, para. 18.

324. The ordinary meaning of the term "related to" in paragraph 6(b) of Annex 2 denotes some degree of *relationship* or *connection* between two things³¹⁴, here the amount of payment, on the one hand, and the type or volume of production, on the other. It covers a broader set of connections than "based on", which term is also used to describe the relationship between two things covered by paragraph 6(b).³¹⁵ Nothing in the ordinary meaning of the term "related to" suggests that the connections covered by this expression may not encompass connections of either a "positive" nature (including directions or requirements to do something) or a "negative" nature (including prohibitions or requirements not to do something) or a combination of both. As the Panel indicated, the ordinary meaning of the term "related to" conveys "a very general notion".³¹⁶ Indeed, the United States agrees that, as far as its ordinary meaning in the abstract is concerned, the term "related to" may be broad enough to capture both positive and negative connections, but argues that the context of paragraph 6(b) requires a more limited interpretation of the term, namely, only as covering a "positive" connection between the "amount of ... payments" and the "type ... of production".³¹⁷ Like the Panel, however, we are of the view that, in the context of paragraph 6(b), the term "related to" covers both positive and negative connections between the amount of payment and the type of production.

325. Paragraph 6 of Annex 2, entitled "[d]ecoupled income support", seeks to decouple or de-link direct payments to producers from various aspects of their production decisions and thus aims at neutrality in this regard. Subparagraph (b) decouples the payments from production; subparagraph (c) decouples payments from prices; and subparagraph (d) decouples payments from factors of production. Subparagraph (e) completes the process by making it clear that no production shall be required in order to receive such payments. Decoupling of payments from production under paragraph 6(b) can only be ensured if the payments are not related to, or based upon, either a positive

³¹⁴ See *Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.), (Oxford University Press, 2002), Vol. 2, p. 2520; see also Panel Report, para. 7.366; United States' appellant's submission, para. 25; and Brazil's appellee's submission, para. 282.

³¹⁵ The Panel noted that "base" in this context may be defined as to "found, build, or construct (*upon*) a given base, build up *around* a base (chiefly *fig.*)"; Panel Report, para. 7.366 (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 1, p. 187). Like the expression "related to", the expression "based on" also requires a connection between two or more things. However, even though "based on" does not require a strict relationship between two things (see, e.g., Appellate Body Report, *EC – Hormones*, paras. 165-166 and 171), the meaning of "based on" indicates a relatively close connection between the things being linked. By contrast, the meaning of "related to" can apply to connections more general in nature than situations in which one thing is "based on" another (see, e.g., Appellate Body Report, *US – Softwood Lumber IV*, para. 89, where the Appellate Body interpreted broadly the phrase "in relation to" in Article 14(d) of the *SCM Agreement*). Accordingly, the meaning of the term "related to" cannot be entirely subsumed into the meaning of "based on".

³¹⁶ Panel Report, para. 7.366.

³¹⁷ United States' appellant's submission, para. 25.

requirement to produce certain crops or a negative requirement not to produce certain crops or a combination of both positive and negative requirements on production of crops.

326. In contrast to the other subparagraphs of paragraph 6, paragraph 6(e) does explicitly distinguish between positive and negative production requirements, because it prohibits positive requirements to produce. The Panel reasoned that "[i]f paragraph 6(b) could be satisfied by ensuring that no production was required to receive payments, paragraph 6(e) would be redundant".³¹⁸ We agree with the Panel that the context provided by paragraph 6(e) indicates that a measure that provided payments, even if a producer undertook no production at all, would not, for that reason alone, necessarily comply with paragraph 6(b). This is because other elements of that measure might still relate the amount of payments to the type or volume of production, contrary to the requirement of paragraph 6(b).

327. The United States seems to argue that the Panel's interpretation of the relationship between paragraphs 6(b) and 6(e) would subsume paragraph 6(e) within the scope of paragraph 6(b), thereby rendering it redundant.³¹⁹ In our view, however, paragraph 6(e) continues to serve a purpose distinct from that of paragraph 6(b). It highlights a different aspect of decoupling income support. In prohibiting Members from making green-box measures contingent on production, paragraph 6(e) implies that Members are allowed, in principle, to require no production at all. Accordingly, payments conditioned on a total ban on any production may qualify as decoupled income support under paragraph 6(e). Even assuming that payments contingent on a total production ban could be seen to relate the amount of the payment to the *volume* of production within the meaning of paragraph 6(b)—the volume of production being nil—giving meaning and effect to both paragraphs 6(b) and 6(e) suggests a reading of paragraph 6(b) that would not disallow a total ban on any production.

328. In addressing the United States' argument on this point, we recall that the measures at issue in this appeal do not provide for payments contingent on a *total ban* on production of *any* crops. The measures at issue here combine payments and planting flexibility in respect of certain covered crops with the reduction or elimination of such payments when certain other excluded crops are produced. The United States argues that, if paragraph 6(e) means that a Member may require a producer not to produce a particular product, "it would not make sense to then prohibit a Member, under paragraph 6(b), from making the amount of payment contingent on fulfilling that requirement".³²⁰

³¹⁸Panel Report, para. 7.368.

³¹⁹United States' appellant's submission, paras. 38-42.

³²⁰*Ibid.*, para. 38. (emphasis omitted)

However, in our view, the mere fact that under paragraph 6(e) "[n]o production shall be required in order to receive such payments" does not mean that a partial exclusion of certain crops from payments, coupled with production flexibility regarding other crops, must be consistent with paragraph 6(b).

329. We agree with the Panel that a partial exclusion of some crops from payments has the potential to channel production towards the production of crops that remain eligible for payments.³²¹ In contrast to a total production ban, the channeling of production that may follow from a partial exclusion of some crops from payments will have *positive* production effects as regards crops eligible for payments. The extent of this will depend on the scope of the exclusion. We note in this regard that the Panel found, as a matter of fact, that planting flexibility limitations at issue in this case "significantly constrain production choices available to PFC and DP payment recipients and effectively eliminate a significant proportion of them".³²² The fact that farmers may continue to receive payments if they produce nothing at all does not detract from this assessment because, according to the Panel, it is not the option preferred by the "overwhelming majority" of farmers, who continue to produce some type of permitted crop.³²³ In the light of these findings by the Panel, we are unable to agree with the United States' argument that the planting flexibility limitations only negatively affect the production of crops that are excluded.

330. We are not persuaded otherwise by the United States' reliance upon the terms "amount of such payments" and "undertaken" in the text of paragraph 6(b). According to the United States, the Panel assumes that the "amount of such payments" in paragraph 6(b) can be related to the current type of production because, in some circumstances, a recipient that produces fruits, vegetables or wild rice "receives less payment than that recipient otherwise would have been entitled to".³²⁴ However, for the United States, in that case, the only "amount" of payment that is even arguably "related to" current production is "zero"³²⁵, because those crops are excluded from payment eligibility. The United States further argues, with respect to the phrase "production ... undertaken by the producer", that the ordinary meaning of the term "undertake" includes to "attempt". In this case, the planting flexibility limitations on a certain range of products, with respect to base acreage, would not relate the amount of payments

³²¹Panel Report, para. 7.367. Indeed, as Brazil submits, this will tend to be the case where the prohibition prevents a producer, intent on maximizing profit, from growing the best alternative crop. In that case, the producer will tend to choose the next best alternative from amongst the permitted crops. (Brazil's appellee's submission, para. 321, citing evidence, referred to in footnote 511 of the Panel Report, from Brazil's expert, Professor Sumner)

³²²Panel Report, para. 7.386.

³²³*Ibid.*, para. 7.386.

³²⁴United States' appellant's submission, para. 26.

³²⁵*Ibid.*

to production "attempted" by the recipient; rather, the amount of payment is related to or based on the type of production *not* "attempted".³²⁶

331. In our view, the concepts of "type or volume of production ... undertaken by the producer" and the "amount of ... payments" are linked in paragraph 6(b) by the requirement that one "not be related to" the other. This requires a consideration of *the relationship* between the type or volume of production and the amount of payment under a program after the base period. A program that disallows payments when certain crops are produced relates the amount of the payment to the type of production undertaken. The flexibility to produce and receive payment for certain crops covered by a program, combined with the reduction or elimination of such payments when excluded crops are produced, creates a link with the type of production undertaken contrary to paragraph 6(b). This is so because the opportunity for farmers to receive payments for producing covered crops, while less or no such payments are made to farmers who produce excluded crops, provides an incentive to switch from producing excluded crops to producing crops eligible for payments.

332. The United States also contends that its measures, which condition payment on the non-production of certain products, "further the fundamental requirement [in paragraph 1 of Annex 2 to the *Agreement on Agriculture*] that such measures 'have no, or at most minimal, trade-distorting effects or effects on production'"³²⁷, because their only effects are to reduce production of the prohibited crops.³²⁸ It follows, for the United States, that paragraph 6(b) should not address "negative" prohibitions on the production of certain crops, such as the United States' measures, given that they comply, inherently, with the fundamental requirement.³²⁹ Brazil argues that if paragraph 6(b) is violated, this *ipso facto* violates the fundamental requirement of paragraph 1 of Annex 2 and further analysis is not required.³³⁰

333. We note that the first sentence of paragraph 1 of Annex 2 lays down a "fundamental requirement" for green box measures, such that they must have "no, or at most minimal, trade-distorting effects or effects on production". The second sentence of paragraph 1 provides that "[a]ccordingly", green box measures must conform to the basic criteria stated in that sentence, "plus"

the policy-specific criteria and conditions set out in the remaining paragraphs of Annex 2, including those in paragraph 6.³³¹

334. As we have noted, the Panel found that the planting flexibility limitations in this case "significantly constrain" production decisions.³³² However one reads the "fundamental requirement" in paragraph 1 of Annex 2, given the factual findings of the Panel, the facts of this case do not present a situation in which the planting flexibility limitations demonstrably have "no, or at most minimal," trade-distorting effects or effects on production.

335. We find further support for our interpretation of paragraph 6(b) in the context provided by paragraph 11 of Annex 2, entitled "Structural adjustment assistance provided through investment aids". Several of the subparagraphs of paragraph 11 are phrased in similar terms to those of paragraph 6. Indeed, like paragraph 6(b), paragraph 11(b) requires that the "amount of ... payments ... shall not be related to ... the type or volume of production ... undertaken by the producer in any year after the base period." However, unlike paragraph 6(b), paragraph 11(b) ends with the phrase "other than as provided for under criterion (e) below". Criterion 11(e) specifically envisages that "payments shall not mandate or in any way designate the agricultural products to be produced by the recipients except to require them not to produce a particular product".

336. We note that the exception provided by paragraph 11(e) and the link to paragraph 11(e) in paragraph 11(b) explicitly *authorize* the type of "negative" requirements not to produce that the United States argues is implicitly *permitted* by the terms of paragraph 6(b). In the light of the similarity of the language chosen in paragraphs 6(b) and 11(b), like the Panel, we attach significance to the fact that the drafters saw as necessary an explicit authorization of negative requirements not to produce under paragraph 11(b). In our view, this indicates that the ordinary meaning of the terms in paragraph 11(b) would otherwise exclude an interpretation allowing such negative requirements. The use of identical language in paragraphs 6(b) and 11(b), except for the reference in paragraph 11(b) to paragraph 11(e), suggests that the meaning of the terms in paragraph 6(b) must be the same as in paragraph 11(b). Accordingly, a comparison of these provisions confirms that the terms of paragraph 6(b) encompass both positive as well as negative connections between the amount of payments under a program and the type of production undertaken.

337. We note that the United States argues that the context in which paragraphs 11(b) and 6(b) appear is very different. The United States notes that paragraph 11 pertains to payments "to assist the

³²⁶United States' appellant's submission, para. 27.

³²⁷Paragraph 1 of Annex 2 to the *Agreement on Agriculture*.

³²⁸United States' appellant's submission, para. 36.

³²⁹See *ibid.*, paras. 32-35.

³³⁰Brazil's responses to questioning at the oral hearing.

³³¹We note in this regard that the Panel's exercise of judicial economy regarding Brazil's claim that the United States measures at issue fail to conform with the "fundamental requirement" of paragraph 1 of Annex 2 has not been appealed. (See Panel Report, para. 7.412)

³³²*Ibid.*, para. 7.386.

financial or physical restructuring of a producer's operations"³³³ and paragraph 6(e) imposes a constraint on the degree to which a government can interfere in the form that restructuring will take. As a requirement not to produce certain products could be understood to fall within the prohibition in paragraph 11(e) against "in any way" designating the products to be produced, it clarifies that negative requirements are permitted. The United States submits that, in the light of the broad prohibition in paragraph 11(e), "the requirement in paragraph 11(b) ... could be understood to preclude conditioning payment on not producing certain products since this could be understood as in some way designating the products to be produced".³³⁴ This required the explicit cross-reference to paragraph 11(e). According to the United States, because the same considerations do not apply in the case of paragraph 6(b), no specific authorization of partial prohibitions on production is required, as it remains implicit in the text of the provision.³³⁵

338. We are not persuaded by this argument. Like Brazil, we believe that a more compelling reason for the specific authorization of negative requirements not to produce a particular crop may be found in the fact that paragraph 11 addresses "structural adjustment", which may be achieved only by providing financial incentives to shift production away from certain products. In our view, the considerations submitted by the United States do not render the meaning of the terms used in paragraph 11(b) different from the meaning of the same terms as used in paragraph 6(b).

339. Finally, we note that the United States has also argued that the Panel's interpretation, with which we agree, would require a Member to continue to make decoupled income support payments, even if a producer's production is *illegal*, for example involving the production of opium poppy, unapproved biotech varieties or environmentally-damaging production.³³⁶ According to the United States, this is a logical consequence of a finding that, to comply with paragraph 6(b) of Annex 2, a measure may not condition payments upon the non-production of certain products, while permitting production of others.

340. In our view, questions regarding the problem of illegal production contrast starkly with the situation addressed in the present case. It remains perfectly *legal* for a holder of upland cotton base acres to grow fruits, vegetables or wild rice in the United States. The consequence of growing such crops is simply the reduction or elimination of production flexibility contract or direct payments to the holders of upland cotton base acres. Our interpretation of paragraph 6(b) would not prevent a WTO

Member from making illegal the production of certain crops. Nor would it prevent a Member from providing decoupled income support while at the same time making the production of certain crops illegal. As Brazil states, there is nothing in the *Agreement on Agriculture* to suggest that the term "production" in paragraph 6 of Annex 2 refers to anything other than *lawful* production.³³⁷ In addition, we observe that specific provisions of the *Agreement on Agriculture* recognize, and exempt from reduction commitments, domestic support programs that address the problem of production of illicit narcotic crops in developing countries³³⁸ or payments under certain environmental programs.³³⁹

4. Conclusion

341. For all these reasons, we *uphold* the Panel's finding in paragraphs 7.388, 7.413, 7.414 and 8.1(b) of the Panel Report that conditioning production flexibility contract payments and direct payments on a producer's compliance with planting flexibility limitations regarding certain products, coupled with the flexibility to produce certain other products, means that the amount of payments under those measures is related to the type of production undertaken by a producer after the base period, within the meaning of paragraph 6(b) of Annex 2 of the *Agreement on Agriculture*.

342. Accordingly, we also *uphold* the Panel's finding, in paragraphs 7.413 and 7.414 of the Panel Report, that production flexibility contract payments and direct payments are not "decoupled income support" within the meaning of paragraph 6, are not green box measures exempt from the reduction commitments by virtue of Annex 2 of the *Agreement on Agriculture*, and are not, therefore, sheltered from challenge by virtue of paragraph (a) of Article 13 of the *Agreement on Agriculture*. Rather, these measures are support covered by the chapeau to paragraph (b) of Article 13, and are to be taken into account in the analysis of that provision.

B. *Article 13(a) of the Agreement on Agriculture – Base Period Update*

343. The Panel indicated that it had "already found that [direct] payments fail to conform to the provisions of paragraph 6 of Annex 2 due to the planting flexibility limitations". For this reason, it indicated that it was "therefore unnecessary for the purposes of this dispute to make findings on their conformity with paragraph 6 due to the updating" of base acres.³⁴⁰ Brazil conditionally appeals the Panel's exercise of judicial economy on the issue of whether the base period update under the direct

³³⁷Brazil's appellee's submission, para. 315.

³³⁸Article 6.2 of the *Agreement on Agriculture* exempts from domestic support reduction commitments that would otherwise be applicable "domestic support to producers in developing country Members to encourage diversification from growing illicit narcotic crops".

³³⁹See paragraph 12 of Annex 2 to the *Agreement on Agriculture*.

³⁴⁰Panel Report, para. 7.393.

payments program is consistent with paragraph 6(a) of Annex 2.³⁴¹ Brazil's appeal is conditional on the Appellate Body reversing the Panel's finding that direct payments, the legislative and regulatory provisions that establish and maintain the direct payments program, as well as payments under the production flexibility contract program, do not fall within the terms of paragraph (a) of Article 13 because they are not consistent with paragraph 6(b) of Annex 2.

344. Having upheld the Panel's finding under paragraph 6(b) of Annex 2 of the *Agreement on Agriculture*, the condition upon which Brazil's appeal regarding the updating of base acres under paragraph 6(a) rests is not fulfilled. It is therefore unnecessary for us to address this issue further.

C. *Article 13(b) of the Agreement on Agriculture – Non-Green Box Domestic Support*

1. Introduction

345. Having rejected the United States' appeal of the Panel's finding that production flexibility contract payments under the FAIR Act of 1996 and direct payments under the FSRI Act of 2002 are not green box measures sheltered from challenge by the provisions of Article 13(a) of the *Agreement on Agriculture*, we now turn to consider the United States' appeal regarding the application of Article 13(b) of the *Agreement on Agriculture*.

346. Article 13 of the *Agreement on Agriculture* is entitled "Due Restraint" and applies during the implementation period.³⁴² Article 13(b) of the *Agreement on Agriculture* provides, in relevant part:

[D]omestic support measures that conform fully to the provisions of Article 6 of this Agreement including direct payments that conform to the requirements of paragraph 5 thereof, as reflected in each Member's Schedule, as well as domestic support within *de minimis* levels and in conformity with paragraph 2 of Article 6, shall be:

...

(ii) exempt from actions based on paragraph 1 of Article XVI of GATT 1994 or Articles 5 and 6 of the Subsidies Agreement, provided that such measures do not grant support to a specific commodity in excess of that decided during the 1992 marketing year; ...

³⁴¹Brazil's other appellant's submission, paras. 237 ff.

³⁴²The "implementation period" during which Article 13 applies is defined in Article 1(f) of the *Agreement on Agriculture* as "the nine-year period commencing in 1995". "Year", for purposes of Article 1(f) "and in relation to the specific commitments of a Member" is defined in Article 1(i) and "refers to the calendar, financial or marketing year specified in the Schedule relating to that Member".

347. Subparagraph (ii) to Article 13(b) exempts non-green box domestic support measures described in the chapeau from actions based on Article XVI:1 of GATT 1994 and Articles 5 and 6 of the *SCM Agreement*. This exemption is, however, subject to a proviso and is thus made conditional upon a requirement that "such measures do not grant support to a specific commodity in excess of that decided during the 1992 marketing year". The dispute in the present appeal relates to the interpretation and application of this proviso to certain United States domestic support measures.³⁴³

348. Before the Panel, the United States claimed that its non-green box domestic support measures did not "grant support to a specific commodity in excess of that decided during the 1992 marketing year" and thus were consistent with the proviso to subparagraph (ii) of Article 13(b) of the *Agreement on Agriculture*. Hence, they were entitled to the exemption from action provided by Article 13(b).³⁴⁴

349. The Panel rejected the United States' argument that its measures did not "grant support to a specific commodity in excess of that decided during the 1992 marketing year". The Panel calculated values of support that were "decided during the 1992 marketing year" (the "1992 benchmark") as well as values of support by which the measures at issue "grant[ed] support to a specific commodity"—namely, upland cotton—in each of the years 1999, 2000, 2001, and 2002 ("implementation period support"). The Panel tabulated support attributable to upland cotton under the relevant United States domestic support measures and concluded that the support granted in each relevant year of the implementation period exceeded the 1992 benchmark.³⁴⁵ Accordingly, the Panel found that:

Brazil has discharged its burden to show that the United States domestic support measures at issue grant support to a specific commodity in excess of that decided during the 1992 marketing year.³⁴⁶

³⁴³Step 2 payments to domestic users; marketing loan program payments; production flexibility contract payments; market loss assistance payments; direct payments; counter-cyclical payments; crop insurance payments; and, cottonseed payments for the 2000 crop. (Panel Report, para. 7.337)

³⁴⁴The Panel noted that Brazil did not claim that the United States' domestic support measures do not comply with the conditions set out in the chapeau of Article 13(b). (Panel Report, paras. 7.415-7.416)

³⁴⁵*Ibid.*, paras. 7.596-7.597. The Panel indicated that the United States' implementation period support exceeded the 1992 benchmark regardless of whether, for certain price-based support measures, budgetary outlays or price gap methodology was used. (*Ibid.*, para. 7.597)

³⁴⁶*Ibid.*, para. 7.598.

350. After finding that evidence and arguments presented by the United States did not rebut Brazil's case³⁴⁷, the Panel concluded:

[I]n light of the above findings, ... that the [relevant] United States domestic support measures ... grant support to a specific commodity in excess of that decided during the 1992 marketing year and that, therefore, they are not exempt from actions based on paragraph 1 of Article XVI of the *GATT 1994* or Articles 5 and 6 of the *SCM Agreement*.³⁴⁸

2. Appeal by the United States

351. The United States appeals the Panel's finding that its relevant domestic support measures granted, during the implementation period, "support to a specific commodity in excess of that decided during the 1992 marketing year", and the consequential finding that these measures are therefore susceptible to challenge under the actionable subsidies provisions of Articles 5 and 6 of the *SCM Agreement* and Article XVI:1 of the *GATT 1994*.

352. The United States challenges, in particular, two elements of the Panel's reasoning. The United States first appeals the Panel's *interpretation* of the phrase "grant support to a specific commodity" in the proviso to Article 13(b)(ii), and, in particular, its finding that four types of payments made with respect to historical production of upland cotton—production flexibility contract payments, market loss assistance payments, direct payments and counter-cyclical payments—grant support to the specific commodity upland cotton, even though producers have flexibility under these programs to grow crops other than upland cotton or not to plant any crop at all. According to the United States, properly construed, the phrase "support to a specific commodity" refers to "product-specific support"³⁴⁹, which would exclude payments under these "non-product-specific" base acre dependent measures.³⁵⁰ It adds that, even if the Panel is correct in its interpretation that "support to a specific commodity" refers to all "non-green box support measures that clearly or explicitly define a commodity as one to which they bestow or confer support"³⁵¹, the Panel erred in the application of its test by allocating to upland cotton all payments to historic upland cotton base acres under these four programs, including those that went to planted commodities other than upland cotton.³⁵²

³⁴⁷Panel Report, para. 7.607.

³⁴⁸*Ibid.*, para. 7.608.

³⁴⁹United States' appellant's submission, para. 93.

³⁵⁰*Ibid.*, para. 105.

³⁵¹Panel Report, para. 7.494(i).

³⁵²United States' appellant's submission, paras. 101-107.

353. Secondly, the United States contests the Panel's use of budgetary outlay methodology to measure the value of support, for purposes of the comparison envisaged by Article 13(b)(ii), of two types of price-based payments: marketing loan program payments and deficiency payments.³⁵³ In this regard, the United States argues that the Panel erred in reading the word "grant" in Article 13(b)(ii) as meaning something actually provided, and not in harmony with the term "decided".³⁵⁴ The United States argues that this led the Panel erroneously to conclude that it could use a calculation methodology other than the price-gap methodology described in paragraph 10 of Annex 3 to the *Agreement on Agriculture* to measure the value of these price-based measures. According to the United States, only the price gap methodology can reflect the nature of the support "decided" under these programs because it filters out fluctuations in market prices; indeed, only the price gap methodology can measure those aspects of support that the government of a Member can control.³⁵⁵

354. The United States, having "corrected" the Panel's calculations for its alleged errors using its own methodologies, asserts that its domestic support measures at issue did not grant a level of product-specific support in any relevant year of the implementation period in excess of the 1992 benchmark.³⁵⁶ On this basis, the United States argues that its domestic support measures are consistent with the proviso to Article 13(b)(ii) of the *Agreement on Agriculture* and are, therefore, exempt from challenge under the peace clause.³⁵⁷

355. Brazil argues that if the Appellate Body upholds the Panel's finding with respect to the interpretation of the phrase "support to a specific commodity" and thereby finds that production flexibility contract payments, market loss assistance payments, direct payments and counter-cyclical payments cannot be excluded from the calculation of support under Article 13(b)(ii), then, regardless of the methodology used to calculate the value of marketing loan program payments and deficiency payments, the United States measures would still exceed the 1992 benchmark.³⁵⁸ Brazil contends that the Panel was correct to find that "support to a specific commodity" does not mean "product-specific support", or support that is directed specifically at only one product, but may capture all "non-green

³⁵³Marketing loan program payments in respect of both the 1992 benchmark and the implementation period support, and deficiency payments in respect of the 1992 benchmark only. (United States' appellant's submission, para. 72)

³⁵⁴*Ibid.*, paras. 64-68. The United States reiterates this argument in the section of its appellant's submission dealing with the interpretation of the phrase "support to a specific commodity": see *ibid.*, paras. 114-116.

³⁵⁵*Ibid.*, paras. 69-75.

³⁵⁶*Ibid.*, paras. 120-122.

³⁵⁷*Ibid.*, paras. 122-124.

³⁵⁸Brazil's appellee's submission, para. 330.

box measures, that clearly or explicitly define a commodity as one to which they bestow or confer support".³⁵⁹

356. Brazil also contends that the Panel was correct to use budgetary outlays for its analysis of the United States' price-based measures. Brazil observes that paragraph 10 of Annex 3 of the *Agreement on Agriculture* permits, in principle, the use of *either* budgetary outlays or the price gap methodology for payments based on price gaps.³⁶⁰ There is thus no textual basis to say that only price gaps may be used to measure these types of payments. Brazil also submits that the Panel correctly found that the term "grant" refers to what a measure actually provides³⁶¹, and therefore contests the United States' claim that factors beyond the control of government, such as market price fluctuations, must be filtered out of the analysis envisaged by the proviso to Article 13(b)(ii) through use of the price gap methodology.³⁶² Brazil also points out that the United States notified the level of support conferred by the marketing loan program for purposes of its base level Aggregate Measurement of Support ("AMS"), as well as in subsequent AMS notifications, through use of a budgetary outlay methodology.³⁶³ According to Brazil, WTO Members should be able to rely upon AMS notifications to determine whether the notifying Member was entitled, during the implementation period, to the protection conferred by the peace clause.

357. Finally, Brazil illustrates that, even using the price gap methodology to calculate the level of support under the deficiency payment and marketing loan payment programs, total United States support still exceeded the 1992 benchmark in each relevant year of the implementation period.³⁶⁴

3. Analysis

358. The United States appeals the Panel's finding that the United States' non-green box domestic support measures granted "support to a specific commodity", namely, upland cotton, during the implementation period, "in excess of that decided during the 1992 marketing year", and the consequential finding that this support was therefore not sheltered from challenge under Article XVI:1 of the GATT 1994 or Articles 5 and 6 of the *SCM Agreement*. The United States' appeal in this regard has two dimensions. First, the United States challenges the Panel's *interpretation* of the phrase "support to a specific commodity" used in the proviso to Article 13(b)(ii) and its *application*

³⁵⁹Brazil's appellee's submission, paras. 369 and 385 (quoting Panel Report, para. 7.481).

³⁶⁰*Ibid.*, para. 350.

³⁶¹*Ibid.*, paras. 344 ff.

³⁶²*Ibid.*, paras. 346 and 351.

³⁶³*Ibid.*, paras. 352 ff.

³⁶⁴*Ibid.*, paras. 442-445.

to four of the domestic support measures. These measures are production flexibility contract payments, market loss assistance payments, direct payments, and counter-cyclical payments.³⁶⁵ The question whether or not these four measures grant "support to a specific commodity" is at the heart of the difference between the participants in regard to the comparison contemplated by Article 13(b) of the *Agreement on Agriculture*.³⁶⁶ Secondly, the United States takes issue with the Panel's adoption of a budgetary outlay *methodology* to measure the value of two price-based support measures for the comparison under the proviso to Article 13(b)(ii).

(a) Interpretation of "Support to Specific Commodity"

359. We address first the meaning of the phrase "support to a specific commodity" in Article 13(b)(ii). We then discuss the application of this interpretation to four domestic support measures: production flexibility contract payments³⁶⁷, market loss assistance payments³⁶⁸, direct payments³⁶⁹ and counter-cyclical payments³⁷⁰. These four measures did not exist in 1992. Therefore, this part of the United States' appeal affects the calculation of *only* the support granted during the implementation period.³⁷¹

³⁶⁵The United States characterizes these measures as "decoupled" from production. (United States' appellant's submission, para. 104)

³⁶⁶On the basis that these four measures are not "support to a specific commodity", the United States has assigned zero values to them in its calculations under the proviso to Article 13(b)(ii). (*Ibid.*, para. 120)

³⁶⁷We describe briefly production flexibility contract payments *supra*, para. 311.

³⁶⁸Market loss assistance payments were provided to recipients of production flexibility contract payments through *ad hoc* legislation as additional assistance to producers to make up for losses caused by low commodity prices. Market loss assistance payments were proportionate to the production flexibility contract payments made to the recipient, and the amount paid depended on the amount allocated to market loss assistance payments for the relevant crop year. Accordingly, eligibility criteria for the market loss assistance payments were, essentially, the same as for the production flexibility contract payments. (See Panel Report, paras. 7.216-7.217)

³⁶⁹We describe briefly direct payments *supra*, para. 312.

³⁷⁰Counter-cyclical payments supplement, for covered commodities, direct payments and any payments made under the marketing loan program. The eligibility requirements and planting flexibility requirements are the same as under the direct payment program, and they are also dependent on base acres. Counter-cyclical payments supplement producer incomes by filling the gap between, on the one hand, the market price and payments under the marketing loan program and the direct payments program and, on the other hand, a target price established for upland cotton at 72.4 cents per pound. (See Panel Report, paras. 7.223-7.226)

³⁷¹We observe that the United States does not dispute that other payments, namely those under the marketing loan program (for a description of marketing loan program payments, see Panel Report, paras. 7.204-7.208), Step 2 payments (for a description of Step 2 payments, see Panel Report, paras. 7.209-7.211), deficiency payments (for a description of deficiency payments, see Panel Report, footnote 294 to para. 7.213), and cottonseed payments (for a description of cottonseed payments, see Panel Report, paras. 7.233-7.235), result in "support to a specific commodity". (United States' appellant's submission, para. 120 and Table 2) Nor does the United States appeal the Panel's finding that the crop insurance program (for a description of the crop insurance program, see Panel Report, paras. 7.227-7.232) results in "support to a specific commodity", although it adds that it disagrees with the conclusion of the Panel. (See United States' appellant's submission, footnote 134)

360. We note that payments in respect of each of these measures are calculated by reference to "base acres" upon which certain commodities (including upland cotton) were grown in a base period, but upon which a producer currently may or may not grow upland cotton. We refer to these four types of payment in this section as the "base acre dependent payments".

361. We turn to our analysis of the phrase "such measures ... grant[ing] support to a specific commodity" in Article 13(b)(ii). The Panel found and the participants do not dispute that the relevant United States measures grant "support"³⁷²; similarly, the Panel found³⁷³ and the participants agree³⁷⁴ that upland cotton is a "commodity" in the sense of that provision.

362. The key element, however, is the significance of the qualifying word "specific" in this phrase. The Panel described the ordinary meaning of the term "specific" as "clearly or explicitly defined; precise; exact; definite"³⁷⁵ and as "specially or peculiarly pertaining to a particular thing or person, or a class of these; peculiar (*to*)".³⁷⁶ In our view, the term "specific" in the phrase "support to a specific commodity" means the "commodity" must be clearly identifiable. The use of term "to" connecting "support" with "a specific commodity" means that support must "specially pertain" to a particular commodity in the sense of being conferred on that commodity. In addition, the terms "such measures ... grant" indicates that a discernible link must exist between "such measures" and the particular commodity to which support is granted. Thus, it is not sufficient that a commodity happens to benefit from support, or that support ends up flowing to that commodity by mere coincidence. Rather, the phrase "such measures" granting "support to a specific commodity" implies a discernible link between the support-conferring measure and the particular commodity to which support is granted.

363. Therefore, we agree with the Panel insofar as it found that the ordinary meaning of the phrase "such measures ... grant[ing] support to a specific commodity" includes "non-green box measures

³⁷²See Panel Report, paras. 7.518-7.520 and, for example, United States' appellant's submission, para. 105. We recognize that the United States qualifies this by emphasizing that, in its view, they grant "non-product-specific" support.

³⁷³Panel Report, paras. 7.480 and 7.518-7.520.

³⁷⁴See United States' appellant's submission, paras. 85 and 104; and Brazil's appellee's submission, para. 385.

³⁷⁵Panel Report, para. 7.481 (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 2, p. 2972).

³⁷⁶*Ibid.*, para. 7.482 (quoting *The New Shorter Oxford English Dictionary*, L. Brown (ed.) (Clarendon Press, 1993), Vol. 2, p. 2972). The Panel found that this second definition was more appropriate in another context, but we believe that both of these definitions shed light upon the meaning of "specific" in "support to a specific commodity".

that clearly or explicitly define a commodity as one to which they bestow or confer support".³⁷⁷ This is because the Panel's test requires that a commodity be specified in the measure, and that the support be conferred on that commodity. We believe, however, that the terms of this definition do not exhaust the scope of measures that may grant "support to a specific commodity". We note in this regard that the Panel looked, in applying its test, to factors such as eligibility criteria and payment rates, as well as the relationship between payments and current market prices of the commodity in question.³⁷⁸ In our view, the Panel was correct to consider such matters, as the requisite link between a measure granting support and a specific commodity may be discerned not just from an explicit specification of the commodity in the text of a measure, as the Panel's test—on its face—seems to imply, but also from an analysis of factors such as the characteristics, structure or design of that measure.³⁷⁹

364. Moving to the context of the proviso to Article 13(b)(ii), we note that the United States argues that "support to a specific commodity" should be interpreted as meaning "product-specific support". The United States emphasizes the similarities between the phrase "support to a specific commodity" in Article 13(b)(ii) and two phrases in Article 1 of the *Agreement on Agriculture* that refer to product-specific support: "support for basic agricultural products"³⁸⁰ and "support ... provided for an agricultural product in favour of the producers of the basic agricultural product".³⁸¹ The United States argues that the meaning of all of these phrases must be the same.

365. These phrases do provide important context for the interpretation of Article 13(b)(ii). In our view, "support to a specific commodity" certainly includes "product-specific" support. However, like the Panel, we do not believe that the scope of the phrase "support to a specific commodity" in the proviso to Article 13(b)(ii) is exhausted by taking into account the category of product-specific support alone.

366. This is for at least two reasons. First, we note that the drafters chose *not* to use phrases such as support "provided for an agricultural product in favour of the producers of the basic agricultural product" or "support for basic agricultural products" in Article 13(b)(ii), but rather chose the distinct

³⁷⁷Panel Report, para. 7.494(i).

³⁷⁸*Ibid.*, paras. 7.510-7.517.

³⁷⁹Although we observe that the Panel correctly identified the elements that we believe are inherent in the term "support to a specific commodity", the Panel's articulation of the test was not absolutely clear. We also note that the Panel appears to have misapplied the test for "support to a specific commodity" by attributing to upland cotton the total budgetary outlays with respect to upland cotton base acres. See *infra*, para. 375.

³⁸⁰This phrase is found in Article 1(h) of the *Agreement on Agriculture*. (United States' appellant's submission, para. 88)

³⁸¹This phrase is found in Article 1(a) of the *Agreement on Agriculture*. (United States' appellant's submission, para. 88)

phrase "support to a specific commodity". This choice of different words by the drafters gives a preliminary indication that they may have intended to convey different meanings.³⁸²

367. Secondly, and more importantly, the United States' argument fails to reckon with the fact that the scope of domestic support measures that may grant "support to a specific commodity" under Article 13(b)(ii) is broader than just "product-specific support" in the sense of Article 1 and Annex 3. The proviso to Article 13(b)(ii) mentions only the term "such measures" granting support; but the meaning of this term can be clarified by reference to the chapeau of Article 13(b) because, as the Panel noted, "[t]he chapeau of paragraph (b) and subparagraph (ii) form part of a single sentence."³⁸³ The chapeau identifies the categories of support measures covered by that provision. These are:

... domestic support measures that conform fully to the provisions of Article 6 of this Agreement including direct payments that conform to the requirements of paragraph 5 thereof, as reflected in each Member's Schedule, as well as domestic support within *de minimis* levels and in conformity with paragraph 2 of Article 6 ...

368. Measures covered by Article 6 include both product-specific and non-product-specific amber box support subject to reduction commitments. In addition, measures covered by the chapeau *also* include product-specific and non-product-specific support within *de minimis* levels. They further include blue box support provided in accordance with Article 6.5, as well as development box support, provided according to the provisions of Article 6.2, for both of which the distinction between product-specific and non-product specific support for purposes of the AMS calculation has little practical relevance.³⁸⁴ Like the Panel, we believe that the use of the term "such measures" in the proviso to Article 13(b)(ii) indicates that all such measures identified in the chapeau of Article 13(b) may qualify as granting "support to a specific commodity" and are eligible to be included in the analysis. By contrast, under the United States' argument, domestic support measures listed in the chapeau (with the exception of product-specific amber box support) could not be "support to a specific commodity" even if they confer support on a specific commodity and there is a discernible link between the measure and that commodity.

³⁸²We note in this regard that, for example, Article 6.4(a)(i) of the *Agreement on Agriculture* mentions "product-specific domestic support", whereas Article 13 does not mention or cross-refer to it.

³⁸³Panel Report, para. 7.470.

³⁸⁴The only type of domestic support clearly excluded from support covered by Article 13(b) is green box support, which does not need to conform with the provisions of Article 6, but rather must conform with the provisions of Annex 2. Green box support, however, qualifies for the exemption from actions provided by Article 13(a).

369. In addition, the United States supports its position by reference to the obligations in Articles 3 and 6 of the *Agreement on Agriculture*, which lay down reduction commitments for total AMS comprising both product-specific and non-product-specific support, but provide no product-specific caps. In the United States' view, because the reduction commitments do not cap product-specific support, the proviso in Article 13(b)(ii) disciplines the degree to which a Member that is in conformity with its reduction commitments can shift support between particular commodities.³⁸⁵

370. Indeed, as the United States correctly points out, Article 13(b)(ii) serves to create a discipline upon Members that seek the shelter of the peace clause during the implementation period. We are not convinced, however, that this discipline is limited to "product-specific support" as defined in Article 1 of the *Agreement on Agriculture*. Rather, it extends to all measures that grant "support to a specific commodity", in the sense that the support is conferred on a specific commodity, and there is a discernible link between the measure and the specific commodity concerned.

(b) Application of Article 13(b)(ii) to the Measures at Issue

371. The proviso to Article 13(b)(ii) requires an assessment of whether the relevant United States non-green box domestic support measures grant, during the implementation period, "support to a specific commodity in excess of that decided during the 1992 marketing year".

372. As we have explained above, the term "such measures ... grant support to a specific commodity" comprises two elements: first, a non-green box measure actually confers support on the specific commodity in question; and second, there is a discernible link between the measure and the commodity, such that the measure is directed at supporting that commodity. Such a discernible link may be evident where a measure explicitly defines a specific commodity as one to which it bestows support. Such a link might also be ascertained, as a matter of fact, from the characteristics, structure or design of the measure under examination. Conversely, support that does not actually flow to a commodity or support that flows to a commodity by coincidence rather than by the inherent design of the measure cannot be regarded as falling within the ambit of the term "support to a specific commodity".

373. With these considerations in mind, we turn now to the application of this interpretation to four measures that the United States claims do not grant "support to a specific commodity": the *production flexibility contract payments*, *market loss assistance payments*, *direct payments* and *counter-cyclical payments*. We refer to these measures as "base acre dependent payments" because each of these measures provides payments based on a calculation in which a payment rate, specific to

³⁸⁵United States' appellant's submission, para. 98.

upland cotton, is multiplied by an ascertained quantity of upland cotton, which, in turn, is a product of a farm's historical planting of upland cotton (its "upland cotton base acres") and its historical yield of upland cotton per acre.³⁸⁶ For purposes of the Article 13(b)(ii) comparison, the Panel outlined three alternative methodologies, and therefore three different calculations, in respect of these measures in its Article 13(b)(ii) analysis.³⁸⁷ We also note that in calculating support granted to upland cotton the United States has ascribed a zero value to the four aforementioned domestic support measures. For purposes of these proceedings, we do not find it necessary to go beyond the Panel record, and thus limit our consideration to these four alternative calculations.

374. The Panel ultimately based its calculations in respect of the base acre dependent payments on the *total* budgetary outlays with respect to upland cotton base acres under each program.³⁸⁸ The United States contends that this calculation methodology led the Panel to include, as support to upland cotton, payments to producers who did not plant upland cotton.³⁸⁹ For the United States, there is "[no] question that payments cannot be deemed to grant support to a crop the recipient does not produce".³⁹⁰ In addition, the United States contends that the Panel erred in finding that the base acre dependent programs "clearly and explicitly specify] upland cotton ... as a commodity to which they grant support".³⁹¹ In the view of the United States, these measures do no such thing. The United States emphasizes that producers receive payments under the base acre dependent programs irrespective of whether and how much upland cotton they plant, and regardless of whether they plant anything at all.³⁹² For the United States, the "Panel's error stems largely from its assertion that merely identifying *historical* criteria relating to a commodity according to which payments will be made would render such payments 'support to a specific commodity'".³⁹³

³⁸⁶We note that each of these programs applied not just to upland cotton, but also to other eligible commodities. We also note that market loss assistance payments did not involve a separate calculation involving these criteria. Rather, market loss assistance payments served to supplement production flexibility contract payments and were made proportionate to a producer's production flexibility contract payments. (Panel Report, para. 7.217)

³⁸⁷See Panel Report, para. 7.596 and "Attachment to Section VII:D" (Panel Report, paras. 7.634-7.647).

³⁸⁸*Ibid.*, paras. 7.580-7.583.

³⁸⁹United States' appellant's submission, para. 106.

³⁹⁰*Ibid.*

³⁹¹*Ibid.*, para. 103 (quoting Panel Report, para. 7.518).

³⁹²United States' appellant's submission, para. 104.

³⁹³*Ibid.*, para. 105. (original emphasis) The United States points out that "base acres" are not "physical acres" but hypothetical acres for calculation of decoupled payments to producers, who are free to produce whatever crop they choose or to produce no crop at all. (United States' responses to questions during the oral hearing)

375. We agree with the United States that payments made with respect to historical upland cotton base acres to commodities other than upland cotton or to producers who produced no commodities at all cannot be deemed to be support granted to upland cotton for purposes of the Article 13(b)(ii) comparison. The Article 13(b)(ii) assessment must be limited to support conferred on planted upland cotton; support flowing to other commodities that were planted, or support that was given where no commodities were produced must of course be removed from the assessment. We reject, therefore, the Panel's calculation methodology to the extent that it failed to limit the Article 13(b)(ii) calculation to payments with respect to upland cotton base acres corresponding to physical acres actually planted with upland cotton.

376. We observe, however, that the Panel acknowledged that a producer with upland cotton base acres may plant any crop other than the excluded fruits, vegetables, and wild rice, but it found that there was "a strongly positive relationship between those recipients who hold upland cotton base acres and those who continue to plant upland cotton, despite their entitlement to plant other crops".³⁹⁴ The Panel further observed that data provided by the United States showed that "a very large proportion of farms with upland cotton base acres continue to plant upland cotton in the year of payment"³⁹⁵, and that "the overwhelming majority of farms enrolled in the programmes which plant upland cotton also hold upland cotton base".³⁹⁶

377. We note in this regard that the Panel included, in "Attachment to Section VII:D" to its Report, and described as "appropriate"³⁹⁷, an alternative calculation using certain methodologies submitted by Brazil for allocating support to acres actually planted with upland cotton under the base acre dependent programs. The first part of this calculation, the "cotton to cotton" methodology, allocated, for each *planted* acre of upland cotton, payments associated with one upland cotton base acre. The second part ("Brazil's methodology") took the results of the "cotton to cotton" methodology and then added to it payments made with respect to non-upland cotton base acres corresponding to physical acres that were actually planted with upland cotton.³⁹⁸ The "cotton to cotton" methodology limits the Article 13(b)(ii) calculation to payments with respect to cotton base acres corresponding to physical acres that were actually planted with upland cotton.

378. We turn next to the United States' contention that the mere fact that a measure is based on *historical* production of upland cotton is not a sufficient basis for a finding that the measure grants at

³⁹⁴Panel Report, para. 7.637.

³⁹⁵*Ibid.*, para. 7.636. (footnote omitted)

³⁹⁶*Ibid.*, para. 7.636.

³⁹⁷*Ibid.*, para. 7.646.

³⁹⁸See *ibid.*, paras. 7.640-7.642.

present "support to [the] specific commodity" upland cotton. We agree that none of the base acre dependent programs expressly ties support to continued production of upland cotton. However, the absence of an express reference in the legislation to continued production of upland cotton does not mean that the payments do not grant support to upland cotton. This is because a link between the four measures at issue and the continued production of upland cotton is discernible from the characteristics, structure and operation of those measures.

379. We note in this regard the reasoning of the Panel:

Where, for example, these measures specify commodities in the eligibility criteria and payment rates, they constitute support to the commodities specified in that way. This applies *a fortiori* where the payments are determined according to, or are related to, current market prices of the specific commodities.³⁹⁹

On this basis, the Panel highlighted several factors revealing a close nexus between payments with respect to historic upland cotton base acres under the production flexibility contract, market loss assistance, direct payment and counter-cyclical payment measures, and the continued production of upland cotton on an equivalent number of physical acres at present. The Panel noted that payments under each program were based on "very specific eligibility criteria", primarily the production of upland cotton in a historical base period.⁴⁰⁰ The Panel also observed that, in the case of each of the measures, a particular payment rate was specified for upland cotton.⁴⁰¹ Yield calculations were also specific to upland cotton and related to historical upland cotton yields per acre.⁴⁰² In the case of market loss assistance payments, payments were specifically designed to compensate for low prices for upland cotton.⁴⁰³ In the case of counter-cyclical payments, the payment rate for upland cotton is directly linked to the market price of upland cotton in the year of payment.⁴⁰⁴ In our view, these characteristics and operational factors of the measures in question demonstrate a link between payments made with respect to historic upland cotton base acres and the continued production of upland cotton.

380. We underline that these Panel findings do not pertain to *all* payments to *current* producers of upland cotton, but rather are limited to payments to producers with respect to historic *upland*

³⁹⁹Panel Report, para. 7.484.

⁴⁰⁰*Ibid.*, paras. 7.513-7.516.

⁴⁰¹*Ibid.*, para. 7.635.

⁴⁰²See *ibid.*, paras. 7.513-7.516.

⁴⁰³*Ibid.*, para. 7.515.

⁴⁰⁴*Ibid.*, para. 7.516.

cotton base acres.⁴⁰⁵ Indeed, we see little in the Panel's finding or on the record that would allow us to discern a link between the support-conferring measures with respect to non-cotton historical base acres and current production of upland cotton. We do not, therefore, accept the methodology submitted by Brazil that included, in the Article 13(b)(ii) calculation, payments with respect to both cotton and non-cotton base acres flowing to current production of upland cotton. We believe that only the "cotton to cotton" methodology, included by the Panel in "Attachment to Section VII:D" to its Report as an "appropriate"⁴⁰⁶ alternative calculation, sufficiently demonstrates a discernible link between payments under base acre dependent measures (related to upland cotton) and upland cotton.

381. Finally, we address the United States' argument that the calculation methodology under Article 13(b)(ii) must be based on only those factors that the government of a Member can control, excluding, for example, producer decisions regarding what crops to grow within the scope of production flexibility allowed by the measures.⁴⁰⁷ In advancing this contention, the United States relies upon the following statement of the Panel:

[I]f the proviso [to Article 13(b)(ii)] focused on where support was spent due to reasons beyond the control of the government, such as producer decisions on what to produce within a programme, it would introduce a major element of unpredictability into Article 13, and render it extremely difficult to ensure compliance.⁴⁰⁸

382. The United States finds support for this view in the terms "grant" and "decided" in Article 13(b)(ii), and claims that "the focus of the Peace Clause comparison is on the support a Member decides".⁴⁰⁹ We note that the verbs "grant" and "decided" have distinct meanings. We agree with the observation of the Panel that "[d]ecided" refers to what the government determines, but 'grant' refers to what its measures provide.⁴¹⁰ In Article 13(b)(ii), each of these words has been chosen to govern one side of the comparison required by that proviso. In the light of the distinct meanings of these words, and the distinct roles they play in the context of Article 13(b)(ii), we reject the idea that the word "grant", which is applicable to implementation period support, must be read to mean the same thing as "decided", which is applicable to the 1992 benchmark level of support.

383. Moreover, we do not accept that unpredictability of producer decisions under planting flexibility rules, *per se*, could modify the specific requirements set out in the proviso to

⁴⁰⁵See *supra*, footnote 184.

⁴⁰⁶Panel Report, para. 7.646.

⁴⁰⁷United States appellant's submission, paras. 64-67 and 114-117.

⁴⁰⁸Panel Report, para. 7.487.

⁴⁰⁹United States appellant's submission, para. 66.

⁴¹⁰Panel Report, para. 7.476.

Article 13(b)(i). What is relevant for the comparison is the support that the measure actually grants during the implementation period. Indeed, we agree with Brazil that a certain degree of unpredictability in the volume of the payments flowing to particular commodities is inherent in many of the support measures disciplined by the *Agreement on Agriculture*, including measures granting support to a specific commodity.⁴¹¹ The existence of such unpredictability cannot be a ground to alter the basis of comparison under the proviso to Article 13(b)(ii) from what is actually "grant[ed]" in the implementation period to what is only "decided".

384. For the reasons stated above, we conclude that payments with respect to upland cotton base acres to producers currently growing upland cotton under the production flexibility contract, market loss assistance, direct payment and counter-cyclical payment measures, calculated in accordance with the "cotton to cotton" methodology, are support granted to the specific commodity upland cotton in the sense of Article 13(b)(ii) of the *Agreement on Agriculture*.⁴¹²

(c) Methodology for Calculating the Value of Price-Based Payments

385. The United States' appeal regarding the Panel's decision to use the budgetary outlay methodology and not the price gap methodology described in paragraph 10 of Annex 3 to the *Agreement on Agriculture* for certain price-based payments concerns calculation of the amounts of two types of payments: (i) payments under the *marketing loan program*, which are relevant to the calculation of both the 1992 benchmark level of support and support during the implementation period; and (ii) *deficiency payments*, made in accordance with the FACT Act of 1990, which were replaced by production flexibility contract payments under the FAIR Act of 1996, and which are therefore relevant only to the calculation of the 1992 benchmark level of support.⁴¹³

⁴¹¹Thus, in the case of measures that compensate for price fluctuations, unless a limit is set on total payments, a government has little control over the eventual amount of payments. In addition, we recall that the export subsidies at issue in *US – FSC* took the form of a foregoing of tax revenue, with the precise amount of the revenue foregone, and the nature of the specific products that it went to support, being dependent upon the actions of private corporations claiming the exemption. In that case, therefore, it could also be said that whether the United States would exceed product-specific export subsidy commitments would also depend on private producers' decisions to claim tax exemptions.

⁴¹²For the Panel's findings on the value of production flexibility contract payments, market loss assistance payments, direct payments and counter-cyclical payments using the "cotton to cotton" methodology see Panel Report, para. 7.641.

⁴¹³United States' appellant's submission, para. 72; Panel Report, para. 7.213. We observe that the United States' arguments relating to the use of the price gap methodology to measure marketing loan program payments and deficiency payments extend only to the analysis required under Article 13(b)(ii) of the *Agreement on Agriculture*; the United States does not argue that a price gap calculation is required in the context of an analysis of significant price suppression under Article 6.3(c) of the *SCM Agreement*.

386. Payments to upland cotton under the marketing loan program could take one of several forms. In each case, however, gains to producers under this program accrued on the basis of a gap between a reference price tied to the market price of upland cotton, known as the "adjusted world price", and the "loan rate" fixed, from time to time, for the marketing loan program.⁴¹⁴ Deficiency payments for upland cotton were based on the gap between either the loan rate under the marketing loan program, or the national average market price for upland cotton (whichever was higher) and a target price of 72.9 cents per pound of upland cotton. In the event that the loan rate or market price fell below the target price, deficiency payments filled the deficit.⁴¹⁵

387. The United States claims that both of these price-based measures represent "non-exempt direct payments ... dependent on a price gap", the value of which should be calculated by reference to the price gap methodology described in paragraph 10 of Annex 3 to the *Agreement on Agriculture*.⁴¹⁶

388. In addressing this issue, we—like the Panel—note that Article 13(b)(ii) gives no specific guidance regarding *how* the "support" that measures granted in the implementation period or that was decided during the 1992 marketing year should be calculated. The Panel therefore turned to the broader context of the *Agreement on Agriculture* and chose to "apply the principles of AMS methodology" in accordance with Annex 3 of the *Agreement on Agriculture*, with certain modifications.⁴¹⁷ We observe that, on appeal, neither of the participants, nor indeed any of the third participants that addressed this issue, suggested that the Panel erred in seeking guidance for its calculations in the principles set out in Annex 3.

389. Against this background, we observe that paragraph 10 of Annex 3 provides that "non-exempt direct payments ... dependent on a price gap" may be measured using either price gap methodology or budgetary outlay methodology.⁴¹⁸ The Panel chose to rely upon actual budgetary outlays⁴¹⁹, but

⁴¹⁴For a description of payments under the marketing loan program, see Panel Report, paras. 7.204-7.208.

⁴¹⁵For a description of deficiency payments, see Panel Report, footnote 294 to para. 7.213.

⁴¹⁶United States' appellant's submission, paras. 71-73 (quoting paragraph 10 of Annex 3 to the *Agreement on Agriculture*).

⁴¹⁷Panel Report, para. 7.552.

⁴¹⁸Paragraph 10 of Annex 3 to the *Agreement on Agriculture* sets forth:

Non-exempt direct payments: non-exempt direct payments which are dependent on a price gap shall be calculated either using the gap between the fixed reference price and the applied administered price multiplied by the quantity of production eligible to receive the administered price, or using budgetary outlays.

⁴¹⁹See, for example, Panel Report, para. 7.596. We reproduce the Panel's findings with respect to the values attributable to deficiency payments and payments under the marketing loan program using budgetary outlays in Table 1 of Annex 2.

included in its Report findings regarding the value of support in each relevant year calculated according to price gap methodology as well.⁴²⁰

390. As we explain in the next section, our conclusion that the United States granted, during the relevant years of the implementation period, "support to a specific commodity", namely, upland cotton, "in excess of that decided during the 1992 marketing year" holds irrespective of whether the Panel's budgetary outlay calculations or its price gap calculations are used to attribute values to marketing loan program payments and deficiency payments. Therefore, it is unnecessary for us to decide here which methodology must be used for purposes of the comparison envisaged by Article 13(b)(ii) with respect to these two types of payment.⁴²¹

(d) Conclusion Regarding the Application of Article 13(b)(ii)

391. We recall, once again, that the proviso to Article 13(b)(ii) of the *Agreement on Agriculture* sets forth that, during the implementation period in which Article 13 applies, non-green box domestic support measures must not "grant support to a specific commodity in excess of that decided during the 1992 marketing year", if such measures are to enjoy exemption from actions "based on paragraph 1 of Article XVI of GATT 1994 or Articles 5 and 6 of the Subsidies Agreement".⁴²²

392. In our review above, we have concluded that, for purposes of the comparison envisaged by Article 13(b)(ii), the values of the four measures, namely, production flexibility contract payments, market loss assistance payments, direct payments and counter-cyclical payments in the years 1999, 2000, 2001, and 2002 are properly determined by using the "cotton to cotton" methodology, and we have therefore modified the Panel's findings in this regard. We further note that the United States has

⁴²⁰See Panel Report, para. 7.564 and footnote 727 to para. 7.565. We reproduce the Panel's findings with respect to the values attributable to deficiency payments and payments under the marketing loan program using price gap methodology in each relevant year in Table 2 of Annex 2.

⁴²¹At the oral hearing, the United States confirmed that it may become unnecessary to rule on its appeal regarding calculation methodology, should the Panel's conclusions with respect to the phrase "support to a specific commodity" in Article 13(b)(ii) be upheld by the Appellate Body. (United States' response to questioning at the oral hearing)

⁴²²We note at this point that we agree with the Panel that:

There is no requirement to quantify the excess, but the decisive question is whether there is any excess. Thus, it would not be strictly necessary ... to make a precise calculation of the amount of the excess if it is clear that, on the basis of the proper evidentiary standard, there is an excess of some degree.

(Panel Report, para. 7.419)

We also note, however, that fairly detailed calculations regarding the values attributable to United States implementation period support is available to us in these proceedings.

not appealed the Panel's findings regarding the values attributable to three further support measures, namely, Step 2 payments to domestic users, crop insurance and cottonseed payments.⁴²³

393. Adding, to the values of the seven measures mentioned above, the values for deficiency payments and marketing loan program payments calculated using *either* budgetary outlays⁴²⁴ or price gap methodology⁴²⁵, we conclude that the United States' domestic support measures in question granted "support to a specific commodity", namely, upland cotton, that was "in excess of that decided during the 1992 marketing year" in each relevant year of the implementation period.

394. It follows that the condition set out in the proviso to Article 13(b)(ii) of the *Agreement on Agriculture* has not been met by the United States. We uphold, therefore, the Panel finding, in paragraph 7.608 of its Report, that the United States' domestic support measures challenged by Brazil are not entitled to the exemption provided by the peace clause from actions under Article XVI:1 of the GATT 1994 and Articles 5 and 6 of the *SCM Agreement*.

VI. Serious Prejudice

A. Significant Price Suppression under Article 6.3(c) of the *SCM Agreement*

1. Introduction

395. The United States appeals the Panel's finding, in paragraphs 7.1416 and 8.1(g)(i) of the Panel Report, that the effect of marketing loan program payments, Step 2 payments, market loss assistance payments, and counter-cyclical payments (the "price-contingent subsidies") is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*. The United States raises several objections to the Panel's analysis leading to this finding. The United States also asks us to find that the Panel failed to set out the findings of fact, the applicability of relevant provisions, and the basic rationale behind this finding, as required by Article 12.7 of the DSU. Brazil, for its part, raises a preliminary issue under Article 11 of the DSU.

396. In this section of this Report, we begin our analysis by addressing the preliminary argument of Brazil regarding Article 11 of the DSU. We then turn to the various errors that the United States alleges that the Panel made in making its finding of significant price suppression under Article 6.3(c) of the *SCM Agreement*. In doing so, we examine the United States' objections to the "market" and

⁴²³For Panel findings on the value of support under these programs, see Panel Report, para. 7.596. See also Tables 1 and 2 of Annex 2.

⁴²⁴See Table 1 of Annex 2.

⁴²⁵See Table 2 of Annex 2.

"price" that the Panel examined in its analysis of the price-contingent subsidies pursuant to Article 6.3(c). We then consider the Panel's order of analysis under Article 6.3(c). Next, we assess the other alleged errors in the Panel's reasoning leading to its finding that the effect of the price-contingent subsidies is significant price suppression. These include the Panel's alleged failure to quantify the amount of the price-contingent subsidies benefiting upland cotton or to allocate the effect of the subsidies to the appropriate period of time. We then consider the implications of this appeal for the Panel's finding regarding serious prejudice under Article 5(c) of the *SCM Agreement*. Finally, we address the United States' claim that the Panel failed to comply with the requirements of Article 12.7 of the DSU.

2. Objective Assessment under Article 11 of the DSU

397. Brazil argues that many of the United States' arguments, particularly those concerning serious prejudice, involve allegations that the Panel failed to "make an objective assessment of the matter before it, including an objective assessment of the facts of the case" pursuant to Article 11 of the DSU.⁴²⁶ Brazil requests us to dismiss the United States' arguments that Brazil lists in Annex A to its appellee's submission, on the basis that the United States has not made a proper claim of error under Article 11 of the DSU.⁴²⁷

398. In its opening statement delivered at the oral hearing, the United States confirmed that it has not made an Article 11 claim in this appeal. Rather, the United States claims that the Panel erred in its interpretation of Article 6.3(c) of the *SCM Agreement* and in applying this interpretation to the facts in this dispute. The United States also requests us not to dismiss certain of its arguments as requested by Brazil. Under these circumstances, there is no need for us to rule that the United States makes no Article 11 claim. We also refrain from ruling on whether the Panel complied with Article 11 of the DSU. Moreover, we decline to dismiss the United States' arguments that Brazil lists in Annex A to its appellee's submission on the basis that an Article 11 claim was not properly set out by the United States.

399. We are nevertheless mindful of the scope of appellate review with respect to legal and factual matters. Pursuant to Article 17.6 of the DSU, appeals are "limited to issues of law covered in the panel report and legal interpretations developed by the panel". To the extent that the United States' arguments concern the Panel's appreciation and weighing of the evidence, we note from the outset that

⁴²⁶Brazil's appellee's submission, paras. 105 and 146.

⁴²⁷*Ibid.*, para. 146.

the Appellate Body will not interfere lightly with the Panel's discretion "as the trier of facts".⁴²⁸ At the same time, the Appellate Body has previously pointed out that the "consistency or inconsistency of a given fact or set of facts with the requirements of a given treaty provision is ... a legal characterization issue".⁴²⁹ Whether the Panel properly interpreted the requirements of Article 6.3(c) of the *SCM Agreement* and properly applied that interpretation to the facts in this case is a legal question. This question is different from whether the Panel made "an objective assessment of the matter before it, including an objective assessment of the facts of the case", in accordance with Article 11 of the DSU.⁴³⁰ Therefore, the Panel's application of the legal requirements of Article 6.3(c) of the *SCM Agreement* to the facts of this case falls within the scope of our review in this appeal, despite the fact that the United States does not claim that the Panel erred under Article 11 of the DSU.

3. Relevant Market under Article 6.3(c) of the SCM Agreement

400. Turning to the question of the relevant "market", we observe that Article 6.3(c) of the *SCM Agreement* addresses the situation where "the effect of the subsidy is ... significant price suppression ... in the same market". (emphasis added) As the Panel suggested⁴³¹, and the parties agree⁴³², it is up to the complaining Member to identify the market in which it alleges that the effect of a subsidy is significant price suppression and to demonstrate that the subsidy has that effect within the meaning of Article 6.3(c). Before the Panel, Brazil identified the following as relevant markets for its claim under Article 6.3(c): (a) the world market for upland cotton; (b) the Brazilian market; (c) the United States market; and (d) 40 third country markets where Brazil exports its cotton and where United States and Brazilian upland cotton are found.⁴³³ In contrast, the United States argued before the Panel that the relevant market under Article 6.3(c) must be "a particular domestic market of a Member", and that it cannot be a "world market".⁴³⁴

⁴²⁸Determination of the credibility and weight properly to be ascribed to (that is, the appreciation of) a given piece of evidence is part and parcel of the fact finding process and is, in principle, left to the discretion of a panel as the trier of facts." (Appellate Body Report, *EC – Hormones*, para. 132) See also Appellate Body Report, *US – Wheat Gluten*, para. 151; Appellate Body Report, *EC – Sardines*, para. 299; Appellate Body Report, *US – Carbon Steel*, para. 142; Appellate Body Report, *Japan – Apples*, para. 221.

⁴²⁹Appellate Body Report, *EC – Hormones*, para. 132.

⁴³⁰On this question, the Appellate Body has made several pronouncements in previous appeals. See, for example, Appellate Body Report, *EC – Hormones*, para. 133; Appellate Body Report, *Korea – Dairy*, para. 137; Appellate Body Report, *Japan – Apples*, para. 222.

⁴³¹Panel Report, para. 7.1246.

⁴³²The United States and Brazil indicated their agreement on this point in response to questioning during the oral hearing.

⁴³³Panel Report, para. 7.1230.

⁴³⁴*Ibid.*, para. 7.1231.

401. The Panel regarded the absence of any geographic limitation or reference to imports or exports in the text of Article 6.3(c), in contrast to Articles 6.3(a) and (b) and 15.2 of the *SCM Agreement*, as indicating that the "same market" under Article 6.3(c) could be a "world market".⁴³⁵ Applying this interpretation to the facts of the present dispute, the Panel concluded that a "world market" for upland cotton does exist.⁴³⁶ The Panel further stated that "[w]here price suppression is demonstrated in [the world] market, it may not be necessary to proceed to an examination of each and every other possible market where the products of both the complaining and defending Members are found".⁴³⁷ In the present dispute, having found that "price suppression has occurred in the same world market"⁴³⁸, the Panel decided that it was not "necessary to proceed to any further examination of ... alleged price suppression in individual country markets".⁴³⁹ Thus, the Panel's analysis of the world market for upland cotton formed the basis for its finding that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c).

402. On appeal, the United States submits that the Panel erred in interpreting the words "same market" in Article 6.3(c) of the *SCM Agreement* as including a "world market".⁴⁴⁰ It also submits that the Panel's finding that a "world market" exists for upland cotton is inconsistent with certain of its other findings.⁴⁴¹ The United States also argues that, in any case, the Panel did not make a finding that United States and Brazilian upland cotton compete in the world market that it had identified for upland cotton.⁴⁴² Brazil contends that significant price suppression under Article 6.3(c) "may apply to any 'market,' from local to global, and everything in between".⁴⁴³

403. We begin our analysis of this issue by identifying the ordinary meaning of the word "market" in the context of Article 6.3(c). Article 6.3(c) of the *SCM Agreement* indicates that:

Serious prejudice in the sense of paragraph (c) of Article 5 may arise in any case where one or several of the following apply:

...

⁴³⁵Panel Report, paras. 7.1238-7.1240.

⁴³⁶*Ibid.*, para. 7.1247.

⁴³⁷*Ibid.*, para. 7.1252.

⁴³⁸*Ibid.*, para. 7.1312.

⁴³⁹*Ibid.*, para. 7.1315.

⁴⁴⁰United States' appellant's submission, para. 307.

⁴⁴¹*Ibid.*, paras. 318 and 319. The United States submits that the Panel failed to reconcile its interpretation of the "same market" in Article 6.3(c) with its reading of the phrase "world market" under Article 6.3(d).

⁴⁴²United States' appellant's submission, para. 321.

⁴⁴³Brazil's appellee's submission, para. 628. (original emphasis)

(c) the effect of the subsidy is a significant price undercutting by the subsidized product as compared with the price of a like product of another Member in the same market or significant price suppression, price depression or lost sales in the same market[.] (emphasis added)

404. The Panel described the ordinary meaning of the word "market" as:⁴⁴⁴

"a place ... with a demand for a commodity or service"¹³⁵⁵; "a geographical area of demand for commodities or services"; "the area of economic activity in which buyers and sellers come together and the forces of supply and demand affect prices".¹³⁵⁶

¹³⁵⁵ *The New Shorter Oxford English Dictionary*, (1993).

¹³⁵⁶ *Merriam-Webster Dictionary online*.

405. We accept that this is an adequate description of the ordinary meaning of the word "market" for the purposes of this dispute, and we do not understand the parties to dispute it.⁴⁴⁵ This ordinary meaning does not, of itself, impose any limitation on the "geographical area" that makes up any given market. Nor does it indicate that a "world market" cannot exist for a given product. As the Panel indicated, the "degree to which a market is limited by geography will depend on the product itself and its ability to be traded across distances".⁴⁴⁶

406. The only express qualification on the type of "market" referred to in Article 6.3(c) is that it must be "the same" market. Aside from this qualification (to which we return below), Article 6.3(c) imposes no explicit geographical limitation on the scope of the relevant market. This contrasts with the other paragraphs of Article 6.3: paragraph (a) restricts the relevant market to "the market of the subsidizing Member"; paragraph (b) restricts the relevant market to "a third country market"; and paragraph (d) refers specifically to the "world market share". We agree with the Panel⁴⁴⁷ that this difference may indicate that the drafters did not intend to confine, *a priori*, the market examined under Article 6.3(c) to any particular area. Thus, the ordinary meaning of the word "market" in Article 6.3(c), when read in the context of the other paragraphs of Article 6.3, neither requires nor excludes the possibility of a national market or a world market.⁴⁴⁸

⁴⁴⁴Panel Report, para. 7.1236.

⁴⁴⁵As indicated by the United States and Brazil in response to questioning during the oral hearing.

⁴⁴⁶Panel Report, para. 7.1237.

⁴⁴⁷*Ibid.*, paras. 7.1238-7.1240.

⁴⁴⁸This stands to reason, given that the purpose of the "actionable subsidies" provisions in Part III of the *SCM Agreement* is to prevent Members from causing adverse effects to the interests of other Members through the use of specific subsidies, wherever such effects may occur.

407. Turning to the phrase "in the same market", it is clear to us from a plain reading of Article 6.3(c) that this phrase applies to all four situations covered in that provision, namely, "significant price undercutting", "significant price suppression, price depression [and] lost sales". We read the Panel Report and the participants' submissions as endorsing this interpretation.⁴⁴⁹ The phrase "in the same market" suggests that the subsidized product in question (United States upland cotton in this case)⁴⁵⁰ and the relevant product of the complaining Member must be "in the same market". In this appeal, the Panel and the participants agree that United States upland cotton⁴⁵¹ and Brazilian upland cotton⁴⁵² must be "in the same market" for Brazil's claim under Article 6.3(c) to succeed.⁴⁵³ Furthermore, the participants agree that these are like products.⁴⁵⁴

408. When can two products be considered to be "in the same market" for the purposes of a claim of significant price suppression under Article 6.3(c)? Article 6.3(c) does not provide an explicit answer. However, recalling that one accepted definition of "market" is "the area of economic activity in which buyers and sellers come together and the forces of supply and demand affect prices"⁴⁵⁵, it seems reasonable to conclude that two products would be in the same market if they were engaged in actual or potential competition in that market. Thus, two products may be "in the same market" even if they are not necessarily sold at the same time and in the same place or country. As the Panel correctly pointed out, the scope of the "market", for determining the area of competition between two products, may depend on several factors such as the nature of the product, the homogeneity of the conditions of competition, and transport costs.⁴⁵⁶ This market for a particular product could well be a

⁴⁴⁹Panel Report, paras. 7.1248 and 7.1251; United States' appellant's submission, para. 310; Brazil's appellee's submission, paras. 636 and 638.

⁴⁵⁰See *infra*, footnote 451.

⁴⁵¹Specifically, the subsidized product is United States upland cotton lint. (Panel Report, paras. 7.139, 7.1221-7.1224 and footnote 191 to para. 7.139). The Panel explained that upland cotton, upon harvest, comprises cotton lint and cottonseed. The cotton lint is separated from the cottonseed through "ginning". (Panel Report, footnote 258 to para. 7.197)

⁴⁵²Panel Report, footnote 258 to para. 7.197 and paras. 7.1221-7.1224. The United States and Brazil confirmed during the oral hearing that they do not contest this identification of the subsidized product and the other relevant product.

⁴⁵³Accordingly, we need not decide whether, in a claim of significant price suppression under Article 6.3(c), the product identified by the complainant must be "like" the relevant subsidized product. We note in this regard that the term "in the same market" appears twice in Article 6.3(c). In the case of *significant price undercutting*, the "subsidized product" must be "compared with the price of a *like product* of another Member in the same market". (emphasis added) This raises the question whether the other three situations mentioned in Article 6.3(c) (namely, "significant price suppression, price depression [and] lost sales") include a requirement that the subsidized product and the relevant product of the complainant be "like".

⁴⁵⁴Panel Report, paras. 7.1248 and 7.1251; United States' appellant's submission, para. 310; Brazil's appellee's submission, paras. 636 and 638.

⁴⁵⁵Panel Report, para. 7.1236 (quoting *Merriam-Webster Dictionary online*).

⁴⁵⁶Panel Report, para. 7.1237 and footnote 1357 to para. 7.1240.

"world market". However, we agree with the Panel that the fact that a world market exists for one product does not necessarily mean that such a market exists for every product.⁴⁵⁷ Thus the determination of the relevant market under Article 6.3(c) of the *SCM Agreement* depends on the subsidized product in question. If a world market exists for the product in question, Article 6.3(c) does not exclude the possibility of this "world market" being the "same market" for the purposes of a significant price suppression analysis under that Article.

409. According to the United States, if the market examined pursuant to a claim of significant price suppression under Article 6.3(c) is a "world market", then the subsidized product and any like product will necessarily be in that market and the word "same" in Article 6.3(c) would have no meaning.⁴⁵⁸ We do not agree with this argument. As we have explained above, there is no *per se* geographical limitation of a market under Article 6.3(c). It could well be a national market, a world market, or any other market. It is for the complaining party to identify the market where it alleges significant price suppression and to establish that that market exists. In doing so, it is for the complaining party to establish that the subsidized product and its product are in actual or potential competition in that alleged market. If that market is established to be a "world market", it cannot be said, for that reason alone, that the two products are not in the "same market" within the meaning of Article 6.3(c).

410. For these reasons, we agree with the Panel that, depending on the facts of the case, a "world market" may be the "same market" for the purposes of a claim of significant price suppression under Article 6.3(c) of the *SCM Agreement*.⁴⁵⁹

411. We now examine the United States' objection to the Panel's examination of the "world market for upland cotton"⁴⁶⁰ in the particular circumstances of this dispute. The United States submits that the Panel's finding that a world market for upland cotton exists is inconsistent with the Panel's suggestion that the United States price for upland cotton is different from the "world price" represented by the A-Index.⁴⁶¹ Essentially, the United States appears to argue that no world market for upland cotton can exist if there is no world price for upland cotton. In our view, whether a world market for upland cotton and a world price for upland cotton exist in the circumstances of this case

⁴⁵⁷*Ibid.*, footnote 1357 to para. 7.1240.

⁴⁵⁸One can speak of a 'same' regional or national market because there are 'other' regional or national markets where the subsidized and like product may (or may not) compete. One cannot speak of a 'same' world market in the same way because there is no 'other' world market where the products can be found." (United States' appellant's submission, para. 311)

⁴⁵⁹Panel Report, paras. 7.1238-7.1244.

⁴⁶⁰*Ibid.*, paras. 7.1247 and 7.1274.

⁴⁶¹United States' appellant's submission, para. 319 (referring to Panel Report, para. 7.1213).

are factual questions. The Panel Report indicates that the Panel examined the evidence before it and concluded on the basis of that evidence that a world market for upland cotton exists⁴⁶² and that a world price in that market also exists and is reflected in the A-Index.⁴⁶³ We see no reason to disturb the Panel's findings of fact in this regard.⁴⁶⁴

412. The United States also contends that the Panel did not make a finding that United States and Brazilian upland cotton were both in the world market that it had identified for upland cotton.⁴⁶⁵ As we explained earlier⁴⁶⁶, the words "in the same market" in Article 6.3(c) of the *SCM Agreement* mean that subsidized United States upland cotton and Brazilian upland cotton must be engaged in actual or potential competition in the market in which the effect of the challenged subsidy is alleged to be significant price suppression. In this regard, we note that the Panel expressly stated that the market it examined pursuant to Article 6.3(c) had to be a market "in which both Brazilian and United States upland cotton were present and competing for sales"⁴⁶⁷ and "where competition exists between Brazilian and United States upland cotton".⁴⁶⁸

413. Whether or not Brazilian and United States upland cotton competed in the "world market for upland cotton"⁴⁶⁹ during the period the Panel examined is a factual question. As we stated earlier⁴⁷⁰, two products may be "in the same market" even if they are not necessarily sold in the same place and at the same time, as long as they are engaged in actual or potential competition. We recall that, in addition to the "world market", Brazil identified "40 third country markets ... where United States and Brazilian like upland cotton is found"⁴⁷¹. We also note that, based on an assessment of the relevant facts, the Panel concluded, as a matter of fact, that these two products did compete in the world

⁴⁶²Panel Report, paras. 7.1245-7.1252.

⁴⁶³*Ibid.*, paras. 7.1260-7.1274. The Panel's "four main reasons" for this conclusion regarding the A-Index were: prices of Brazilian and United States upland cotton are "constituent elements" of the A-Index; "key market participants" perceive the A-Index as reflecting the world market price for upland cotton; the International Cotton Advisory Council treats the A-Index in a similar manner; and the Economic Research Service of the United States Department of Agriculture (the "USDA") has itself referred to the A-Index as the world price. In addition, "the United States 'adjusted world price' is based on and derived from the A-Index" (*ibid.*, paras. 7.1265-7.1271) (original emphasis).

⁴⁶⁴See Appellate Body Report, *EC – Hormones*, para. 132. See also Appellate Body Report, *US – Wheat Gluten*, para. 151.

⁴⁶⁵United States' appellant's submission, para. 320.

⁴⁶⁶*Supra*, paras. 407-408.

⁴⁶⁷Panel Report, para. 7.1248.

⁴⁶⁸*Ibid.*, para. 7.1251.

⁴⁶⁹*Ibid.*, paras. 7.1247 and 7.1274.

⁴⁷⁰*Supra*, para. 408.

⁴⁷¹Panel Report, para. 7.1230.

market for upland cotton. In particular, the Panel referred to "the world upland cotton market, and the relative proportion of that market enjoyed by the United States and Brazil".⁴⁷²

414. We are therefore not persuaded by the United States' arguments that the Panel erred with respect to whether United States and Brazilian upland cotton were "in the same market" according to Article 6.3(c).

4. Relevant Price under Article 6.3(c) of the *SCM Agreement*

415. We now turn to the United States' arguments on appeal with respect to the relevant "price" under Article 6.3(c). The Panel found that "the A-Index can be taken to reflect a world price in the world market for upland cotton that is sufficient to form the basis for our analysis as to whether there is price suppression in the same world market within the meaning of Article 6.3(c) for the purposes of this dispute".⁴⁷³ The United States argues that, even if the Panel properly found that the effect of the price-contingent subsidies is significant suppression of the *world price* for upland cotton, this could not constitute significant price suppression for purposes of Brazil's claim under Article 6.3(c) of the *SCM Agreement*. According to the United States, Brazil had to show that the effect of the challenged subsidies is significant suppression of "the price of Brazilian upland cotton in the 'world market'".⁴⁷⁴

416. We have already found that the "market" referred to in Article 6.3(c), in connection with significant price suppression, can be a "world market"⁴⁷⁵, and that the Panel was correct in examining the world market for upland cotton in the present dispute.⁴⁷⁶ The question before us is whether it was sufficient for the Panel to analyze the price of upland cotton in general in the world market or whether the Panel was required to analyze the price of Brazilian upland cotton in the world market and find significant price suppression with respect to that price.

417. In our view, it was sufficient for the Panel to analyze the price of upland cotton in general in the world market. The Panel did so by relying on the A-Index. The Panel specifically found, based on its reading of the evidence before it:

⁴⁷²*Ibid.*, para. 7.1313. See also *ibid.*, para. 7.1246.

⁴⁷³Panel Report, para. 7.1274. According to the Panel, the "A-Index" "is a composite of an average of the five lowest price quotes from a selection of the principal upland cottons traded in the world market obtained by Cotlook, a private UK-based organization". (Panel Report, para. 7.1264)

⁴⁷⁴United States' appellant's submission, para. 239.

⁴⁷⁵*Supra*, para. 410.

⁴⁷⁶*Supra*, para. 414.

[P]rices for upland cotton transactions throughout the world are ... largely determined by the A-Index price.⁴⁷⁷

Therefore, the Panel found that the A-Index adequately reflected prices in the world market for upland cotton.⁴⁷⁸ The Panel also found that "developments in the world upland cotton price would inevitably affect prices" wherever Brazilian and United States upland cotton compete, "due to the nature of the world prices in question and the nature of the world upland cotton market, and the relative proportion of that market enjoyed by the United States and Brazil".⁴⁷⁹ It was not necessary, in these circumstances, for the Panel to proceed to a separate analysis of the prices of Brazilian upland cotton in the world market.

418. For these reasons, we reject the United States' contention that the Panel erred in its analysis of significant price suppression under Article 6.3(c) of the *SCM Agreement* "in not examining Brazilian upland cotton prices in the 'world market'".⁴⁸⁰

5. Significant Price Suppression as the Effect of the Price-Contingent Subsidies

(a) Introduction

419. We now address the reasons the Panel provided for its ultimate finding under Article 6.3(c). First, the Panel found that price suppression had occurred within the meaning of Article 6.3(c)⁴⁸¹ after examining three main considerations: "(a) the relative magnitude of the United States' production and exports in the world upland cotton market; (b) general price trends [in the world market as revealed by the A-Index]; and (c) the nature of the subsidies at issue, and in particular, whether or not the nature of these subsidies is such as to have discernible price suppressive effects".⁴⁸² Next, the Panel found that the price suppression it had found to exist was "significant" price suppression under Article 6.3(c)⁴⁸³, "given the relative magnitude of United States production and exports, the overall price trends we identified in the world market, ... the nature of the mandatory United States subsidies in question ... and the readily available evidence of the order of magnitude of the subsidies".⁴⁸⁴

⁴⁷⁷Panel Report, para. 7.1311.

⁴⁷⁸*Ibid.*, para. 7.1274.

⁴⁷⁹*Ibid.*, para. 7.1313.

⁴⁸⁰United States' appellant's submission, para. 238.

⁴⁸¹Panel Report, para. 7.1312.

⁴⁸²*Ibid.*, para. 7.1280.

⁴⁸³*Ibid.*, para. 7.1333.

⁴⁸⁴Panel Report, para. 7.1332. (footnotes omitted) We address the United States' arguments regarding the magnitude or quantification of the subsidies *infra*, paras. 459-472.

420. The Panel went on to find that "a causal link exists between" the price-contingent subsidies and the significant price suppression it had found⁴⁸⁵, for four main reasons:⁴⁸⁶

[T]he United States exerts a substantial proportionate influence in the world upland cotton market.⁴⁸⁷

[T]he [price-contingent subsidies] are directly linked to world prices for upland cotton, thereby insulating United States producers from low prices.⁴⁸⁸

[T]here is a discern[ible] temporal coincidence of suppressed world market prices and the price-contingent United States subsidies.⁴⁸⁹

[C]redible evidence on the record concerning the divergence between United States producers' total costs of production and revenue from sales of upland cotton since 1997 ... supports the proposition that United States upland cotton producers would not have been economically capable of remaining in the production of upland cotton had it not been for the United States subsidies at issue and that the effect of the subsidies was to allow United States producers to sell upland cotton at a price lower than would otherwise have been necessary to cover their total costs.⁴⁹⁰

421. Finally, the Panel found that the following "other causal factors alleged by the United States"⁴⁹¹ "do not attenuate the genuine and substantial causal link that we have found between the United States mandatory price-contingent subsidies at issue and the significant price suppression. Nor do they reduce the effect of the mandatory price-contingent subsidies to a level which cannot be considered 'significant'":⁴⁹²

[W]eakness in world demand for cotton due to competing, low-priced synthetic fibres, and weak world economic growth.⁴⁹³

[B]urgeoning United States textile imports, reflecting the strong United States dollar since the mid-1990's and declining United States competitiveness in textile and apparel production[.]⁴⁹⁴

⁴⁸⁵Panel Report, para. 7.1355.

⁴⁸⁶*Ibid.*, para. 7.1347.

⁴⁸⁷*Ibid.*, para. 7.1348.

⁴⁸⁸*Ibid.*, para. 7.1349.

⁴⁸⁹*Ibid.*, para. 7.1351.

⁴⁹⁰*Ibid.*, para. 7.1353. (footnotes omitted)

⁴⁹¹*Ibid.*, para. 7.1357.

⁴⁹²*Ibid.*, para. 7.1363.

⁴⁹³Panel Report, para. 7.1358.

⁴⁹⁴*Ibid.*, para. 7.1359.

[T]he strong United States dollar since the mid-1990s[.]⁴⁹⁵

China subsidized the release of millions of bales of government stocks between 1999 and 2001[.]⁴⁹⁶

[U]pland cotton planting decisions ... are driven by other factors such as (1) the effect of technological factors of upland cotton production ... (2) the relative movement of upland cotton prices *vis-à-vis* prices of competing crops ... (3) the expected prices for the upcoming crop year.⁴⁹⁷

(b) Appeal by the United States

422. In addition to the alleged errors already discussed in connection with the relevant "market" and "price", the United States contends on appeal that the Panel erred in finding that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*.⁴⁹⁸ These errors, according to the United States, are:

(a) in relation to the effects of the price-contingent subsidies:

- (i) failing to analyze "the relevant production decision faced by farmers – that is, the decision on what to plant"⁴⁹⁹,
- (ii) ignoring data indicating that United States upland cotton production responded to market signals⁵⁰⁰,
- (iii) "failing to examine supply response in other countries – that is, to what extent other countries would increase supply in response to any alleged decrease in cotton production resulting from the absence of U.S. payments"⁵⁰¹; and
- (iv) "the four main, cumulative grounds the Panel identified supporting a finding of causation do not withstand scrutiny"⁵⁰².

⁴⁹⁵ *Ibid.*, para. 7.1360.

⁴⁹⁶ *Ibid.*, para. 7.1361.

⁴⁹⁷ *Ibid.*, para. 7.1362.

⁴⁹⁸ *Ibid.*, paras. 7.1416 and 8.1(g)(i).

⁴⁹⁹ United States' appellant's submission, paras. 136 and 154.

⁵⁰⁰ *Ibid.*, para. 155.

⁵⁰¹ United States' appellant's submission, para. 227.

⁵⁰² *Ibid.*, para. 180.

(b) in relation to the quantification of subsidies:

- (i) "accepting Brazil's argument that, for purposes of a serious prejudice claim, Brazil need not allege and demonstrate, and the Panel need not find, the amount of the challenged subsidy that benefits upland cotton"⁵⁰³,
- (ii) finding "that subsidies not tied to current production of upland cotton (decoupled payments) need not be allocated over the total sales of the recipients"⁵⁰⁴, and
- (iii) failing to determine "the extent to which processed cotton benefits from subsidies provided with respect to raw cotton"⁵⁰⁵; and

(c) in relation to the effect of subsidies over time:

- (i) concluding "that the payments need not be allocated to the marketing year to which they relate"⁵⁰⁶, and
 - (ii) "making a finding of present serious prejudice related to past recurring subsidy payments", in the absence of a finding "that the past recurring subsidy payments at issue (that is, those from marketing years 1999-2001) had continuing effects at the time of panel establishment"⁵⁰⁷
- (c) Meaning of "Significant Price Suppression"

423. A central question before the Panel with regard to Article 6.3(c) of the *SCM Agreement* was whether the effect of the subsidy is "significant price suppression".⁵⁰⁸ It is worth setting out the Panel's understanding of the meaning of the term "price suppression". In explaining this term, the Panel stated, in paragraph 7.1277 of the Panel Report:

⁵⁰³ *Ibid.*, para. 240.

⁵⁰⁴ *Ibid.*, para. 264.

⁵⁰⁵ *Ibid.*, para. 301.

⁵⁰⁶ *Ibid.*, para. 277.

⁵⁰⁷ *Ibid.*, para. 278.

⁵⁰⁸ According to the Panel, Brazil claimed that certain United States subsidies "significantly suppress[ed] upland cotton prices" within the meaning of Article 6.3(c). (Panel Report, para. 7.1108(i))

Thus, "price suppression" refers to the situation where "prices" – in terms of the "amount of money set for sale of upland cotton" or the "value or worth" of upland cotton – either are prevented or inhibited from rising (i.e. they do not increase when they otherwise would have) or they do actually increase, but the increase is less than it otherwise would have been. *Price depression* refers to the situation where "prices" are pressed down, or reduced.¹³⁸⁸

¹³⁸⁸ In the remainder of our analysis, we use the term "price suppression" to refer both to an actual decline (which otherwise would not have declined, or would have done so to a lesser degree) and an increase in prices (which otherwise would have increased to a greater degree). (emphasis added)

424. Although the Panel first identified "price suppression" and "price depression" as two separate concepts in paragraph 7.1277, footnote 1388 of the Panel Report suggests that, for its analysis, the Panel used the term "price suppression" to refer to both price suppression and price depression. We recognize that "the situation where 'prices' ... are prevented or inhibited from rising" and "the situation where 'prices' are pressed down, or reduced"⁵⁰⁹ may overlap. Nevertheless, it would have been preferable, in our view, for the Panel to avoid using the term "price suppression" as short-hand for both price suppression and price depression, given that Article 6.3(c) of the *SCM Agreement* refers to "price suppression" and "price depression" as distinct concepts. We agree, however, that the Panel's description of "price suppression" in paragraph 7.1277 of the Panel Report reflects the ordinary meaning of that term, particularly when read in conjunction with the French and Spanish versions of Article 6.3(c)⁵¹⁰, as required by Article 33(3) of the *Vienna Convention on the Law of Treaties* (the "*Vienna Convention*").⁵¹¹

425. The Panel described its task in assessing "price suppression" under Article 6.3(c) as follows:

We need to examine whether these prices were suppressed, that is, lower than they would have been without the United States subsidies in respect of upland cotton.⁵¹²

426. As regards the word "significant" in the context of "significant price suppression" in Article 6.3(c), the Panel found that this word means "important, notable or consequential".⁵¹³

⁵⁰⁹Panel Report, para. 7.1277.

⁵¹⁰The French version states, in part, "la subvention ... a pour effet d'empêcher des hausses de prix ou de déprimer les prix ... dans une mesure notable"; the Spanish version states, in part, "la subvención ... tenga un efecto significativo de contención de la subida de los precios, reducción de los precios"; (emphasis added)

⁵¹¹Done at Vienna, 23 May 1969, 1155 U.N.T.S. 331; 8 International Legal Materials 679. Article 33(3) provides: "The terms of the treaty are presumed to have the same meaning in each authentic text."

⁵¹²Panel Report, para. 7.1288. See also *ibid.*, para. 7.1279.

427. Article 6.3(c) does not set forth any specific methodology for determining whether the effect of a subsidy is significant price suppression. There may well be different ways to make this determination. However, we find no difficulty with the Panel's approach in the particular circumstances of this dispute. We therefore turn to an examination of how the Panel carried out its assessment.

(d) Panel's Order of Analysis

428. In addressing Brazil's claims of serious prejudice under Articles 5(c) and 6.3(c) of the *SCM Agreement*, the Panel began by examining whether the effect of the challenged subsidies was significant price suppression within the meaning of Article 6.3(c). The Panel explained that it adopted this order of analysis because both parties agreed that the Panel could not make an affirmative finding of serious prejudice under Article 5(c) without making an affirmative finding that the effect of the challenged subsidies is significant price suppression within the meaning of Article 6.3(c).⁵¹⁴ Neither party appeals this decision by the Panel.

429. Having determined the relevant products, market, and price, the Panel continued its analysis with respect to Article 6.3(c) in the following order:

Is there "price suppression"?⁵¹⁵

Is it "significant" price suppression?⁵¹⁶

"The effect of the subsidy"⁵¹⁷

430. The United States contests the Panel's decision to address "significant price suppression" before addressing "the effect of the subsidy", arguing that "[a] finding of price suppression without any prior finding of 'the effect of the subsidy' would be meaningless; how could one know that prices were lower than they otherwise would have been without knowing what allegedly caused the prices to be lower?"⁵¹⁸ The United States also contends that the Panel used "circular" reasoning by assuming causation in finding price suppression and using its conclusion on price suppression to support its finding on causation (the effect of the subsidy).⁵¹⁹

⁵¹³*Ibid.*, para. 7.1326.

⁵¹⁴*Ibid.*, para. 7.1228.

⁵¹⁵*Ibid.*, heading (ii) to paras. 7.1275-7.1315.

⁵¹⁶*Ibid.*, heading (iii) to paras. 7.1316-7.1333.

⁵¹⁷*Ibid.*, heading (k) to paras. 7.1334-7.1363.

⁵¹⁸United States' appellant's submission, para. 230. (original emphasis)

⁵¹⁹*Ibid.*, para. 131.

431. As noted above, Article 6.3(c) is silent as to the sequence of steps to be followed in assessing whether the effect of a subsidy is significant price suppression. We note that Article 6.8 indicates that the existence of serious prejudice pursuant to Articles 5(c) and 6.3(c) is to be determined on the basis of information submitted to or obtained by the panel, including information submitted in accordance with Annex V of the *SCM Agreement*.⁵²⁰ Annex V provides some limited guidance about the type of information on which a panel might base its assessment under Article 6.3(c). But we find little other guidance on this issue. The text of Article 6.3(c) does not, however, preclude the approach taken by the Panel to examine first whether significant price suppression exists and then, if it is found to exist, to proceed further to examine whether the significant price suppression is the effect of the subsidy. The Panel evidently considered that, in the absence of significant price suppression, it would not need to proceed to analyze the effect of the subsidy. We see no legal error in this approach.

432. One might contend that, having decided to separate its analysis of significant price suppression from its analysis of the effects of the challenged subsidies, the Panel's price suppression analysis should have addressed prices without reference to the subsidies and their effects. For instance, in its significant price suppression analysis, the Panel could have addressed purely price developments in the world market for upland cotton, such as whether prices fell significantly during the period under examination or whether prices were significantly lower during that period than other periods. Then, in its "effects" analysis, the Panel could have addressed causal factors related to the nature of the subsidies, their relationship to prices, their magnitude, and their impact on production and exports. In this causal analysis, the Panel could also have addressed factors other than the challenged subsidies that may have been suppressing the prices in question.

433. However, the ordinary meaning of the transitive verb "suppress" implies the existence of a subject (the challenged subsidies) and an object (in this case, prices in the world market for upland cotton). This suggests that it would be difficult to make a judgement on significant price suppression without taking into account the effect of the subsidies.⁵²¹ The Panel's definition of price suppression, explained above⁵²², reflects this problem; it includes the notion that prices "do not increase when they *otherwise* would have" or "they do actually increase, but the increase is less than

⁵²⁰ Annex V contains "Procedures for Developing Information Concerning Serious Prejudice".

⁵²¹ Similarly, it might be difficult to ascertain whether imports or exports are "displace[d]" or "impede[d]" under paragraphs (a) or (b) of Article 6.3 of the *SCM Agreement* without considering the effect of the challenged subsidy. By way of contrast, it might be possible to determine whether the world market share of a subsidizing Member has increased within the meaning of Article 6.3(d) before assessing whether any increase is the effect of the subsidy.

⁵²² *Supra*, para. 423.

it *otherwise* would have been".⁵²³ The word "otherwise" in this context refers to the hypothetical situation in which the challenged subsidies are absent. Therefore, the fact that the Panel may have addressed some of the same or similar factors in its reasoning as to significant price suppression and its reasoning as to "effects" is not necessarily wrong.⁵²⁴

434. The specific factors that the Panel examined in determining whether or not "price suppression" had occurred were: "(a) the relative magnitude of the United States' production and exports in the world upland cotton market; (b) general price trends; and (c) the nature of the subsidies at issue, and in particular, whether or not the nature of these subsidies is such as to have discernible price suppressive effects".⁵²⁵ In the absence of explicit guidance on assessing significant price suppression in the text of Article 6.3(c), we have no reason to reject the relevance of these factors for the Panel's assessment in the present case. An assessment of "general price trends"⁵²⁶ is clearly relevant to significant price suppression (although, as the Panel itself recognized, price trends alone are not conclusive).⁵²⁷ The two other factors—the nature of the subsidies and the relative magnitude of the United States' production and exports of upland cotton—are also relevant for this assessment. We are not persuaded that the fact that these latter factors were also considered in connection with the Panel's analysis of "the effect of the subsidy"⁵²⁸ amounts to legal error for that reason alone.

⁵²³ Panel Report, para. 7.1277. (emphasis added)

⁵²⁴ An analysis under Article 6.3(c) *SCM Agreement* could involve assessing similar facts from different perspectives in order to answer different factual and legal questions when addressing "significant price suppression" and "the effect of" the challenged subsidies.

⁵²⁵ Panel Report, para. 7.1280.

⁵²⁶ *Ibid.*, para. 7.1286. See also *ibid.*, para. 7.1310.

⁵²⁷ *Ibid.*, para. 7.1288.

⁵²⁸ We discuss these factors *infra*, paras. 449 and 450.

435. Turning to the Panel's assessment of the "effect of the subsidy"⁵²⁹, the Panel addressed the question whether there was a "causal link"⁵³⁰ between the price-contingent subsidies and the significant price suppression it had found. It then addressed the impact of "[o]ther alleged causal factors".⁵³¹ We observe that Article 6.3(c) does not use the word "cause"; rather, it states that "the effect of the subsidy is ... significant price suppression". However, the ordinary meaning of the noun "effect" is "[s]omething ... caused or produced; a result, a consequence".⁵³² The "something" in this context is significant price suppression, and thus the question is whether significant price suppression is "caused" by or is a "result" or "consequence" of the challenged subsidy. The Panel's conclusion that "[t]he text of the treaty requires the establishment of a causal link between the subsidy and the significant price suppression"⁵³³ is thus consistent with this ordinary meaning of the term "effect". This is also confirmed by the context provided by Article 5(c) of the *SCM Agreement*, which provides:

No Member should cause, through the use of any subsidy referred to in paragraphs 1 and 2 of Article 1, adverse effects to the interests of other Members, i.e.:

- ...
- (c) serious prejudice to the interests of another Member.

436. As the Panel pointed out, "Articles 5 and 6.3 ... do not contain the more elaborate and precise 'causation' and non-attribution language" found in the trade remedy provisions of the *SCM Agreement*.⁵³⁴ Part V of the *SCM Agreement*, which relates to the imposition of countervailing duties, requires, *inter alia*, an examination of "any known factors other than the subsidized imports which at the same time are injuring the domestic industry".⁵³⁵ However, such causation requirements have not been expressly prescribed for an examination of *serious prejudice* under Articles 5(c) and Article 6.3(c) in Part III of the *SCM Agreement*. This suggests that a panel has a certain degree of discretion in selecting an appropriate methodology for determining whether the "effect" of a subsidy is significant price suppression under Article 6.3(c).

⁵²⁹Panel Report, heading (k) to paras. 7.1334-7.1363.

⁵³⁰*Ibid.*, heading (i) to paras. 7.1347-7.1356.

⁵³¹*Ibid.*, heading (ii) to paras. 7.1357-7.1363.

⁵³²*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 1, p. 793.

⁵³³Panel Report, para. 7.1341.

⁵³⁴*Ibid.*, para. 7.1343.

⁵³⁵See Article 15.5 of the *SCM Agreement*. Article 3.5 of the *Anti-Dumping Agreement* and Article 4.2(b) of the *Agreement on Safeguards* are broadly analogous to Article 15.5 of the *SCM Agreement*.

437. Nevertheless, we agree with the Panel that it is necessary to ensure that the effects of other factors on prices are not improperly attributed to the challenged subsidies.⁵³⁶ Pursuant to Article 6.3(c) of the *SCM Agreement*, "[s]erious prejudice in the sense of paragraph (c) of Article 5 may arise" when "the effect of the subsidy is ... significant price suppression". (emphasis added) If the significant price suppression found in the world market for upland cotton were caused by factors other than the challenged subsidies, then that price suppression would not be "the effect of" the challenged subsidies in the sense of Article 6.3(c). Therefore, we do not find fault with the Panel's approach of "examin[ing] whether or not 'the effect of the subsidy' is the significant price suppression which [it had] found to exist in the same world market"⁵³⁷ and separately "consider[ing] the role of other alleged causal factors in the record before [it] which may affect [the] analysis of the causal link between the United States subsidies and the significant price suppression."⁵³⁸

438. The Panel's approach with respect to causation and non-attribution is similar to that reflected in Appellate Body decisions in the context of other WTO agreements. In connection with the *Agreement on Safeguards*, the Appellate Body has stated that a causal link "between increased imports of the product concerned and serious injury or threat thereof"⁵³⁹ "involves a genuine and substantial relationship of cause and effect between these two elements"⁵⁴⁰, and it has also required non-attribution of effects caused by other factors.⁵⁴¹ In the context of the *Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994* (the "*Anti-Dumping Agreement*"), the Appellate Body has stated: "[i]n order that investigating authorities, applying Article 3.5, are able to ensure that the injurious effects of the other known factors are not 'attributed' to dumped imports, they must appropriately assess the injurious effects of those other factors."⁵⁴² It must be borne in mind that these provisions of the *Agreement on Safeguards* and the *Anti-Dumping Agreement*, as well as the provisions of Part V of the *SCM Agreement*, relate to a determination of "injury" rather than "serious prejudice", and they apply in different contexts and with different purposes. Therefore, they must not be automatically transposed into Part III of the *SCM Agreement*. Nevertheless, they may suggest ways of assessing whether the effect of a subsidy is significant price suppression rather than it being the effect of other factors.

⁵³⁶Panel Report, para. 7.1344.

⁵³⁷*Ibid.*, para. 7.1345.

⁵³⁸*Ibid.*, para. 7.1346.

⁵³⁹Article 4.2(b) of the *Agreement on Safeguards*. Compare Article 15.5 of the *SCM Agreement* and Article 3.5 of the *Anti-Dumping Agreement*.

⁵⁴⁰Appellate Body Report, *US – Wheat Gluten*, para. 69.

⁵⁴¹Appellate Body Report, *US – Line Pipe*, para. 208.

⁵⁴²Appellate Body Report, *US – Hot-Rolled Steel*, para. 223.

(e) Rationale for the Panel's Finding that the Effect of the Price-Contingent Subsidies is Significant Price Suppression

439. We now address the United States' appeal relating to the specific reasons behind the Panel's conclusion that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*. The United States alleges that the Panel ignored or failed to take into account certain evidence and arguments in analyzing the effect of the price-contingent subsidies, and that the four main grounds on which the Panel based its analysis "do not withstand scrutiny".⁵⁴³ We begin by addressing the three key elements that the United States alleges the Panel failed to include in its analysis, and then we address the reasons the Panel relied upon for its conclusion that the effect of the price-contingent subsidies is significant price suppression.

440. First, the United States contends that the Panel failed to address the relevant economic decision faced by United States upland cotton farmers at the time of planting, namely, the decision of whether to plant upland cotton or alternative crops (and how much of each). According to the United States, planted acreage of United States upland cotton responds to expected market prices at the time of harvest, rather than current prices at the time of planting.⁵⁴⁴ Brazil counters that farmers decide what to plant based on expected market prices as well as expected payments under the challenged subsidy programs, such that planted acreage responds to both these factors.⁵⁴⁵ Brazil also points out that farmers sell their upland cotton throughout the course of a year, at whatever prices they can obtain during the year.⁵⁴⁶ During the oral hearing, the United States accepted that farmers decide what to plant based on expected market prices as well as expected subsidies.⁵⁴⁷ However, according to the United States, for the 1999-2001 and 2003 crop years, when farmers made their planting decisions, the expected upland cotton price (that is, the price the farmers expected to receive upon harvest) was higher than the "income guarantee set by the marketing loan rate, suggesting that the effect of the subsidy on the planting decision was minimal".⁵⁴⁸

441. We note that the United States presented extensive evidence and arguments to the Panel in relation to expected prices and planting decisions.⁵⁴⁹ Brazil also points to several questions asked by

⁵⁴³United States' appellant's submission, para. 180. See *supra*, para. 420.

⁵⁴⁴United States' appellant's submission, paras. 154 and 155.

⁵⁴⁵Brazil's appellee's submission, para. 692.

⁵⁴⁶Brazil's response to questioning at the oral hearing.

⁵⁴⁷See also United States' further rebuttal submission to the Panel, paras. 95-97.

⁵⁴⁸United States' statement and response to questioning at the oral hearing.

⁵⁴⁹See, for example: United States' further submission to the Panel, paras. 55-60; United States' further rebuttal submission to the Panel, paras. 95-97 and 152-177.

the Panel and responses to the Panel regarding planting decisions of United States upland cotton producers to demonstrate that the Panel was aware of the United States' arguments in this regard and took them into account.⁵⁵⁰ The Panel Report makes it clear that the Panel specifically addressed "upland cotton planting decisions", "expected prices", and "expected market revenue".⁵⁵¹ The way in which United States upland cotton farmers make decisions relating to the production of upland cotton, and the basis on which they make such decisions, are factual matters that fall within the Panel's task of weighing and assessing the relevant evidence, and we will not review these matters. However, in our view, the application of the legal requirements of Article 6.3(c) to the facts determined by the Panel falls within the scope of appellate review.⁵⁵²

442. Turning first to Chart 2 at paragraph 7.1293 of the Panel Report, the United States submits that it is defective because it "assumes that cotton production decisions are made continuously throughout the marketing year", it "does not identify the planting decision period", and it "does not identify the expected harvest season prices at the time of that planting decision".⁵⁵³ The Panel explained that it used this chart to demonstrate "that the per unit payment under the marketing loan programme increases when the gap between the adjusted world price and the loan rate widens"⁵⁵⁴ and "that except for a short period in MY 2000, the adjusted world price was *below* the marketing loan rate throughout virtually *the whole period from MY 1999-2002*".⁵⁵⁵ The Panel concluded from this graph, in connection with marketing loan program payments, that "[t]he further the adjusted world price drops, the greater the extent to which United States upland cotton producers' revenue is insulated from the decline, numbing United States production decisions from world market signals".⁵⁵⁶

443. The Panel explained how the marketing loan program payments operate and found that these payments accounted for more than half of United States upland cotton producer revenue.⁵⁵⁷ This demonstrates that, in assessing the effect of marketing loan program payments under Article 6.3(c), the Panel took into account the magnitude of the payments relative to the revenue of United States

⁵⁵⁰Brazil's appellee's submission, para. 685 (referring, *inter alia*, to Brazil's response to Question 167 posed by the Panel (Panel Report, pp. I-216-217, para.151); United States' response to Question 212 Posed by the Panel (Panel Report, p. I-360, para. 51); Question 213 Posed by the Panel (Panel Report, p. I-361)).

⁵⁵¹Panel Report, para. 7.1362.

⁵⁵²See the discussion *supra*, para. 399.

⁵⁵³United States' statement at the oral hearing.

⁵⁵⁴Panel Report, para. 7.1293.

⁵⁵⁵*Ibid.*, para. 7.1294. (original emphasis)

⁵⁵⁶*Ibid.*, para. 7.1294.

⁵⁵⁷*Ibid.*, para. 7.1294.

upland cotton producers and found that marketing loan program payments made up a significant proportion of producers' revenue.⁵⁵⁸

444. During the oral hearing, the United States presented data to show that, when planting decisions were made for the 1999, 2000, 2001, and 2003 upland cotton crops, the *expected* upland cotton price upon harvest was higher than the marketing loan rate.⁵⁵⁹ Accordingly, the United States contends, the marketing loan program payments would have had only a minimal effect on planting decisions, because farmers would have expected to receive a higher price from the sale of their upland cotton and no marketing loan program payments.

445. We note, based on the evidence provided by the United States, that, for four of the five upland cotton crops between 1999 and 2003, the *expected* harvest price at the time of making planting decisions was always substantially higher than the *actual* price realized at the time of harvest of the crop. This suggests that although farmers had expected higher prices in making their planting decisions, they were also aware that if actual prices were ultimately lower, they would be "insulated"⁵⁶⁰ by government support, including not only marketing loan program payments but also counter-cyclical payments, which were based on a target upland cotton price of 72.4 cents per pound.⁵⁶¹ We are therefore satisfied that the Panel adopted a plausible view of the facts in connection with expected prices and planting decisions, even though it attributed to these factors a different weight or meaning than did the United States. As the Appellate Body has said, it is not necessary for panels to "accord to factual evidence of the parties the same meaning and weight as do the parties".⁵⁶²

446. Turning to the second key element of the United States' submission, the United States argues that the Panel ignored data showing that "U.S. cotton planted acreage did respond to expected market prices of cotton and other competing crops", "U.S. farmers change cotton acreage commensurately with changes made by cotton farmers in the rest of the world", and "the U.S. share of world cotton production has been stable, again demonstrating that U.S. farmers respond to the same market signals as cotton farmers in the rest of the world do".⁵⁶³ The Panel Report contains several passages

⁵⁵⁸We return to the issue of quantification of the price-contingent subsidies in section VI.A.5(f) below.

⁵⁵⁹This data corresponds with the United States' written argument that "the uncontroverted evidence before the Panel ... showed that U.S. cotton plantings respond to expected prices *at the time planting decisions are taken*". (United States' appellant's submission, para. 137) (original emphasis) The United States presented similar data to the Panel. (See, for example, United States' further rebuttal submission to the Panel, paras. 162-163)

⁵⁶⁰Panel Report, para. 7.1294.

⁵⁶¹*Ibid.*, para. 7.225.

⁵⁶²Appellate Body Report, *Australia – Salmon*, para. 267.

⁵⁶³United States' appellant's submission, para. 155.

suggesting that the Panel did take into account evidence of this kind. For example, the Panel considered the United States' evidence regarding expected upland cotton prices⁵⁶⁴ and set out the United States' share of world upland cotton production during the relevant period.⁵⁶⁵ It would not amount to an error in the application of Article 6.3(c) to the facts of this case for the Panel not to address specifically in its Report every item of evidence provided and to refer explicitly to every argument made by the parties, if the Panel considered certain items or arguments less significant for its reasoning than others.⁵⁶⁶

447. We now address the third key element of the United States' submission. The United States argues that "the Panel should have considered to what extent other market participants would increase supply or reduce demand in response to any alleged increase in cotton prices resulting from the absence of U.S. payments".⁵⁶⁷ Brazil responds that the Panel took this factor into account because it took into account relevant aspects of certain econometric models incorporating this factor: "the models track price effects that would occur as a result of reduced U.S. upland cotton supply *and* increased supply from other countries".⁵⁶⁸ The participants agree that these models incorporate the supply response of third countries.⁵⁶⁹ The dispute lies in whether the Panel *took into account* supply responses of third countries, as reflected in these models or otherwise.

448. Whether and to what extent other upland cotton producers would have increased supply or reduced demand in the absence of the United States' price-contingent subsidies is ultimately an empirical inquiry. The answer to this inquiry depends on an assessment of various factors bearing on the ability of cotton producers to assess and respond to supply and demand in the world upland cotton market. We note that the Panel indicated expressly that it had taken the models in question into account.⁵⁷⁰ It would have been helpful had the Panel revealed how it used these models in examining the question of third country responses. Nevertheless, we are not prepared to second-guess the Panel's

⁵⁶⁴Panel Report, para. 7.1362.

⁵⁶⁵*Ibid.*, para. 7.1282. In this paragraph, the Panel stated: "In the marketing years 1999 to 2002, the respective shares of the United States in world production of upland cotton were approximately 19.2, 19.3, 20.6 and 19.6 per cent, respectively".

⁵⁶⁶Appellate Body Report, *EC – Hormones*, paras. 135 and 138.

⁵⁶⁷United States' appellant's submission, para. 237.

⁵⁶⁸Brazil's appellee's submission, paras. 793-798 (referring to Panel Report, paras. 7.1205, 7.1209, and 7.1215). (original emphasis)

⁵⁶⁹In relation to models presented by Brazil, both parties refer to Brazil's further submission to the Panel of 9 September 2003, paras. 9-10 of Annex I (which is entitled "A Quantitative Simulation Analysis of the Impact of U.S. Cotton Subsidies on Cotton Prices and Quantities by Professor Daniel Sumner"). (United States' appellant's submission, para. 235; Brazil's appellee's submission, para. 793) In relation to third party studies, see United States' appellant's submission, para. 236 and Brazil's appellee's submission, paras. 795-796.

⁵⁷⁰Panel Report, paras. 7.1205, 7.1209 and 7.1215.

appreciation and weighing of the evidence before it, and we do not see any error on the part of the Panel in the application of the law to the facts in addressing this question.

449. We now turn to the four main grounds⁵⁷¹ on which the Panel based its conclusion that "a causal link exists between" the price-contingent subsidies and the significant price suppression it had found⁵⁷², which the United States contests.⁵⁷³ The first reason the Panel provided for finding a "causal link"⁵⁷⁴ was the "substantial proportionate influence" of the United States "in the world upland cotton market ... flow[ing]... from the magnitude of the United States production and export of upland cotton".⁵⁷⁵ The United States counters that, "absent some analysis of how U.S. cotton competes with cotton from other sources, relative sizes are meaningless."⁵⁷⁶ We agree that, in and of itself, the degree of influence of the United States in the world market for upland cotton may not be conclusive as to the effect of the price-contingent subsidies on prices in that market. However, if the price-contingent subsidies increased United States production and exports or decreased prices for United States upland cotton, then the fact that United States production and exports of upland cotton significantly influenced world market prices would make it more likely that the effect of the price-contingent subsidies is significant price suppression. Accordingly, this fact seems to support the Panel's conclusion, when read in conjunction with its other findings.

450. The second reason the Panel provided for finding a "causal link"⁵⁷⁷ was its view that the price-contingent subsidies "are directly linked to world prices for upland cotton".⁵⁷⁸ This conclusion flowed from the Panel's earlier assessment—in connection with its analysis of significant price suppression—of the *nature* of the price-contingent subsidies.⁵⁷⁹ The nature of a subsidy plays an important role in any analysis of whether the effect of the subsidy is significant price suppression under Article 6.3(c). With respect to marketing loan program payments, the Panel found that "[t]he further the adjusted world price drops, the greater the extent to which United States upland cotton producers' revenue is insulated from the decline".⁵⁸⁰ As a result, during the 1999-2002 marketing years, United States production and exports remained stable or increased, even though prices of

⁵⁷¹United States' appellant's submission, para. 180.

⁵⁷²Panel Report, para. 7.1355.

⁵⁷³United States' appellant's submission, para. 180.

⁵⁷⁴Panel Report, para. 7.1347.

⁵⁷⁵*Ibid.*, para. 7.1348.

⁵⁷⁶United States' appellant's submission, para. 183.

⁵⁷⁷Panel Report, para. 7.1347.

⁵⁷⁸*Ibid.*, para. 7.1349.

⁵⁷⁹*Supra*, para. 434.

⁵⁸⁰Panel Report, para. 7.1294.

United States upland cotton decreased.⁵⁸¹ The Panel found that Step 2 payments stimulate domestic and foreign demand for United States upland cotton⁵⁸² by "eliminating any positive difference between United States internal prices and international prices of upland cotton".⁵⁸³ The Panel stated that Step 2 payments "result in lower world market prices than would prevail in their absence".⁵⁸⁴ Finally, the Panel found that market loss assistance payments and counter-cyclical payments are made in response to low prices for upland cotton⁵⁸⁵ and stimulate United States production of upland cotton by reducing the "total and per unit revenue risk associated with price variability".⁵⁸⁶ The United States contends that the Panel's analysis of the price-contingent subsidies was "deficient".⁵⁸⁷ However, the Panel found that the price-contingent subsidies stimulated United States production and exports of upland cotton and thereby lowered United States upland cotton prices.⁵⁸⁸ This seems to us to support the Panel's conclusion that the effect of the price-contingent subsidies is significant price suppression.⁵⁸⁹

451. The third reason the Panel provided for finding a "causal link"⁵⁹⁰ was that "there is a discernible temporal coincidence of suppressed world market prices" and the price-contingent subsidies.⁵⁹¹ The United States describes this as "an exercise in spurious correlation".⁵⁹² However, in our view, one would normally expect a discernible correlation between significantly suppressed prices and the challenged subsidies if the effect of these subsidies is significant price suppression. Accordingly, this is an important factor in any analysis of whether the effect of a subsidy is significant price suppression within the meaning of Article 6.3(c). However, we recognize that mere correlation between payment of subsidies and significantly suppressed prices would be insufficient, without more, to prove that the effect of the subsidies is significant price suppression.

⁵⁸¹Panel Report, para. 7.1296.

⁵⁸²*Ibid.*, para. 7.1299.

⁵⁸³*Ibid.*, para. 7.1298.

⁵⁸⁴*Ibid.*, para. 7.1299.

⁵⁸⁵*Ibid.*, para. 7.1301.

⁵⁸⁶*Ibid.*, para. 7.1302 and footnote 1410 to para. 7.1302.

⁵⁸⁷United States' appellant's submission, para. 185.

⁵⁸⁸Panel Report, para. 7.1291, 7.1295-7.1296, 7.1299, and 7.1308-7.1311.

⁵⁸⁹We do not exclude the possibility that challenged subsidies that are not "price-contingent" (to use the Panel's term) could have some effect on production and exports and contribute to price suppression.

⁵⁹⁰Panel Report, para. 7.1347.

⁵⁹¹*Ibid.*, para. 7.1351.

⁵⁹²United States' appellant's submission, para. 208.

452. The fourth reason the Panel provided for finding a "causal link"⁵⁹³ was the "divergence between United States producers' total costs of production and revenue from sales of upland cotton since 1997".⁵⁹⁴ The United States argues that the Panel should have examined variable rather than total costs⁵⁹⁵ in assessing whether "United States upland cotton producers would ... have been economically capable of remaining in the production of upland cotton had it not been for the United States subsidies at issue".⁵⁹⁶

453. We agree with the general proposition of the United States that variable costs may play a role in farmers' decision-making as to whether to plant upland cotton or some alternative crop, and how much of each crop to plant. From a short-term perspective, variable costs may be particularly important. However, from a longer-term perspective, total costs may be relevant. Based on the evidence before it regarding upland cotton production in the United States, the Panel concluded that "the six-year period from 1997-2002 ... lends itself to an assessment of the medium- to longer-term examination of developments in the United States upland cotton industry".⁵⁹⁷ The Panel found that "the effect of the subsidies was to allow United States producers to sell upland cotton at a price lower than would otherwise have been necessary to cover their total costs".⁵⁹⁸ In the circumstances of this dispute, we do not consider that the Panel's reliance on total rather than variable costs of production amounts to an error vitiating the Panel's analysis under Article 6.3(c).

454. Finally, we consider the "other causal factors alleged by the United States"⁵⁹⁹ to have had an effect on prices. The United States argues that the Panel erred in addressing upland cotton planting decisions as an "other causal factor", given that the United States maintained that the price-contingent subsidies did not cause price suppression at all.⁶⁰⁰ We disagree. We have already addressed the United States' arguments with respect to planting decisions, and we find no fault in the Panel's consideration of the issue of "planting decisions".⁶⁰¹

⁵⁹³ Panel Report, para. 7.1347.

⁵⁹⁴ *Ibid.*, para. 7.1353. (footnote omitted)

⁵⁹⁵ United States' appellant's submission, para. 215.

⁵⁹⁶ Panel Report, para. 7.1353.

⁵⁹⁷ *Ibid.*, para. 7.1354.

⁵⁹⁸ *Ibid.*, para. 7.1353.

⁵⁹⁹ *Ibid.*, para. 7.1357.

⁶⁰⁰ United States' appellant's submission, para. 138.

⁶⁰¹ *Supra*, paras. 440-445.

455. The United States also argues that United States upland cotton exports increased during 1998-2002⁶⁰² because textile imports increased in the same period, leading to a decline in the use of cotton by domestic mills.⁶⁰³ The Panel regarded this factor as "concerning support, rather than suppression, of world cotton prices".⁶⁰⁴ However, even assuming that increasing textile imports led to increased exports of upland cotton, this does not mean that the price-contingent subsidies did not have the effect of significant price suppression. It was not unreasonable for the Panel to conclude that the "effect" of the price-contingent subsidies was significant price suppression, even if some other factor might also have price-suppressive effects.⁶⁰⁵

456. The remaining three "other causal factors" that the Panel examined were weakness in world demand for upland cotton, the strong United States dollar, and the release by China of government upland cotton stocks between 1999 and 2001.⁶⁰⁶ The United States does not specifically address these three factors in its appellant's submission. However, the Panel's discussion of these "other factors" was part of the reasoning leading to the Panel's conclusion under Article 6.3(c), which the United States does appeal.⁶⁰⁷ The Panel found that the United States' argument that weak demand caused low prices was inconsistent with the increase in United States upland cotton production and the absence of "pronounced declines" in world upland cotton consumption.⁶⁰⁸ With regard to the United States dollar, the Panel stated that exchange rates would affect market prices, but that market prices did not guide "United States producer decisions (except to the extent that, when they are lower than the marketing loan rate, they dictate the magnitude of United States government subsidies to producers)".⁶⁰⁹ The Panel pointed to evidence on the record confirming that marketing loan program payments and Step 2 payments "offset" declines in market prices.⁶¹⁰ With respect to upland cotton stocks released by China, the Panel agreed with the United States (and Brazil) that "an infusion of a large amount of supply onto the market would exert a downward pressure on prices".⁶¹¹ However, the

⁶⁰² The United States also argues that 1998 was an inappropriate base year for the Panel's examination because of unusually weak world demand and reduced United States production due to drought. (United States' appellant's submission, para. 209)

⁶⁰³ United States' appellant's submission, para. 211.

⁶⁰⁴ Panel Report, para. 7.1359.

⁶⁰⁵ In this regard, see *supra*, para. 437 and *infra*, para. 457.

⁶⁰⁶ Panel Report, paras. 7.1358, 7.1360, and 7.1361.

⁶⁰⁷ In appealing this finding, the United States refers in a footnote to paras. 7.1107-7.1416 and 8.1(g)(i) of the Panel Report. (United States' appellant's submission, footnote 531 to para. 516(8))

⁶⁰⁸ Panel Report, para. 7.1358.

⁶⁰⁹ *Ibid.*, para. 7.1360.

⁶¹⁰ *Ibid.*, footnote 1477 to para. 7.1360.

⁶¹¹ *Ibid.*, para. 7.1361.

Panel pointed out that the stock released by the Chinese government "was smaller in magnitude than the United States exports over this period".⁶¹²

457. The Panel concluded:

Although some of these factors may have contributed to lower, and even suppressed, world upland cotton prices during MY 1999-2002, they do not attenuate the genuine and substantial causal link that we have found between the United States mandatory price-contingent subsidies at issue and the significant price suppression. Nor do they reduce the effect of the mandatory price-contingent subsidies to a level which cannot be considered "significant".⁶¹³

In sum, the Panel Report shows that it examined the other factors raised by the United States. Although the Panel found that some of them had price-suppressive effects, it did not attribute those effects to the United States' price-contingent subsidies.

458. Unlike in certain other instances under the WTO agreements, a panel conducting an analysis under Article 6.3(c) of the *SCM Agreement* is the first trier of facts, rather than a reviewer of factual determinations made by a domestic investigating authority. Bearing this in mind, we underline the responsibility of panels in gathering and analyzing relevant factual data and information in assessing claims under Article 6.3(c) in order to arrive at reasoned conclusions. In this case, the voluminous evidentiary record before the Panel included several economic studies, and substantial data and information. For its part, the Panel posed a large number of questions to which the parties submitted detailed answers. Overall, the Panel evidently conducted an extensive analysis, but we believe that, in its reasoning, the Panel could have provided a more detailed explanation of its analysis of the complex facts and economic arguments arising in this dispute. The Panel could have done so in order to demonstrate precisely how it evaluated the different factors bearing on the relationship between the price-contingent subsidies and significant price suppression. Nevertheless, in the light of the Panel's examination of the relevant evidence, coupled with its legal reasoning, we find no legal error in the Panel's causation analysis.

(f) Amount of the Price-Contingent Subsidies

459. In reaching the conclusion that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*, the Panel made the following statements with respect to the amount of the price-contingent subsidies as a whole:

We have readily available information on the record showing us that the price-contingent subsidies in question involve very large amounts of United States government money benefiting United States upland cotton.⁶¹⁴

[W]hile we do not believe that it is strictly necessary [to calculate precisely the amount of the subsidies in question, we observe that we have readily available information on the record showing us that the price-contingent subsidies in question involve very large amounts of United States government money benefiting United States upland cotton production].⁶¹⁵

In addition, the Panel made statements regarding the amount of individual price-contingent subsidies, namely marketing loan program payments and Step 2 payments.⁶¹⁶

460. On appeal, the United States raises several points. First, the United States argues that the Panel was required to quantify the amount of the price-contingent subsidies benefiting upland cotton.⁶¹⁷ Secondly, the United States submits that counter-cyclical and market loss assistance payments to recipients who did not produce upland cotton did not benefit upland cotton at all and therefore could not have caused serious prejudice.⁶¹⁸ As for counter-cyclical and market loss assistance payments to recipients who produced both upland cotton and other products, the Panel should have "allocated [the subsidies] over the total sales of the recipients".⁶¹⁹ Thirdly, the United States maintains that the Panel erred, in its Article 6.3(c) analysis, by failing to identify the amount of benefit flowing to processed cotton from price-contingent subsidies paid to producers of raw cotton.⁶²⁰

461. Beginning with the text of Article 6.3(c), we note that this provision does not state explicitly that a panel needs to quantify the amount of the challenged subsidy. However, in assessing whether "the effect of the subsidy is ... significant price suppression", and ultimately serious prejudice, a panel

⁶¹⁴Panel Report, para. 7.1308.

⁶¹⁵*Ibid.*, para. 7.1349.

⁶¹⁶While we do not believe it is necessary to calculate the precise amount of the subsidies in question, we observe that we have this information readily available on the record. This is a very large amount". (Panel Report, paras. 7.1297 and 7.1300) (footnote omitted)

⁶¹⁷United States' appellant's submission, para. 240. The United States does not contest the Panel's view that, in assessing the price-contingent subsidies under Article 6.3(c), it was not required to quantify precisely the amount of the subsidies benefiting upland cotton. (See United States' appellant's submission, para. 258; Panel Report, paras. 7.1173, 7.1186 and 7.1226) The United States clarified this point in response to questioning during the oral hearing.

⁶¹⁸United States' appellant's submission, para. 242.

⁶¹⁹*Ibid.*, para. 264.

⁶²⁰*Ibid.*, para. 301 and footnote 314 to para. 301. In response to questioning during the oral hearing, the United States confirmed that its appeal regarding "raw" and "processed" cotton relates to all the price-contingent subsidies.

will need to consider the effects of the subsidy on prices. The magnitude of the subsidy is an important factor in this analysis.⁶²¹ A large subsidy that is closely linked to prices of the relevant product is likely to have a greater impact on prices than a small subsidy that is less closely linked to prices. All other things being equal, the smaller the subsidy for a given product, the smaller the degree to which it will affect the costs or revenue of the recipient, and the smaller its likely impact on the prices charged by the recipient for the product. However, the size of a subsidy is only one of the factors that may be relevant to the determination of the effects of a challenged subsidy. A panel needs to assess the effect of the subsidy taking into account all relevant factors.

462. In order for a panel to find that a subsidy has the effect of significant price suppression, or some other effect mentioned in Article 6.3(c), the panel must determine that the payment is a specific subsidy within the meaning of Articles 1 and 2 of the *SCM Agreement*.⁶²² The Panel did so in this dispute⁶²³, and we do not understand the United States to contest this conclusion. Rather, the United States argues that a panel needs to quantify the amount of the "benefit" conferred on the subsidized product by a challenged subsidy.⁶²⁴ However, the definitions of a specific subsidy in Articles 1 and 2 do not expressly require the quantification of the "benefit" conferred by the subsidy on any particular product.

463. Turning to the context of Article 6.3(c), we note that Article 6.1(a)—which has now expired—contains the only reference in Part III of the *SCM Agreement* to a calculation of *ad valorem* subsidization of a product. Footnote 14 to Article 6.1(a) explains that this calculation is to be performed in accordance with Annex IV on the "Calculation of the Total Ad Valorem Subsidization (Paragraph 1(a) of Article 6)". No similar provisions are found in Article 6.3(c), which suggests that no precise quantification is envisaged in that provision.

464. The United States does not argue, as a general matter, that the methodologies in Part V of the *SCM Agreement* apply directly to a serious prejudice analysis under Part III of the *SCM Agreement*.⁶²⁵ However, the United States identifies Part V as providing relevant context for the

⁶²¹*Supra*, para. 432.

⁶²²As the United States points out, the word "subsidy" in Article 6.3(c) is defined in Article 1.1 of the *SCM Agreement*, and the subsidies subject to the disciplines in Part III of the *SCM Agreement* (including Articles 5(c) and 6.3(c)) must be "specific" pursuant to Article 1.2. A "subsidy" as defined in the *SCM Agreement* involves the conferral of a "benefit" under Article 1.1(b). (See United States' appellant's submission, paras. 244 and 245.)

⁶²³Panel Report, paras. 7.1120 and 7.1154.

⁶²⁴United States' appellant's submission, para. 246.

⁶²⁵*Ibid.*, para. 258, as confirmed during the oral hearing.

interpretation of Articles 5(c) and 6.3(c) of the *SCM Agreement*.⁶²⁶ We note that the apparent rationale for Part III differs from that for Part V of the *SCM Agreement*. Under Part V, the amount of the subsidy must be calculated because, under Article 19.4 of the *SCM Agreement* and Article VI:3 of the GATT 1994, countervailing duties cannot be levied in excess of that amount. In contrast, under Part III, the remedy envisaged under Article 7.8 of the *SCM Agreement* is the withdrawal of the subsidy or the removal of the adverse effects. This remedy is not specific to individual companies. Rather, it targets the effects of the subsidy more generally. Article 6.3(c) thus goes in the same vein and does not require a precise quantification of the subsidies at issue.

465. The provisions of the *SCM Agreement* regarding quantification of subsidies reveal that the methodological approaches to quantification may be quite different, depending on the context and purpose of quantification.⁶²⁷ The absence of any indication in Article 6.3(c) as to whether one of these methods, or any other method, should be used suggests to us that no such precise quantification was envisaged as a necessary prerequisite for a panel's analysis under Article 6.3(c).

466. Pursuant to Article 6.8, "the existence of serious prejudice" under Article 6.3(c) "should be determined on the basis of the information submitted to or obtained by the panel, including information submitted in accordance with the provisions of Annex V" of the *SCM Agreement*. The United States is correct that Annex V refers to "information ... as necessary to establish the existence and amount of subsidization" (in paragraph 2) and "data concerning the amount of the subsidy in question" (in paragraph 5)⁶²⁸, but Annex V also refers to other information.⁶²⁹ This demonstrates that the amount of the subsidy, as well as other elements, are relevant for the assessment of whether price suppression exists. But we do not read Annex V as mandating the precise quantification of subsidies in order to determine their effect under Article 6.3(c).

467. In sum, reading Article 6.3(c) in the context of Article 6.8 and Annex V suggests that a panel should have regard to the magnitude of the challenged subsidy and its relationship to prices of the product in the relevant market when analyzing whether the effect of a subsidy is significant price

⁶²⁶United States' appellant's submission, para. 260.

⁶²⁷In relation to countervailing duties, Article 19.4 of the *SCM Agreement* specifies that the amount of the subsidy is to be "calculated in terms of subsidization per unit of the subsidized and exported product". Article 14 of the *SCM Agreement* adds that this calculation is to be done "in terms of the benefit to the recipient". In contrast, under Article 6.1(a) and paragraph 1 of Annex IV of the *SCM Agreement*, which relate to a claim of serious prejudice as mentioned above, the "total ad valorem subsidization of a product" is to be calculated "in terms of the cost to the granting government". (footnote omitted)

⁶²⁸United States' appellant's submission, paras. 247-252.

⁶²⁹For example, paragraph 3 of Annex V refers to information such as "customs data concerning imports and declared values of the products concerned". Paragraph 5 of Annex V refers to information such as "prices of the subsidized product, prices of the non-subsidized product, prices of other suppliers to the market, changes in the supply of the subsidized product to the market in question and changes in market shares".

suppression. In many cases, it may be difficult to decide this question in the absence of such an assessment. Nevertheless, this does not mean that Article 6.3(c) imposes an obligation on panels to quantify precisely the amount of a subsidy benefiting the product at issue in every case. A precise, definitive quantification of the subsidy is not required.

468. In the present case, the Panel could have been more explicit and specified what it meant by "very large amounts"⁶³⁰, beyond including cross-references to its earlier findings regarding certain subsidies. Nevertheless, the information before the Panel clearly supports the Panel's general statements regarding the magnitude of the price-contingent subsidies.⁶³¹

469. In addition to its arguments regarding quantification, the United States contends that the Panel should have used an allocation methodology to determine the amount of "decoupled" market loss assistance payments and counter-cyclical payments that benefits a given product. It argues that Annex IV of the *SCM Agreement* contains an "economically neutral"⁶³² allocation methodology agreed by WTO Members, pursuant to which "the subsidy would be allocated to the product according to the ratio of sales of that product to the total value of the recipient firm's sales".⁶³³ It is clear that use of the Annex IV methodology is not expressly *required* by Article 6.3(c). We also observe that the Panel described as "appropriate"⁶³⁴ certain alternative allocation methodologies to the one it relied upon that sought to reduce the amount of payments with respect to upland cotton base acres within the base acre dependent programs to account only for payments corresponding to acres that were actually planted with upland cotton.⁶³⁵ In our view, even using these alternative allocation methodologies for market loss assistance payments and counter-cyclical payments, the Panel's conclusion regarding the order of magnitude of the price-contingent subsidies stands.⁶³⁶

470. Finally, we address the related United States argument that the Panel failed to determine the extent to which the "benefit" of price-contingent subsidies paid to producers of "raw" cotton flowed through to "processed" cotton. We note that the Panel seemed to regard market loss assistance payments and counter-cyclical payments as benefiting the production of upland cotton lint.⁶³⁷ As for

⁶³⁰*Supra*, para. 459.

⁶³¹Panel Report, paras. 7.596 and 7.641; United States' response to questions posed by the Panel (Panel Report, p. I-126, para. 211).

⁶³²United States' appellant's submission, para. 269.

⁶³³*Ibid.*, para. 268.

⁶³⁴Panel Report, para. 7.646.

⁶³⁵*Ibid.*, "Attachment to Section VII:D", paras. 7.634-7.647.

⁶³⁶Table 3 of Annex 2.

⁶³⁷Panel Report, para. 7.1226 and footnote 258 to para. 7.197. See *supra*, para. 407 and footnote 451.

marketing loan program payments and Step 2 payments, the Panel suggested that it is a condition of eligibility for these payments that harvested cotton containing cotton lint and cottonseed "be baled" and/or "ginned".⁶³⁸

471. The United States contends that the Appellate Body's reasoning in *US – Softwood Lumber IV* indicates that it cannot be presumed that a "subsidy", as defined in Article 1.1 of the *SCM Agreement*, provided to a producer of an input (such as raw cotton) "passes through" to the producer of the processed product (in this case, upland cotton lint).⁶³⁹ However, the Appellate Body's reasoning in that dispute focuses not on the requirements for establishing serious prejudice under Articles 5(c) and 6.3(c) of the *SCM Agreement*, but on the conduct of countervailing duty investigations pursuant to Part V of the *SCM Agreement*.⁶⁴⁰

472. As we have already noted⁶⁴¹, the requirement in Article VI:3 of the GATT 1994 and Article 19.4 of the *SCM Agreement* that countervailing duties on a product be limited to the amount of the subsidy accruing to that product finds no parallel in the provisions on actionable subsidies and pertinent remedies under Part III of the *SCM Agreement*. Therefore, the need for a "pass-through" analysis under Part V of the *SCM Agreement* is not critical for an assessment of significant price suppression under Article 6.3(c) in Part III of the *SCM Agreement*. Nevertheless, we acknowledge that the "subsidized product" must be properly identified for purposes of significant price suppression under Article 6.3(c) of the *SCM Agreement*. And if the challenged payments do not, in fact, subsidize that product, this may undermine the conclusion that the effect of the subsidy is significant suppression of prices of that product in the relevant market.

473. For these reasons, we find that the Panel did not err in its assessment of the amount of the subsidies for the purpose of its analysis under Article 6.3(c) of the *SCM Agreement*.

⁶³⁸Panel Report, footnote 258 to para. 7.197. See also *ibid.*, footnotes 1339 and 1340 to para. 7.1225.

⁶³⁹United States' appellant's submission, paras. 304 and 305 (quoting Appellate Body Report, *US – Softwood Lumber IV*, para. 142).

⁶⁴⁰Appellate Body Report, *US – Softwood Lumber IV*, paras. 140-142. The Appellate Body there addressed the need for authorities to ensure that the subsidy at issue confers a benefit on the product against which countervailing duties are to be imposed (pursuant to Article 1.1 of the *SCM Agreement*) and that those duties do not exceed the total amount of the subsidy accruing to that product (pursuant to Article VI:3 of the GATT 1994). The facts in that case are also quite different from those in the present dispute. In *US – Softwood Lumber IV*, it was undisputed that lumber is a distinct product from trees or logs, and countervailing duties were imposed on exported lumber and not on trees or logs. (Appellate Body Report, *US – Softwood Lumber IV*, para. 124) In contrast, in the present dispute, no such clear distinction exists between cotton lint and "raw cotton", meaning (presumably) harvested cotton containing cottonseed and cotton lint.

⁶⁴¹*Supra*, para. 464.

(g) Effect of the Price-Contingent Subsidies Over Time

474. The United States asserts that the Panel erred in making serious prejudice findings with respect to the price-contingent subsidies provided in marketing years 1999 to 2001.⁶⁴² According to the United States, a "recurring" subsidy payment does not confer a benefit after the year for which it is paid, and therefore it is no longer a "subsidy" under Article 1 of the *SCM Agreement*. A subsidy that is paid annually must be "allocated" or "expensed"⁶⁴³ to the year "for which the payment is made"⁶⁴⁴, and the effect of such a payment cannot be "significant price suppression" in any other year. The price-contingent subsidies "are made annually with respect to a particular marketing year"⁶⁴⁵, and therefore the effect of those subsidies cannot extend to any later marketing year. In any case, the United States argues that the Panel did not find that these subsidy payments had "continuing effects".⁶⁴⁶ The Panel was established in marketing year 2002⁶⁴⁷ and, therefore, the Panel could not have found that the effect of the price-contingent subsidies for marketing years 1999 to 2001 is significant price suppression.⁶⁴⁸

475. We observe that the United States' contention that the effect of a subsidy must be "allocated" or "expensed" to the year in which it is paid is confined to "recurring" subsidies, that is, subsidies paid on an annual basis. The United States acknowledges that "non-recurring" subsidies could be "allocated" to subsequent years as well. Article 6.3(c) of the *SCM Agreement* applies to a subsidy whether it is "recurring" or "non-recurring". This Article does not suggest that the effect of a subsidy is limited to or continues only for a specified period of time.

476. In this appeal, we are asked to address the limited question of whether the effect of a subsidy may continue beyond the year in which it was paid, in the context of a significant price suppression analysis under Article 6.3(c) of the *SCM Agreement*. Whether the effect of a subsidy begins and

⁶⁴²See *supra*, para. 422(c). "Because the recurring subsidies provided in each of marketing years 1999, 2000, and 2001 ceased to exist when the benefit was used up for production in those years, the effect of those subsidies cannot be the subject of subsidies claims in marketing year 2002." (United States' appellant's submission, para. 284)

⁶⁴³United States' appellant's submission, para. 284.

⁶⁴⁴The United States argues that "recurring" subsidies should be "allocated ... to the marketing year to which they relate". (United States' appellant's submission, para. 275) In response to questioning during the oral hearing, the United States clarified that when it refers to the year to which a subsidy *relates* it means "the year for which the payment is made".

⁶⁴⁵United States' appellant's submission, para. 291.

⁶⁴⁶*Ibid.*, para. 278.

⁶⁴⁷The DSB established the Panel on 18 March 2003. (WT/DS267/15; Panel Report, para. 1.2) "The date on which the Panel was established fell during the 2002 marketing year for upland cotton in the United States, which began on 1 August 2002 and ended on 31 July 2003." (Panel Report, para. 7.185)

⁶⁴⁸United States' appellant's submission, para. 278.

expires in the year in which it is paid or begins in one year and continues in any subsequent year, and how long a subsidy can be regarded as having effects, are fact-specific questions. The answers to these questions may depend on the nature of the subsidy and the product in question. We see nothing in the text of Article 6.3(c) that excludes *a priori* the possibility that the effect of a "recurring" subsidy may continue after the year in which it is paid. Article 6.3(c) deals with the "effect" of a subsidy, and not with the financial accounting of the amount of the subsidy.⁶⁴⁹

477. The context of Article 6.3(c) within Part III of the *SCM Agreement* does not support the suggestion that the effect of a subsidy is immediate, short-lived, or limited to one year, regardless of whether or not it is paid every year. Article 6.2 of the *SCM Agreement* refers to the possibility of the subsidizing Member demonstrating that "the subsidy in question *has not resulted* in any of the effects enumerated in paragraph 3".⁶⁵⁰ (emphasis added) The word "resulted" in this sentence highlights the temporal relationship between the subsidy and the effect, in that one might expect a time lag between the provision of the subsidy and the resulting effect.⁶⁵¹ In addition, the use of the present perfect tense in this provision implies that some time may have passed between the granting of the subsidy and the demonstration of the absence of its effects.⁶⁵²

478. Article 6.4 of the *SCM Agreement* is also relevant context for interpreting Article 6.3(c). Article 6.4 requires that the displacement or impeding of exports be demonstrated "over an appropriately representative period", which "shall be at least one year", so that "clear trends" in changes in market share can be demonstrated.⁶⁵³ This suggests that the effect of a subsidy under Article 6.4 must be examined over a sufficiently long period of time and is not limited to the year in which it was paid. As the Panel has also pointed out in the context of Article 6.3(c), "[c]onsideration

⁶⁴⁹Although the accounting treatment of a subsidy may be relevant, it does not control the assessment of the effect of the subsidy under Article 6.3(c).

⁶⁵⁰The French version of Article 6.2 states that "la subvention ... n'a eu aucun des effets énumérés au paragraphe 3". The Spanish version of Article 6.2 states "la subvención en cuestión no ha producido ninguno de los efectos enumerados en el párrafo 3".

⁶⁵¹The Spanish version of Article 6.2 uses the word "producido" for "resulted", again suggesting a time lag between the provision of the subsidy and the resulting effect. The French version of Article 6.2 uses a more neutral term, "eu", which includes but perhaps does not emphasize this temporal connotation as strongly. See *supra*, footnote 650.

⁶⁵²The French and Spanish versions of Article 6.2 also use the present perfect tense. See *supra*, footnote 650.

⁶⁵³Article 6.4 reads in relevant part:

[T]he displacement or impeding of exports shall include any case in which ... it has been demonstrated that there has been a *change* in relative shares of the market to the disadvantage of the non-subsidized like product (*over an appropriately representative period* sufficient to demonstrate clear *trends* in the development in the market for the product concerned, which, in normal circumstances, shall be *at least one year*). ... (emphasis added)

of developments over a period of longer than one year ... provides a more robust basis for a serious prejudice evaluation than merely paying attention to developments in a single recent year".⁶⁵⁴

479. The United States supports its arguments regarding the "allocation" of "recurring" and "non-recurring" subsidies by referring to several sources.⁶⁵⁵ The United States submits that "the Appellate Body has acknowledged that 'non-recurring' subsidies may be allocated over time"⁶⁵⁶, citing the following statement of the Appellate Body in *US – Lead and Bismuth II*:

[W]e agree with the Panel that while an investigating authority may presume, in the context of an administrative review under Article 21.2, that a "benefit" continues to flow from an untied, non-recurring "financial contribution", this presumption can never be "irrebuttable".⁶⁵⁷

In our view, this statement does not support the United States' argument. A proper reading of this statement reveals that it was made in the context of Part V of the *SCM Agreement*, and it focuses on the *benefit* flowing from a "non-recurring" financial contribution rather than the *effect* of a subsidy. Indeed, the Appellate Body's conclusion that investigating authorities cannot adopt an irrebuttable presumption that a benefit continues to flow from certain non-recurring financial contributions highlights the importance of examining the particular characteristics of a given subsidy in evaluating its impact.

480. In addition, the United States refers to paragraph 7 of Annex IV to the *SCM Agreement*⁶⁵⁸, which provides that "[s]ubsidies granted prior to the entry into force of the WTO Agreement, the benefits of which are allocated to future production, shall be included in the overall rate of subsidization." Although this provision recognizes that the benefits of some subsidies may be allocated to future production, it does not specify that this applies exclusively to "non-recurring"

⁶⁵⁴Panel Report, para. 7.1199.

⁶⁵⁵United States' appellant's submission, paras. 282 and 283, citing: *SCM Agreement*, paragraph 7 of Annex IV; Guidelines on Amortization and Depreciation adopted by the Tokyo Round Committee on Subsidies and Countervailing Measures, SCM/64, BISD 32S/154 (25 April 1985), para. 1; *Anti-Dumping Agreement*, Article 2.2.1.1; Appellate Body Report, *US – Lead and Bismuth II*, para. 62; Report by the Informal Group of Experts to the Committee on Subsidies and Countervailing Measures, G/SCM/W/415/Rev.2 (15 May 1998), Recommendation 1 and paras. 1-12.

⁶⁵⁶United States' appellant's submission, para. 283.

⁶⁵⁷Appellate Body Report, *US – Lead and Bismuth II*, para. 62.

⁶⁵⁸The title of Annex IV of the *SCM Agreement* is "Calculation of the Total Ad Valorem Subsidization (Paragraph 1(a) of Article 6)". (footnote omitted)

subsidies. In any event, as the Panel noted, the "effect" of a subsidy cannot be equated with the "benefit" of a subsidy.⁶⁵⁹

481. The United States also points to Article 2.2.1.1 of the *Anti-Dumping Agreement*, which relates to the calculation of costs in constructing a normal value under Article 2.2, in order to calculate a dumping margin in certain circumstances. Article 2.2.1.1 states, in relevant part, that "costs shall be adjusted appropriately for those non-recurring items of cost which benefit future and/or current production". However, this provision pertains to the method of calculation of producers' costs in constructing the normal value of a product, which is a different inquiry. It does not apply in assessing the effect of a subsidy under Article 6.3(c) of the *SCM Agreement*.

482. For these reasons, we are not persuaded by the United States' contention that the effect of annually paid subsidies must be "allocated" or "expensed" solely to the year in which they are paid and that, therefore, the effect of such subsidies cannot be significant price suppression in any subsequent year. We do not agree with the proposition that, if subsidies are paid annually, their effects are also necessarily extinguished annually.

483. Turning to the effect of the subsidies at issue in this appeal, we note that the Panel found that the effect of the price-contingent subsidies for marketing years 1999 to 2002⁶⁶⁰ "is significant price suppression ... in the period MY 1999-2002".⁶⁶¹ The Panel did not specify which subsidies had effects in which years; nor did it specifically state that the effect of the subsidies for marketing years 1999-2001 was significant price suppression in marketing year 2002. This is consistent with the Panel's earlier statement regarding the way in which it would conduct its analysis:

[I]n our price suppression analysis under Article 6.3(c), we examine one effects-related variable – prices – and one subsidized product – upland cotton. To the extent a sufficient nexus with these exists among the subsidies at issue so that their effects manifest themselves collectively, we believe that we may legitimately treat them as a "subsidy" and group them and their effects together.⁶⁶²

484. For this reason, the Panel examined the price-contingent subsidies for marketing years 1999 to 2002 as a group⁶⁶³, and its finding of significant price suppression in marketing years 1999 to

⁶⁵⁹Panel Report, para. 7.1179.

⁶⁶⁰*Ibid.*, para. 7.1108.

⁶⁶¹*Ibid.*, para. 7.1416. Before the Panel, Brazil also claimed that United States subsidies to be granted from marketing year 2003 to marketing year 2007 threaten to cause serious prejudice to Brazil's interests. (*Ibid.*, para. 7.1478) However, the payments to be made in marketing years 2003-2007 and the issue of *threat* of serious prejudice under the *SCM Agreement* do not form part of this appeal.

⁶⁶²*Ibid.*, para. 7.1192.

⁶⁶³Panel Report, para. 7.1290.

2002⁶⁶⁴ applied to this group of subsidies. As we noted above, the effects of a "recurring" subsidy may continue after the year in which it is paid.⁶⁶⁵ Given that the Panel found significant price suppression in the period 1999 to 2002 as a whole, and this period includes the marketing year 2002, we are unable to agree with the United States' assertion that the Panel erred in not making a specific finding that the price-contingent subsidies for marketing years 1999 to 2001 "had continuing effects at the time of panel establishment".⁶⁶⁶

6. Serious Prejudice under Article 5(c) of the SCM Agreement

485. Having found that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*⁶⁶⁷, the Panel then considered whether the United States had caused adverse effects in the form of serious prejudice to the interests of Brazil through the use of these subsidies, contrary to Article 5(c) of the *SCM Agreement*. The Panel found that the significant price suppression it had found under Article 6.3(c) of the *SCM Agreement* amounted to serious prejudice within the meaning of the Article 5(c) of the *SCM Agreement*⁶⁶⁸, based on the following findings:

[A]n affirmative conclusion that the effects-based situation in Article 6.3(c) exists is a sufficient basis for an affirmative conclusion that "serious prejudice" exists for the purposes of Article 5(c) of the *SCM Agreement*.⁶⁶⁹

[A]ssuming *arguendo* that any sort of additional demonstration is necessary to establish that the "significant price suppression" we have found to exist in the same world market constitutes prejudice amounting to "serious prejudice" within the meaning of Article 5(c), ... Brazil has also fulfilled that burden.⁶⁷⁰

486. Thus, the Panel provided two alternative reasons for finding that the significant price suppression it had found amounted to serious prejudice within the meaning of the Article 5(c) of the *SCM Agreement*.⁶⁷¹ The Panel's primary reason was that if the effect of a subsidy is significant price suppression within the meaning of Article 6.3(c), this is sufficient, without more, to conclude that the

⁶⁶⁴ *Ibid.*, para. 7.1416.

⁶⁶⁵ *Supra*, para. 482.

⁶⁶⁶ United States' appellant's submission, para. 278.

⁶⁶⁷ Panel Report, paras. 7.1355-7.1356 and 7.1363.

⁶⁶⁸ *Ibid.*, paras. 7.1395 and 8.1(g)(i).

⁶⁶⁹ *Ibid.*, para. 7.1390.

⁶⁷⁰ *Ibid.*, para. 7.1391.

⁶⁷¹ Panel Report, paras. 7.1395 and 8.1(g)(i).

subsidizing Member has caused serious prejudice to the interests of another Member within the meaning of Article 5(c).⁶⁷² The Panel's alternative reason was that, even if this is not sufficient, Brazil had fulfilled the burden of demonstrating that the United States had caused serious prejudice to the interests of Brazil within the meaning of Article 5(c).⁶⁷³

487. In its Notice of Appeal, and in the "Conclusion" section of its Appellant's Submission, the United States challenged the Panel's finding "that 'significant price suppression' is sufficient to establish 'serious prejudice' for purposes of Articles 5(c) and 6.3 of the SCM Agreement".⁶⁷⁴ Brazil asks us to dismiss this claim because the United States did "not appear to have advanced arguments in its Appellant's Submission" in relation to it.⁶⁷⁵ In response to questioning during the oral hearing, the United States clarified that, in its Notice of Appeal, it intended to challenge only the first of the two findings mentioned above (that is, the Panel's finding in paragraph 7.1390 of the Panel Report). However, the United States indicated that it did not pursue this claim in its appellant's submission.

488. As neither party has appealed the Panel's finding in paragraph 7.1390 of the Panel Report (regarding the sufficiency of a finding of an effect under Article 6.3(c) for a finding of serious prejudice under Article 5(c), in general terms) or the Panel's alternative finding in paragraph 7.1391 of the Panel Report (regarding serious prejudice to the interests of Brazil in the particular circumstances of this dispute), we express no opinion on either of those findings. Nor do we address the Panel's consequential finding that the significant price suppression that it had found to be the effect of the price-contingent subsidies under Article 6.3(c) of the *SCM Agreement* amounted to serious prejudice within the meaning of Article 5(c) of the *SCM Agreement*.⁶⁷⁶ Accordingly, upon adoption of the Panel Report by the DSB, the Panel's findings in paragraphs 7.1390 and 7.1391 of the Panel Report as mentioned above⁶⁷⁷ would stand, without endorsement or rejection by the Appellate Body.

7. Basic Rationale under Article 12.7 of the DSU

489. The United States contends that, contrary to Article 12.7 of the DSU, the Panel failed to set out the basic rationale behind its finding that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*. Article 12.7 of the

⁶⁷² *Ibid.*, para. 7.1390.

⁶⁷³ *Ibid.*, para. 7.1391.

⁶⁷⁴ United States' Notice of Appeal (WT/DS267/17, 18 October 2004, attached as Annex 1 to this Report), para. 8(i); United States' appellant's submission, para. 516(8)(i).

⁶⁷⁵ Brazil's appellee's submission, para. 1084.

⁶⁷⁶ Panel Report, paras. 7.1395 and 8.1(g)(i).

⁶⁷⁷ *Supra*, para. 485.

DSU requires a panel to set out in its report "the findings of fact, the applicability of relevant provisions and the basic rationale behind any findings and recommendations that it makes".

490. The United States submits that the Panel "provided no explanation of what degree of price suppression it had found to be 'significant'."⁶⁷⁸ In fact, the Panel based its reasoning in this regard on the ordinary meaning of "significant"⁶⁷⁹, explaining that the "significance" of price suppression could, depending on the circumstances, have both quantitative and qualitative aspects.⁶⁸⁰ We find that the Panel adequately explained the basis for its conclusion that the price suppression it had found was "significant" with the meaning of Article 6.3(c).⁶⁸¹ We therefore see no failure on the part of the Panel to comply with Article 12.7 of the DSU in this regard.

491. The United States also argues that the Panel "failed to set out the basic rationale behind its findings and recommendations ... with respect to the amount of the subsidy".⁶⁸² We have already held that the Panel did not err in interpreting or applying Article 6.3(c) of the *SCM Agreement* in relation to the amount of the challenged subsidies.⁶⁸³ In addition, we note that the Panel articulated a basic rationale for its conclusions in this regard.⁶⁸⁴ Accordingly, we decline to find an error on the part of the Panel under Article 12.7 of the DSU.

492. In addition, the United States contends that, contrary to Article 12.7 of the DSU, the Panel failed to set out the basic rationale behind several steps in its reasoning leading to the conclusion that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*. The United States contends that the Panel "prejudged ... the outcome of its causation analysis" in making its finding of price suppression⁶⁸⁵ and that the Panel

⁶⁷⁸United States' appellant's submission, para. 330.

⁶⁷⁹Panel Report, para. 7.1325 (referring to *The New Shorter Oxford English Dictionary* (1993)).

⁶⁸⁰The 'significance' of any degree of price suppression ... may not solely depend upon a given level of numeric significance". (Panel Report, para. 7.1329)

⁶⁸¹Panel Report, paras. 7.1316-7.1333.

⁶⁸²United States' appellant's submission, para. 326.

⁶⁸³*Supra*, para. 473.

⁶⁸⁴Panel Report, paras. 7.1166-7.1190. In assessing the need to quantify the benefit conferred on upland cotton by the subsidies at issue, the Panel compared the specific provisions in Parts III and V of the *SCM Agreement*, as well as certain aspects of Articles VI and XVI of the GATT 1994. It highlighted the different remedies contained in the provisions of Part III and V and the rationale behind these different parts. The Panel identified the specific arguments of the United States that it was addressing as well as the relevant Appellate Body pronouncements. The Panel's basic rationale for deciding that it need not quantify precisely the benefit conferred on upland cotton by the subsidies at issue appears to have been that "the more precise quantitative concepts and methodologies found in Part V of the *SCM Agreement* are not directly applicable in our examination of Brazil's actionable subsidy claims under Part III of the *SCM Agreement*". (Panel Report, para. 7.1167)

⁶⁸⁵United States' appellant's submission, para. 325.

"never explained why it did not analyze the farmer's planting decision and the use of expected prices".⁶⁸⁶ In the present dispute, the Panel set out the basic rationale for its findings on "significant price suppression" and the "causal link" with the price-contingent subsidies.⁶⁸⁷ As we have already explained, the Panel did address the "planting decision" and "expected prices"⁶⁸⁸, and the overlap between different sections of the Panel's analysis stemmed in part from the elements that constitute "price suppression" under Article 6.3(c).⁶⁸⁹

493. In its appellant's submission, the United States argues that the Panel failed to comply with Article 12.7 of the DSU, *inter alia*, in making its findings as to: (i) "why the processed cotton was a 'subsidized product' and why [the Panel] could assume that all of the subsidies paid to cotton producers for raw cotton passed through to the processor"⁶⁹⁰, and (ii) "why any price suppression that it found meant that there was serious prejudice to the interests of Brazil".⁶⁹¹

494. However, paragraph 10 of the United States' Notice of Appeal (which contains the United States' allegations in connection with Article 12.7 of the DSU) does not refer to the "subsidized product", "pass through", or "serious prejudice". Nor does the general statement in paragraph 10 of the issues covered in the United States' claim under Article 12.7 of the DSU appear to extend to these two findings.⁶⁹²

495. We acknowledge that the wording of paragraph 10 of the United States' Notice of Appeal (and, in particular, the use of the words "for example") suggests that the findings listed in this paragraph are simply *examples* of findings challenged in connection with Article 12.7 of the DSU, and that the United States' claim of error under Article 12.7 extends to other Panel findings. In other words, paragraph 10 purports to provide an illustrative rather than exhaustive list of the findings that the United States intends to challenge under Article 12.7 of the DSU. However, the fact that paragraph 10 purports to provide an illustrative list is not conclusive as to whether the Notice of

⁶⁸⁶*Ibid.*, para. 324.

⁶⁸⁷Panel Report, paras. 7.1275-7.1363. The Panel referred to and addressed a great deal of factual evidence provided by the parties. The Panel also clearly identified the provisions of the covered agreements that it considered relevant to this issue and gave detailed explanations for its conclusions at each step.

⁶⁸⁸*Supra*, para. 441.

⁶⁸⁹*Supra*, para. 433.

⁶⁹⁰United States' appellant's submission, para. 328.

⁶⁹¹*Ibid.*, para. 329.

⁶⁹²It could be argued that the "pass-through" issue is encompassed in the reference to "the amount of the challenged subsidies" in paragraph 10. However, if the United States wished to include this issue in its claim of error under Article 12.7, as described in paragraph 10 of the Notice of Appeal, one might have expected it to do so more explicitly, given that a substantive claim of error regarding the need for a "pass-through" analysis is raised specifically in paragraph 8(d) of the Notice of Appeal in respect of the issues appealed regarding "serious prejudice".

Appeal contains a sufficient reference to the Panel's findings described in paragraph 493 above for us to conclude that these findings are included in the United States' appeal. The significance of terms such as "for example" is likely to depend on the particular claim in question and the particular context in which the term is used in a given appeal. In our view, the United States' Notice of Appeal did not provide adequate notice to Brazil, as contemplated by Rule 20(2) of the *Working Procedures for Appellate Review* (the "*Working Procedures*")⁶⁹³, that the United States intended to make a claim of error under Article 12.7 of the DSU with respect to the Panel's findings described in paragraph 493 above. We therefore decline to rule on these findings in connection with Article 12.7 of the DSU.

8. Conclusion

496. For these reasons, the United States has not persuaded us that the Panel committed a legal error in interpreting the relevant legal requirements of Article 6.3(c) or in applying its interpretation to the facts of this case. We therefore *uphold* the Panel's finding, in paragraphs 7.1416 and 8.1(g)(i) of the Panel Report, that the effect of marketing loan program payments, Step 2 payments, market loss assistance payments, and counter-cyclical payments is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*.⁶⁹⁴ We also find that the Panel set out the findings of fact, the applicability of relevant provisions, and the basic rationale behind this finding, as required by Article 12.7 of the DSU.

B. *World Market Share under Article 6.3(d) of the SCM Agreement*

1. Introduction

497. In addition to its claim that it had suffered serious prejudice resulting from price suppression under Article 6.3(c) of the *SCM Agreement*, Brazil also made claims before the Panel alleging that the effect of the challenged subsidies was serious prejudice resulting from an increase in the United States' world market share in upland cotton under Article 6.3(d) of that Agreement.⁶⁹⁵ The principal disagreement between the parties regarding the application of Article 6.3(d) related to the meaning of the phrase contained therein, "world market share". Brazil submitted that this phrase meant "a Member's share of the world market for exports"⁶⁹⁶, and put forward evidence regarding increases in

⁶⁹³See *supra*, footnote 18.

⁶⁹⁴See *supra*, para. 488.

⁶⁹⁵The Panel listed the following as subsidies at issue for purposes of Brazil's claim under Article 6.3(d) of the *SCM Agreement*: "user marketing (Step 2) payments to domestic users and exporters; marketing loan programme payments; [production flexibility contract] payments; [market loss assistance] payments; [direct payments; [counter-cyclical] payments; crop insurance payments; and cottonseed payments". (Panel Report, para. 7.1418) (footnote omitted)

⁶⁹⁶Panel Report, para. 7.1424. (footnote omitted)

the United States' share of the world market for exports of upland cotton. The United States contended that the United States' share of the "world market" for upland cotton encompassed all consumption of all upland cotton, including consumption by a country of its own cotton production.⁶⁹⁷

498. The Panel rejected Brazil's contention that the "world market share" referred to in Article 6.3(d) was limited to the world market for exports.⁶⁹⁸ The Panel also rejected the United States' argument that "world market share" focuses on a Member's share of consumption, based largely upon an interpretation of the object and purpose of subsidies disciplines⁶⁹⁹ and logical inconsistencies in the United States' arguments.⁷⁰⁰ Instead, the Panel reached the view that:

... the phrase "world market share" of the subsidizing Member in Article 6.3(d) of the *SCM Agreement* refers to share of the world market supplied by the subsidizing Member of the product concerned.⁷⁰¹

499. In view of the fact that the evidence and argumentation submitted by Brazil "focused exclusively upon a different, and in [the Panel's] view erroneous, legal interpretation of the phrase 'world market share' in Article 6.3(d)", the Panel found that "Brazil has not established a *prima facie* case of violation of Article 6.3(d) or Article 5(c) of the *SCM Agreement*".⁷⁰²

500. Brazil appeals the Panel's finding that it failed to make a *prima facie* case of violation under Article 6.3(d) (and Article 5(c)) of the *SCM Agreement*. Its appeal has two sequential elements. First, Brazil appeals the Panel's legal interpretation of Article 6.3(d). Brazil stresses that its appeal regarding the Panel's legal interpretation of the phrase "world market share" is *not conditional*.⁷⁰³ Brazil suggests that the text of Article 6.3(d) is silent on the question of whether "world market share" refers to world market share of *exports* or world market share of something else.⁷⁰⁴ However, the use of the word "*trade*" in footnote 17 to Article 6.3(d) (in the context of "multilaterally agreed specific rules apply to the trade in the product or commodity") suggests that the focus of the provision is upon a Member's share of world *trade* in a product, which requires a focus on *exports*, not

⁶⁹⁷*Ibid.*, para. 7.1425.

⁶⁹⁸*Ibid.*, paras. 7.1438-7.1450, and 7.1455-7.1463.

⁶⁹⁹*Ibid.*, paras. 7.1451-7.1453.

⁷⁰⁰*Ibid.*, footnote 1527 to para. 7.1451.

⁷⁰¹*Ibid.*, para. 7.1464. (underlining added)

⁷⁰²*Ibid.*, para. 7.1465. (footnote omitted)

⁷⁰³Brazil's other appellant's submission, para. 264.

⁷⁰⁴*Ibid.*, para. 275.

production, as the Panel found.⁷⁰⁵ Brazil argues that Article XVI:3 of the GATT 1994 addresses a Member's "share of world export trade" and that structural similarities between Article XVI:3 and Article 6.3(d) require the phrase "world market share" in the latter provision to be read in the same way.⁷⁰⁶ Brazil also points to the context provided by paragraphs (a) and (b) of Article 6.3, as well as Articles 6.4 and 6.7, and argues that the focus of a serious prejudice analysis under Article 6.3 is on the effects of the subsidies on like products from the complaining Member.⁷⁰⁷ In addition, Brazil argues that the Panel's reasoning subverts the object and purpose of the *SCM Agreement*, which is to reduce trade distortions caused by subsidies. The Panel's reading denies any remedy to countries that lose market share to subsidized products.⁷⁰⁸

501. Secondly, Brazil requests us to complete the analysis of its claim of serious prejudice under Article 6.3(d). Brazil makes this element of its appeal *conditional* upon us reversing the Panel's findings that United States price-contingent subsidies⁷⁰⁹ caused significant price suppression in terms of Article 6.3(c) of the *SCM Agreement*. Brazil submits that findings by the Panel and undisputed facts on the record would allow us to complete the analysis and find a violation of Article 6.3(d) by the United States.⁷¹⁰

502. The United States counters that the Panel was correct to reject the Brazilian interpretation that "world market share" in Article 6.3(d) means "world market share of exports". The Panel correctly reasoned that nothing in the ordinary meaning of "world market share" suggests that it should not include the domestic market of the Member concerned.⁷¹¹ The United States recalls that the Panel distinguished between Article 6.3(d) (which deals with "world market share") and Article XVI:3 of GATT 1994 (which deals with "share of world export trade") and suggests that the distinct choice of words reflected in these provisions contains important context to suggest that the coverage of Article 6.3(d) is different from that of Article XVI:3.⁷¹² The United States rebuts Brazil's arguments

⁷⁰⁵Brazil's other appellant's submission, paras. 276-277.

⁷⁰⁶*Ibid.*, paras. 275-280.

⁷⁰⁷*Ibid.*, paras. 281-288.

⁷⁰⁸*Ibid.*, paras. 289-294.

⁷⁰⁹That is, marketing loan program payments, Step 2 payments, market loss assistance payments and counter-cyclical payments.

⁷¹⁰Brazil's other appellant's submission, paras. 296-315.

⁷¹¹Indeed (and although the United States does not appeal this point), the United States stresses that the Panel's interpretation that the focus in the phrase "world market share" is upon production is too narrow, because it focuses only on *supply* in the world "market" and not upon *demand*. A correct interpretation would take into account demand—that is *consumption*—as well. On this basis, the focus in Article 6.3(d) is not upon a share of the world's supply or production, but rather upon total *sales*. (United States' appellee's submission, paras. 148-152)

⁷¹²United States' appellee's submission, para. 153.

regarding footnote 17 to Article 6.3(d) by stressing that the term "trade" in the footnote does not purport to limit the scope of the otherwise broad term "world market share" in the text of Article 6.3(d) itself.⁷¹³ Other elements of the context in which Article 6.3(d) appears, such as paragraphs (a) and (b) of Article 6.3 and Articles 6.4 and 6.7 of the *SCM Agreement*, explicitly limit the aspects of the market that they address. This contrasts with Article 6.3(d), which focuses only upon the general concept "world market share". The United States also contests Brazil's view that the Panel's interpretation of Article 6.3(d) reduces the provision to inutility.⁷¹⁴ With respect to Brazil's conditional request to complete the analysis, the United States submits that, even if the Appellate Body accepts Brazil's arguments with respect to the interpretation of Article 6.3(d), there are insufficient facts available for the Appellate Body to complete the analysis of Brazil's claim on this matter. The United States observes that the Panel did not undertake an analysis regarding a causal link between the subsidies at issue and an increase in the United States' world market share of exports in upland cotton, and that the causation analysis regarding price suppression under 6.3(c) could not be transposed into an analysis of world market share under Article 6.3(d).⁷¹⁵

503. Benin and Chad, third participants in this appeal, support Brazil's interpretation of the phrase "world market share" in Article 6.3(d) of the *SCM Agreement*.⁷¹⁶ Benin and Chad argue that, in the event we agree with Brazil that "world market share" refers to a Member's share of world exports, then we should complete the analysis. In the view of Benin and Chad, the undisputed evidence on record demonstrates that the effect of the United States' subsidies is serious prejudice to the interests of Benin and Chad as well, within the meaning of Articles 6.3(d) and 5(c) of the *SCM Agreement*. Benin and Chad submit that the "interests of another Member" in Article 5(c) are not limited only to the interests of the complaining Member and ask us to find accordingly.⁷¹⁷

2. Analysis

504. Article 6.3 of the *SCM Agreement* provides, in relevant part:

Serious prejudice in the sense of paragraph (c) of Article 5 may arise in any case where one or several of the following apply:

...

⁷¹³*Ibid.*, paras. 154-156.

⁷¹⁴*Ibid.*, para. 161.

⁷¹⁵*Ibid.*, paras. 163-165.

⁷¹⁶Benin and Chad's third participants' submission, paras. 75-79.

⁷¹⁷*Ibid.*, paras. 80-91.

(d) the effect of the subsidy is an increase in the world market share of the subsidizing Member in a particular subsidized primary product or commodity¹⁷ as compared to the average share it had during the previous period of three years and this increase follows a consistent trend over a period when subsidies have been granted.

¹⁷ Unless other multilaterally agreed specific rules apply to the trade in the product or commodity in question.

505. As we have noted above, the four subparagraphs of Article 6.3 describe circumstances in which a subsidy has certain effects, which, in turn, may constitute serious prejudice under Article 5(c).⁷¹⁸ Article 6.3(d) addresses a situation in which subsidies have the effect of increasing the "world market share of the subsidizing Member in a particular subsidized product or commodity". The Panel held that the phrase "world market share" of the subsidizing Member in Article 6.3(d) of the *SCM Agreement* "refers to share of the world market *supplied* by the subsidizing Member of the product concerned".⁷¹⁹ As Brazil had failed to submit evidence pertaining to this legal interpretation, the Panel found that Brazil had failed to make a *prima facie* case of violation of this provision.⁷²⁰

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506. Brazil's appeal with respect to the application of Article 6.3(d) of the *SCM Agreement* has two elements. First, Brazil appeals the Panel's interpretation of the phrase "world market share" in that provision. Second, Brazil requests us to complete the analysis of this issue and rule that the effect of certain United States subsidies is an increase in the world market share of the United States in upland cotton. This second element of Brazil's appeal is *conditional* upon us reversing the Panel's findings with respect to the interpretation of Article 6.3(c) of the *SCM Agreement*.

⁷¹⁸On the relationship between Articles 5(c) and 6.3 of the *SCM Agreement*, see *supra*, paras. 485-488.

⁷¹⁹Panel Report, para. 7.1464. (emphasis added)

⁷²⁰*Ibid.*, para. 7.1465.

507. We observe with regard to the interpretation of the phrase "world market share" in Article 6.3(d) that, above⁷²¹, we upheld the Panel's finding that the effect of the price-contingent subsidies at issue in these proceedings is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*. We observe, therefore, that the condition upon which the second part of Brazil's appeal is contingent is *not* fulfilled, and thus there is no need for us to complete the analysis and to examine whether or not the United States subsidies at issue have the effect of increasing the United States' world market share in upland cotton.

508. Nor do we believe that it is necessary to make a finding on the interpretation of the phrase "world market share" in Article 6.3(d) of the *SCM Agreement*. We recall that Article 17.12 of the DSU requires that the "Appellate Body shall address each of the issues raised in accordance with paragraph 6 [of Article 17] during the appellate proceeding". In addition, we note that Article 3.3 of the DSU explains that:

The prompt settlement of situations in which a Member considers that any benefits accruing to it directly or indirectly under the covered agreements are being impaired by measures taken by another Member is essential to the effective functioning of the WTO and the maintenance of a proper balance between the rights and obligations of Members.

For its part, Article 3.4 of the DSU provides that "[r]ecommendations or rulings made by the DSB shall be aimed at achieving a satisfactory settlement of the matter". Similarly, Article 3.7 states that "[t]he aim of the dispute settlement mechanism is to secure a positive solution to a dispute".

509. In *US – Wool Shirts and Blouses*, the Appellate Body cautioned that:

Given the explicit aim of dispute settlement that permeates the *DSU*, we do not consider that Article 3.2 of the *DSU* is meant to encourage either panels or the Appellate Body to "make law" by clarifying existing provisions of the *WTO Agreement* outside the context of resolving a particular dispute.⁷²²

510. With this in mind, we observe that although an interpretation by the Appellate Body, in the abstract, of the meaning of the phrase "world market share" in Article 6.3(d) of the *SCM Agreement*

⁷²¹*Supra*, para. 496.

⁷²²Appellate Body Report, *US – Wool Shirts and Blouses*, p. 19, DSR 1997:1, 323 at 340.

might offer at best some degree of "guidance" on that issue, it would not affect the resolution of this particular dispute.⁷²³ Indeed, irrespective of whether we were to uphold or reverse the Panel's finding on this issue, upon adoption of the recommendations and rulings by the DSB, the United States would be under no additional obligation regarding implementation. Thus, although we recognize that there may be cases in which it would be useful for us to review an issue, despite the fact that our ruling would not result in rulings and recommendations by the DSB, we find no compelling reason for doing so in this case.

511. Accordingly, we believe that an interpretation of the phrase "world market share" in Article 6.3(d) of the *SCM Agreement* is unnecessary for purposes of resolving this dispute. We emphasize that we neither uphold nor reverse the Panel's findings on the interpretation of the phrase "world market share" in Article 6.3(d) of the *SCM Agreement*.

512. Finally, we recall that Article 24.1 of the DSU requires that "[a]t all stages of the determination of the causes of a dispute and of dispute settlement procedures involving a least-developed country Member, particular consideration shall be given to the special situation of least-developed country Members". We fully recognize the importance of this provision. However, we recall that Benin and Chad request us to find that their interests have suffered serious prejudice in the sense of Article 5(c) of the *SCM Agreement*, if we find Brazil has suffered serious prejudice as a result of an increase in the United States' world market share in upland cotton in the sense of Article 6.3(d) of the *SCM Agreement*. As we do not find it necessary to rule on Brazil's appeal regarding the interpretation of the phrase "world market share" in Article 6.3(d), we therefore are not in a position to accede to Benin and Chad's request to complete the analysis and to find that, in addition to Brazil, Benin and Chad also have suffered serious prejudice to their interests in the sense of Articles 6.3(d) and 5(c) of the *SCM Agreement*. We note that Benin and Chad's request to complete the analysis was predicated upon us reversing the Panel's interpretation of the phrase "world market share" in Article 6.3(d) of the *SCM Agreement*.⁷²⁴ This condition is not met.

⁷²³We note, in this regard, that, in *US – Steel Safeguards*, the Appellate Body noted that "several participants expressed an interest in having [it] rule on causation as it would provide guidance to Members on applying safeguard measures in the future consistently with their WTO obligations". (Appellate Body Report, *US – Steel Safeguards*, para. 484) Despite this request for guidance, the Appellate Body declined to make a ruling on this specific aspect of the case. (Appellate Body Report, *US – Steel Safeguards*, para. 483)

⁷²⁴Benin and Chad's third participants' submission, para. 83.

VII. Import Substitution Subsidies and Export Subsidies

A. Step 2 Payments to Domestic Users

1. Introduction

513. We examine next the United States' claims against the Panel's findings relating to the Step 2 payments provided to domestic users and exporters of United States upland cotton under Section 1207(a) of the FSRJ Act of 2002.

514. According to the Panel⁷²⁵, the program pursuant to which Step 2 payments are granted has been authorized since 1990 under successive legislation, including the FAIR Act of 1996⁷²⁶ and the FSRJ Act of 2002.⁷²⁷ Under the program, marketing certificates or cash payments (collectively referred to by the Panel as "user marketing (Step 2) payments")⁷²⁸ are issued to eligible domestic users and exporters of eligible upland cotton when certain market conditions exist such that United States cotton pricing benchmarks are exceeded. "Eligible upland cotton" is defined as "domestically produced baled upland cotton which bale is opened by an eligible domestic user ... or exported by an eligible exporter".⁷²⁹ An "eligible domestic user" of upland cotton is defined under the regulations as:

A person regularly engaged in the business of opening bales of eligible upland cotton for the purpose of manufacturing such cotton into cotton products in the United States (domestic user), who has entered into an agreement with CCC⁷³⁰ to participate in the upland cotton user marketing certificate program.⁷³¹

⁷²⁵Panel Report, para. 7.209.

⁷²⁶Section 136 of the FAIR Act of 1996, reproduced in Exhibits BRA-28 and US-22.

⁷²⁷Section 1207 of the FSRJ Act of 2002, reproduced in Exhibits BRA-29 and US-1, implemented under 7 CFR 1427, Subpart C, reproduced in Exhibit BRA-37.

⁷²⁸The Panel explained that "[f]or the purposes of this dispute, on the basis of the views of the parties, we make no distinction between user marketing (Step 2) cash payments and marketing certificates". (Panel Report, footnote 284 to para. 7.209, referring to Brazil's and the United States' respective responses to Panel Question No. 110 (a))

⁷²⁹7 CFR Section 1427.103(a).

⁷³⁰Additional information about the CCC is provided, *infra*, footnote 859; see also Panel Report, para. 7.702.

⁷³¹7 CFR Section 1427.104(a)(1).

515. For its part, an "eligible exporter" of upland cotton is:

A person, including a producer or a cooperative marketing association ... regularly engaged in selling eligible upland cotton for exportation from the United States (exporter), who has entered into an agreement with CCC to participate in the upland cotton user marketing certificate program.⁷³²

516. The Panel explained that, under the FAIR Act of 1996, the United States Secretary of Agriculture "issued user marketing (Step 2) payments to domestic users and exporters of upland cotton for documented purchases by domestic users and sales for export by exporters made in a week following a consecutive four-week period when the lowest price quotation for United States cotton delivered to Northern Europe exceeded the Northern Europe price quotation by more than 1.25 cents per pound, and the adjusted world price did not exceed 130 per cent of the marketing loan rate for upland cotton."⁷³³ The payments to domestic users and exporters are calculated "at a rate per pound equal to the difference between the two price quotations during the fourth week of the period, minus the 1.25 cents per pound threshold".⁷³⁴ Step 2 payments continued to be authorized under the FSRI Act of 2002, although with certain modifications. The Panel pointed out that "[i]n particular, application of the 1.25 cents per pound threshold has been delayed until 1 August 2006 (i.e. for the 2002 through 2005 marketing years)".⁷³⁵ The consequence of this, the Panel explained, is that "Step 2 payments are issued following a consecutive four-week period when the lowest price quotation for United States cotton delivered to Northern Europe exceeded the Northern Europe price quotation by any amount and the adjusted world price did not exceed 134 per cent (not 130 per cent, as under the FAIR Act of 1996) of the marketing loan rate".⁷³⁶ Domestic users and exporters receive payments that are calculated "at a rate per pound equal to the difference between the two price quotations during the fourth week of the period, with no reduction for the threshold".⁷³⁷

517. We address first the United States' appeal of the Panel findings in respect of Step 2 payments to *domestic users* of United States upland cotton. We examine the United States' appeal of the

⁷³²7 CFR Section 1427.104(a)(2).

⁷³³Panel Report, para. 7.210.

⁷³⁴*Ibid.*, para. 7.210 (referring to Section 136(a) of the FAIR Act of 1996 reproduced in Exhibits BRA-28 and US-22). The Panel added that Section 136(a)(5) limited total expenditures under this program to \$701 million, but this was later repealed. (*Ibid.*, footnote 286 to para. 7.210)

⁷³⁵*Ibid.*, para. 7.211.

⁷³⁶*Ibid.*

⁷³⁷*Ibid.*, para. 7.211 (referring to Section 1207(a) of the FSRI Act of 2002, reproduced in Exhibits BRA-29 and US-1, and 7 CFR 1427.107 (1 January 2003 edition), reproduced in Exhibit BRA-37).

Panel's finding in respect of Step 2 payments to *exporters* of United States upland cotton in the next Section of this Report.

2. Panel Findings

518. Before the Panel, Brazil argued that Step 2 payments to domestic users of upland cotton are *per se* import substitution subsidies that are inconsistent with Articles 3.1(b) and 3.2 of the *SCM Agreement*.⁷³⁸ Brazil explained that Step 2 payments to domestic users are "contingent on the use of domestic over imported goods within the meaning of Article 3.1(b) of the *SCM Agreement*" because the payments "are 'conditional' on proof of consumption of domestically produced upland cotton".⁷³⁹

519. The United States did not dispute that Step 2 payments are "subsidies" and that to receive a Step 2 payment a domestic user must "open a bale of domestically produced baled upland cotton".⁷⁴⁰ The United States, however, asserted that Step 2 payments to domestic users of upland cotton are included, and they comply with, the United States' domestic support reduction commitments pursuant to Article 6.3 of the *Agreement on Agriculture*.⁷⁴¹ As Step 2 payments to domestic users are permitted under the *Agreement on Agriculture*, the United States argued that these payments cannot be contrary to Article 3 of the *SCM Agreement*. This is because the introductory language of Article 3.1 of the *SCM Agreement* makes it clear that that provision applies "[e]xcept as provided in the *Agreement on Agriculture*".⁷⁴² The United States additionally asserted that "pursuant to Article 21 of the *Agreement on Agriculture*, all of the Annex 1A agreements (including the *SCM Agreement*) apply subject to the provisions of the *Agreement on Agriculture*".⁷⁴³

520. The Panel began its examination by observing that "[t]he introductory clause of Article 3.1 of the *SCM Agreement* ([e]xcept as provided in the *Agreement on Agriculture*) indicates that any examination of the WTO-consistency of a subsidy for agricultural products under the *SCM*

⁷³⁸Panel Report, para. 7.1019. Before the Panel, Brazil also claimed that Step 2 payments to *domestic users* are contrary to Article III.4 of the GATT 1994 and that they are not justified under Article III.8(b) because they are not exclusively paid to domestic *producers* of cotton, but rather to domestic *users*.

The Panel exercised judicial economy in respect of this claim, in the light of the fact that it had already found the same measure to be inconsistent with Articles 3.1(b) and 3.2 of the *SCM Agreement*. Brazil has not appealed the Panel's exercise of judicial economy. (*Ibid.*, paras. 7.1099 and 7.1106)

⁷³⁹*Ibid.*, para. 7.1019.

⁷⁴⁰*Ibid.*, para. 7.1022 (quoting the United States' response to Question 144 Posed by the Panel (Panel Report, p. I-128, para. 217 and p. I-249, para. 58)).

⁷⁴¹*Ibid.*, para. 7.1023.

⁷⁴²*Ibid.*, para. 7.1024.

⁷⁴³*Ibid.*

Agreement may depend upon the provisions of the *Agreement on Agriculture*.⁷⁴⁴ The Panel then examined Article 21.1 of the *Agreement on Agriculture* and observed that this provision "expressly acknowledges the application of the *GATT 1994* and the *SCM Agreement* to agricultural products, while indicating that the *Agreement on Agriculture* would take precedence in the event, and to the extent, of any conflict".⁷⁴⁵ The Panel described the situations in which, in its view, Article 21.1 of the *Agreement on Agriculture* applies,⁷⁴⁶ and then turned to "the relevant provisions of the *Agreement on Agriculture* in order to discern whether, and/or to what extent, these provisions affect a claim concerning the prohibition on import substitution subsidies in Article 3.1(b) of the *SCM Agreement*."⁷⁴⁷ The Panel concluded that "none of the situations" it described arises in this dispute from the relevant provisions in the *Agreement on Agriculture*.⁷⁴⁸

521. The Panel examined Article 13 of the *Agreement on Agriculture*, but concluded that this provision did not affect its analysis of Brazil's claims under Article 3.1(b) of the *SCM Agreement*.⁷⁴⁹ The Panel then looked at Article 6.3 and paragraph 7 of Annex 3 of the *Agreement on Agriculture*, rejecting the United States' contention that "user marketing (Step 2) payments to upland cotton domestic users that provide support to domestic producers contingent on the use of domestic goods [are] consistent with the *Agreement on Agriculture*".⁷⁵⁰ The Panel reasoned instead that:

Article 6.3 does not provide that compliance with such "domestic support reduction commitments" shall necessarily be considered to be in compliance with other applicable WTO obligations. Nor does it contain an explicit textual indication that otherwise prohibited measures are necessarily justified by virtue of compliance with the domestic support reduction commitments. The obligations are parallel, and the operation of Article 6.3 of the *Agreement on Agriculture* does not pre-empt or exclude the operation of the obligation under Article 3.1(b) of the *SCM Agreement*.⁷⁵¹

522. From this the Panel concluded that "Article 3.1(b) of the *SCM Agreement* can be read together with the *Agreement on Agriculture* provisions relating to domestic support in a coherent and consistent manner which gives full and effective meaning to all of their terms".⁷⁵² Accordingly, the

⁷⁴⁴Panel Report, para. 7.1034. (footnote omitted)

⁷⁴⁵*Ibid.*, para. 7.1036.

⁷⁴⁶*Ibid.*, para. 7.1038. See *infra*, para. 532.

⁷⁴⁷*Ibid.*, para. 7.1041. (footnote omitted)

⁷⁴⁸*Ibid.*, para. 7.1039.

⁷⁴⁹*Ibid.*, para. 7.1052.

⁷⁵⁰*Ibid.*, para. 7.1056.

⁷⁵¹*Ibid.*, para. 7.1058. (original emphasis)

⁷⁵²*Ibid.*, para. 7.1071.

Panel found no conflict between the domestic support provisions of the *Agreement on Agriculture* and Article 3.1(b) of the *SCM Agreement* and, therefore, saw no necessity to apply the rules in Article 21.1 of the *Agreement on Agriculture*.⁷⁵³

523. Having examined the relationship between the relevant provisions of the *Agreement on Agriculture* and the *SCM Agreement*, the Panel proceeded to examine whether the Step 2 payments to domestic users are contingent on the use of domestic products contrary to Article 3.1(b) of the *SCM Agreement*. The Panel noted that the United States had acknowledged that "to receive a payment under the user marketing (Step 2) programme, a domestic user must open a bale of domestically produced baled upland cotton" and, therefore, did "not dispute that user marketing (Step 2) payments to domestic users constitute a subsidy conditional or dependent upon the use of domestic over imported goods within the meaning of Article 3.1(b) of the *SCM Agreement*".⁷⁵⁴ The Panel also conducted its own examination and found that:

... user marketing (Step 2) payments to domestic users under section 1207(a) of the FSR1 Act of 2002 will not be made except upon proof of consumption of eligible upland cotton – which must be "domestically produced", and "not imported". It is not just that it will invariably be easier for domestic users to meet the conditions for user marketing (Step 2) payments to domestic users by using domestic – rather than imported – upland cotton. The text of the measure explicitly *requires* the use of domestically produced upland cotton as a pre-condition for receipt of the payments.

The use of United States domestically produced upland cotton is a condition for obtaining the subsidy. User marketing (Step 2) payments to domestic users under section 1207(a) of the FSR1 Act of 2002 are clearly conditional, or dependent upon, such use.⁷⁵⁵

524. The Panel, furthermore, recalled its finding that the "fact that the user marketing (Step 2) payments are also available in another factual situation ... – i.e. exporters – would not have the effect of dissolving such contingency in respect of domestic users, particularly ... where the other factual contingency (upon export performance) also gives rise to a prohibited subsidy".⁷⁵⁶

⁷⁵³Panel Report, para. 7.1071.

⁷⁵⁴*Ibid.*, para. 7.1082 (referring to the United States' response to Question 144 Posed by the Panel (Panel Report, p. 1-249, para. 58) and Appellate Body Report, *Canada – Autos*, para. 126). (footnotes omitted)

⁷⁵⁵*Ibid.*, paras. 7.1085-7.1086. (original emphasis)

⁷⁵⁶*Ibid.*, para. 7.1087.

525. Therefore, the Panel concluded that "section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to domestic users is inconsistent with Article 3.1(b) of the *SCM Agreement*".⁷⁵⁷ In addition, the Panel found that "[f]o the extent that section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to domestic users is inconsistent with Article 3.1(b), it is, consequently, also inconsistent with Article 3.2 of the *SCM Agreement*".⁷⁵⁸

3. Arguments on Appeal

526. On appeal, the United States requests us to reverse the Panel's findings. According to the United States, the Panel's conclusion fails to give meaning to the introductory phrase "[e]xcept as provided in the Agreement on Agriculture" of Article 3.1 of the *SCM Agreement*.⁷⁵⁹ This phrase not only applies to export subsidies covered by Article 3.1(a) of the *SCM Agreement*, but also to import substitution subsidies covered by Article 3.1(b). The United States contends that Step 2 payments to domestic users are properly classified as domestic support subject to reduction commitments under Article 6 of the *Agreement on Agriculture*.⁷⁶⁰ Indeed, paragraph 7 of Annex 3 requires that measures directed at agricultural processors shall be included in the AMS to the extent that such measures benefit the producers of the basic agricultural products. This approach is consistent with the objective of the *Agreement on Agriculture* of providing for substantial progressive reductions in agricultural support and protection sustained over an agreed period of time.⁷⁶¹ Furthermore, the United States argues that the lack of any reference to domestic content subsidies in Article 13(b) of the *Agreement on Agriculture* does not support the Panel's interpretation.⁷⁶² Article 13(b) does not refer to Article 3 of the *SCM Agreement* because the substantive obligation of Article 3.1(b) does not apply in the case of domestic content subsidies in favour of agricultural producers.

527. Brazil requests that we uphold the Panel's findings. According to Brazil, "[t]he obligations in the *Agreement on Agriculture* and the *SCM Agreement* apply cumulatively, unless there is an exception or a conflict".⁷⁶³ In Brazil's view, no conflict arises. Under the *Agreement on Agriculture*, WTO Members enjoy a right to grant domestic support in favour of agricultural producers. However, this does not create a conflict with Article 3.1(b) of the *SCM Agreement*, because it is perfectly possible for Members to grant domestic support without making payments contingent on domestic

⁷⁵⁷Panel Report, para. 7.1097. (footnote omitted)

⁷⁵⁸*Ibid.*, para. 7.1098.

⁷⁵⁹United States' appellant's submission, paras. 429-430.

⁷⁶⁰*Ibid.*, para. 434.

⁷⁶¹*Ibid.*, para. 435.

⁷⁶²*Ibid.*, paras. 431-432.

⁷⁶³Brazil's appellee's submission, para. 75.

content. In other words, Members can fully enjoy their right to grant domestic support *and* comply with Article 3.1(b).⁷⁶⁴

528. Brazil asserts that this interpretation is consistent with a primary objective of the covered agreements, namely, avoiding discrimination under the national treatment rule. It is also consistent with an adopted 1958 GATT panel report involving a subsidy to agricultural producers that was contingent on purchase of domestic goods.⁷⁶⁵ Thus, Brazil states that domestic content subsidies in favour of agricultural producers have been understood to be impermissible since 1958, so there is nothing novel about Brazil's complaint.⁷⁶⁶ The *Agreement on Agriculture* did not mark a step back to allowing discrimination and protection that was prohibited under the GATT 1947. Therefore, domestic support under the *Agreement on Agriculture* can and must be granted consistently with Article 3.1(b) of the *SCM Agreement* and Article III:4 of the GATT 1994.⁷⁶⁷

4. Does Article 3.1(b) of the *SCM Agreement* Apply to Agricultural Products?

529. At the outset, we note that the United States did not dispute before the Panel that, if the *SCM Agreement* were applicable, "user marketing (Step 2) payments to domestic users [would] constitute a subsidy conditional or dependent upon the use of domestic over imported goods within the meaning of Article 3.1(b)" of that Agreement.⁷⁶⁸ Instead, before the Panel and on appeal, the United States asserts that Article 3.1(b) of the *SCM Agreement* is inapplicable to Step 2 payments to domestic users because these payments are consistent with the United States' domestic support reduction commitments under the *Agreement on Agriculture*.⁷⁶⁹

⁷⁶⁴Brazil's appellee's submission, para. 867.

⁷⁶⁵*Ibid.*, para. 860 (referring to GATT Panel Report, *Italy – Agricultural Machinery*, para. 16). According to Brazil, that panel recognized that the GATT contracting parties were entitled to grant support to agricultural producers but found that this could be done without granting domestic content subsidies.

⁷⁶⁶Brazil's appellee's submission, para. 861.

⁷⁶⁷*Ibid.*, paras. 863-865.

⁷⁶⁸Panel Report, para. 7.1082.

⁷⁶⁹*Ibid.*, para. 7.1023; United States' appellant's submission, paras. 434-436.

530. Article 3.1(b) of the *SCM Agreement* provides:

Article 3

Prohibition

Except as provided in the Agreement on Agriculture, the following subsidies, within the meaning of Article 1, shall be prohibited:

...

- (b) subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods.

We note that the introductory language of the chapeau makes it clear that the *Agreement on Agriculture* prevails over Article 3 of the *SCM Agreement*, but only to the extent that the former contains an exception.

531. Article 21.1 of the *Agreement on Agriculture*, which deals more broadly with the relationship between that Agreement and the other covered agreements relating to the trade in goods, provides:

The provisions of GATT 1994 and of other Multilateral Trade Agreements in Annex 1A to the WTO Agreement shall apply subject to the provisions of this Agreement.⁷⁷⁰

532. We agree that Article 21.1 could apply in the three situations described by the Panel, namely:

... where, for example, the domestic support provisions of the *Agreement on Agriculture* would prevail in the event that an explicit carve-out or exemption from the disciplines in Article 3.1(b) of the *SCM Agreement* existed in the text of the *Agreement on Agriculture*. Another situation would be where it would be impossible for a Member to comply with its domestic support obligations under the *Agreement on Agriculture* and the Article 3.1(b) prohibition simultaneously. Another situation might be where there is an explicit authorization in the text of the *Agreement on Agriculture* that would authorize a measure that, in the absence of such an express authorization, would be prohibited by Article 3.1(b) of the *SCM Agreement*.⁷⁷¹

⁷⁷⁰The *SCM Agreement* is among the Multilateral Trade Agreements in Annex 1A to the *WTO Agreement*.

⁷⁷¹Panel Report, para. 7.1038. (original emphasis) The Panel concluded that "none of the situations just mentioned arise[s] in this dispute from the relevant provisions in the *Agreement on Agriculture*". (Panel Report, para. 7.1039)

The Appellate Body has interpreted Article 21.1 to mean that the provisions of the GATT 1994 and of other Multilateral Trade Agreements in Annex 1A apply, "except to the extent that the *Agreement on Agriculture* contains specific provisions dealing specifically with the same matter".⁷⁷² There could be, therefore, situations other than those identified by the Panel where Article 21.1 of the *Agreement on Agriculture* may be applicable.

533. The key issue before us is whether the *Agreement on Agriculture* contains "specific provisions dealing specifically with the same matter" as Article 3.1(b) of the *SCM Agreement*, that is, subsidies contingent upon the use of domestic over imported goods. We, therefore, turn to the relevant provisions of the *Agreement on Agriculture*.

534. The United States draws our attention to the domestic support provisions in the *Agreement on Agriculture*, particularly to Article 6.3 and to paragraph 7 of Annex 3. Article 6 of the *Agreement on Agriculture* deals with domestic support commitments. Pursuant to Article 6, WTO Members have committed themselves to reduce the domestic support that they provide to their agricultural sector.⁷⁷³ For this purpose, domestic support is calculated using what is known as the AMS, which is defined in Article 1(a) as:

... the annual level of support, expressed in monetary terms, provided for an agricultural product in favour of the producers of the basic agricultural product or non-product-specific support provided in favour of agricultural producers in general, other than support provided under programmes that qualify as exempt from reduction under Annex 2 to this Agreement ...

A WTO Member's domestic support reduction commitments are registered in Part IV of its Schedule.

535. Article 6.3 of the *Agreement on Agriculture*, the particular provision relied on by the United States, reads:

A Member shall be considered to be in compliance with its domestic support reduction commitments in any year in which its domestic support in favour of agricultural producers expressed in terms of Current Total AMS does not exceed the corresponding annual or final bound commitment level specified in Part IV of the Member's Schedule.

⁷⁷²Appellate Body Report, *EC – Bananas III*, para. 155. (See also Appellate Body Report, *Chile – Price Band System*, para. 186)

⁷⁷³Certain domestic measures are exempted from these reduction commitments under Articles 6.4 and 6.5 and Annex 2 of the *Agreement on Agriculture*.

The United States also relies on paragraph 7 of Annex 3 of the *Agreement on Agriculture*. This Annex explains how WTO Members are to calculate AMS. Paragraph 7 of Annex 3 states, in relevant part, that "[m]easures directed at agricultural processors shall be included [in the AMS calculation] to the extent that such measures benefit the producers of the basic agricultural products".

536. Before determining whether Article 6.3 and paragraph 7 of Annex 3 of the *Agreement on Agriculture* deal specifically with the same matter as Article 3.1(b) of the *SCM Agreement*, we must address the question whether the Step 2 payments to domestic users of United States upland cotton fall within paragraph 7 of Annex 3 because the United States claims that they are "[m]easures directed at agricultural processors" and "benefit the producers of the basic agricultural products". The United States argues that Step 2 payments to domestic users fall within paragraph 7 of Annex 3 because, even though the payment is provided to persons opening a bale of cotton, the payment *benefits* producers of United States cotton. The United States explains that this is the case "because [the program] serves to maintain the price competitiveness of U.S. cotton vis-a-vis foreign cotton through a payment to capture some differential between prevailing foreign and domestic cotton prices."⁷⁷⁴

537. We recall that "domestic users" are defined, under the United States' regulations, as "person[s] regularly engaged in the business of opening bales of eligible upland cotton for the purpose of manufacturing such cotton into cotton products in the United States."⁷⁷⁵ The United States has acknowledged that the domestic users of United States cotton that receive Step 2 payments include textile mills.⁷⁷⁶ There is no dispute between the parties that the producers of United States cotton are "producers of ... basic agricultural products" for purposes of paragraph 7 of Annex 3. Moreover, Brazil has not disputed the United States' claim that Step 2 payments to domestic users may "benefit" the producers of United States cotton. Therefore, we will proceed with our examination on the assumption that Step 2 payments to domestic users of United States cotton are contemplated by paragraph 7 of Annex 3 of the *Agreement on Agriculture*.⁷⁷⁷

538. We thus turn to the issue raised by the United States' appeal, that is, whether Article 6.3 and paragraph 7 of Annex 3 of the *Agreement on Agriculture* are "specific provisions dealing specifically with the same matter" as Article 3.1(b) of the *SCM Agreement*, namely, subsidies contingent upon the use of domestic over imported goods.

⁷⁷⁴United States' appellant's submission, para. 428.

⁷⁷⁵See *supra*, para. 514.

⁷⁷⁶United States' response to questioning at oral hearing.

⁷⁷⁷In this dispute we do not decide whether subsidies paid to textile manufacturers on their purchases of cotton could be regarded as measures directed at "agricultural processors" within the meaning of paragraph 7 of Annex 3.

539. The United States finds in the second sentence of paragraph 7 of Annex 3 of the *Agreement on Agriculture* an exception to the broad prohibition against subsidies contingent upon the use of domestic over imported goods that is established in Article 3.1(b) of the *SCM Agreement*. We note that Annex 3 sets out instructions on how to calculate WTO Members' AMS. Paragraph 7 is one of 13 paragraphs contained in Annex 3. It reads:

The AMS shall be calculated as close as practicable to the point of first sale of the basic agricultural product concerned. Measures directed at agricultural processors shall be included to the extent that such measures benefit the producers of the basic agricultural products.

540. Neither of the two sentences in paragraph 7 of Annex 3 refers to import substitution subsidies. Paragraph 7 of Annex 3 reflects a preference for calculating domestic support as near as possible to the stage of production of an agricultural good. Hence, the first sentence of paragraph 7 of Annex 3 provides that "[t]he AMS shall be calculated as close as practicable to the point of first sale of the basic agricultural product concerned". The second sentence of paragraph 7 recognizes situations where subsidies are not provided directly to the agricultural producer, but rather to an agricultural processor, yet the measures may benefit the producers of the basic agricultural good. This sentence also clarifies that only the portion of the subsidy that benefits the producers of the basic agricultural good, and not the entire amount, shall be included in a Member's AMS.

541. It may well be that a measure that is an import substitution subsidy could fall within the second sentence of paragraph 7 as "[m]easures directed at agricultural processors [that] shall be included [in the AMS calculation] to the extent that such measures benefit the producers of the basic agricultural products". There is nothing, however, in the text of paragraph 7 that suggests that such measures, when they are import substitution subsidies, are exempt from the prohibition in Article 3.1(b) of the *SCM Agreement*. We agree with the Panel that there is a clear distinction between a provision that requires a Member to include a certain type of payment (or part thereof) in its AMS calculation and one that would authorize subsidies that are contingent on the use of domestic over imported goods.⁷⁷⁸

542. The United States argues that, if payments to processors that fall within paragraph 7 are not exempted from the prohibition in Article 3.1(b) of the *SCM Agreement*, paragraph 7 would be rendered inutile.⁷⁷⁹ According to the United States, if domestic users were allowed to claim Step 2 payments, regardless of the origin of the cotton, this "would cause the benefit to [domestic] cotton

⁷⁷⁸Panel Report, para. 7.1059.

⁷⁷⁹United States' appellant's submission, para. 428.

producers to evaporate" and the "subsidy would be transformed from a subsidy 'in favor of agricultural producers' to a simple input subsidy".⁷⁸⁰ Rather than "a cotton subsidy", it would become a "textile subsidy".⁷⁸¹ Like the Panel, we do not believe that the scope of paragraph 7 is limited to measures that have an import substitution component in them. There could be other measures covered by paragraph 7 of Annex 3 that do not necessarily have such a component. Indeed, Brazil submits that if the Step 2 payments were provided to United States processors of cotton, regardless of the origin of the cotton, these processors "would still buy *at least* some U.S. upland cotton, so producers would continue to derive *some* benefit".⁷⁸² Thus, paragraph 7 of Annex 3 refers more broadly to measures directed at agricultural processors that benefit producers of a basic agricultural product and, contrary to the United States' assertion, it is not rendered inutile by the Panel's interpretation. WTO Members may still provide subsidies directed at agricultural processors that benefit producers of a basic agricultural commodity in accordance with the *Agreement on Agriculture*, as long as such subsidies do not include an import substitution component.

543. In addition to paragraph 7 of Annex 3, the United States draws our attention to Article 6.3 of the *Agreement on Agriculture*. The United States points out that Article 6.3 explicitly provides that a WTO Member "shall be considered to be *in compliance* with its domestic support reduction commitments in any year in which its domestic support in favour of agricultural producers expressed in terms of Current Total AMS does not exceed the corresponding annual or final bound commitment level". (emphasis added)

544. Like paragraph 7 of Annex 3, Article 6.3 does not explicitly refer to import substitution subsidies. Article 6.3 deals with domestic support. It establishes only a *quantitative* limitation on the amount of domestic support that a WTO Member can provide in a given year. The quantitative limitation in Article 6.3 applies generally to all domestic support measures that are included in a WTO Member's AMS. Article 3.1(b) of the *SCM Agreement* prohibits subsidies that are contingent—that is, "conditional"⁷⁸³—on the use of domestic over imported goods.⁷⁸⁴

545. Article 6.3 does not authorize subsidies that are contingent on the use of domestic over imported goods. It only provides that a WTO Member shall be considered to be in compliance with its domestic support *reduction commitments* if its Current Total AMS does not exceed that Member's

⁷⁸⁰United States' appellant's submission, para. 428.

⁷⁸¹*Ibid.* (emphasis omitted)

⁷⁸²Brazil's appellee's submission, footnote 1242 to para. 854. (original emphasis)

⁷⁸³Appellate Body Report, *Canada – Autos*, para. 123.

⁷⁸⁴See Panel Report, para. 7.1067.

annual or final bound commitment level specified in its Schedule. It does not say that compliance with Article 6.3 of the *Agreement on Agriculture* insulates the subsidy from the prohibition in Article 3.1(b). We, therefore, agree with the Panel that:

Article 6.3 does *not* provide that compliance with such "domestic support reduction commitments" shall necessarily be considered to be in compliance with other applicable WTO obligations. Nor does it contain an explicit textual indication that otherwise prohibited measures are necessarily justified by virtue of compliance with the domestic support reduction commitments.⁷⁸⁵

546. For these reasons, we find that paragraph 7 of Annex 3 and Article 6.3 of the *Agreement on Agriculture* do not deal specifically with the same matter as Article 3.1(b) of the *SCM Agreement*, that is, subsidies contingent upon the use of domestic over imported goods.

547. We are mindful that the introductory language of Article 3.1 of the *SCM Agreement* clarifies that this provision applies "[e]xcept as provided in the Agreement on Agriculture". Furthermore, as the United States has pointed out, this introductory language applies to both the export subsidy prohibition in paragraph (a) and to the prohibition on import substitution subsidies in paragraph (b) of Article 3.1. As we explained previously, in our review of the provisions of the *Agreement on Agriculture* relied on by the United States, we did not find a provision that deals specifically with subsidies that have an import substitution component. By contrast, the prohibition on the provision of subsidies contingent upon the use of domestic over imported goods in Article 3.1(b) of the *SCM Agreement* is explicit and clear. Because Article 3.1(b) treats subsidies contingent on the use of domestic over imported products as prohibited subsidies, it would be expected that the drafters would have included an equally explicit and clear provision in the *Agreement on Agriculture* if they had indeed intended to authorize such prohibited subsidies provided in connection with agricultural goods. We find no provision in the *Agreement on Agriculture* dealing specifically with subsidies contingent upon the use of domestic over imported agricultural goods.

548. Our approach in this case is consistent with the Appellate Body's approach in *EC – Bananas III*. In that case, the European Communities relied on Article 4.1 of the *Agreement on Agriculture* in arguing that the market access concessions it made for agricultural products pursuant to the *Agreement on Agriculture* prevailed over Article XIII of the GATT 1994.⁷⁸⁶ The Appellate Body, however, found that "[t]here is nothing in Articles 4.1 or 4.2, or in any other article of the *Agreement on Agriculture*, that deals specifically with the allocation of tariff quotas on agricultural

⁷⁸⁵Panel Report, para. 7.1058. (original emphasis)

⁷⁸⁶Appellate Body Report, *EC – Bananas III*, para. 153.

products".⁷⁸⁷ It further explained that "[i]f the negotiators had intended to permit Members to act inconsistently with Article XIII of the GATT 1994, they would have said so explicitly".⁷⁸⁸ The situation before us is similar. We have found nothing in Article 6.3, paragraph 7 of Annex 3 or anywhere else in the *Agreement on Agriculture* that "deals specifically" with subsidies that are contingent on the use of domestic over imported agricultural products.

549. We recall that the *Agreement on Agriculture* and the *SCM Agreement* "are both Multilateral Agreements on Trade in Goods contained in Annex 1A of the *Marrakesh Agreement Establishing the World Trade Organization* (the "*WTO Agreement*"), and, as such, are *both* 'integral parts' of the same treaty, the *WTO Agreement*, that are 'binding on all Members'".⁷⁸⁹ Furthermore, as the Appellate Body has explained, "a treaty interpreter must read all applicable provisions of a treaty in a way that gives meaning to *all* of them, harmoniously".⁷⁹⁰ We agree with the Panel that "Article 3.1(b) of the *SCM Agreement* can be read together with the *Agreement on Agriculture* provisions relating to domestic support in a coherent and consistent manner which gives full and effective meaning to all of their terms".⁷⁹¹

550. In sum, we are not persuaded by the United States' submission that the prohibition in Article 3.1(b) of the *SCM Agreement* is inapplicable to import substitution subsidies provided in connection with products falling under the *Agreement on Agriculture*. WTO Members may still provide domestic support that is consistent with their reduction commitments under the *Agreement on Agriculture*. In providing such domestic support, however, WTO Members must be mindful of their other WTO obligations, including the prohibition in Article 3.1(b) of the *SCM Agreement* on the provision of subsidies that are contingent on the use of domestic over imported goods.

551. Turning to the particular measure before us in this dispute, we recall that the United States acknowledged before the Panel that, if the *SCM Agreement* were applicable, "user marketing (Step 2) payments to domestic users [would] constitute a subsidy conditional or dependent upon the

⁷⁸⁷ Appellate Body Report, *EC – Bananas III*, para. 157.

⁷⁸⁸ *Ibid.*

⁷⁸⁹ Appellate Body Report, *Argentina – Footwear (EC)*, para. 81 (quoting from *WTO Agreement*, Article II.2). (original emphasis) In that case, the Appellate Body was referring to the GATT 1994 and the *Agreement on Safeguards*.

⁷⁹⁰ Appellate Body, *Argentina – Footwear (EC)*, para. 81 and footnote 72 thereto (referring to Appellate Body Report, *Korea – Dairy*, para. 81; Appellate Body Report, *US – Gasoline*, p. 23, DSR 1996:1, 3 at 21; Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 12, DSR 1996:1, 97 at 106; and Appellate Body Report, *India – Patents (US)*, para. 45). (original emphasis)

⁷⁹¹ Panel Report, para. 7.1071.

use of domestic over imported goods within the meaning of Article 3.1(b)" of that Agreement.⁷⁹² The Panel also conducted its own analysis and concluded that:

The use of United States domestically produced upland cotton is a condition for obtaining the subsidy. User marketing (Step 2) payments to domestic users under section 1207(a) of the FSRI Act of 2002 are clearly conditional, or dependent upon, such use.⁷⁹³

The United States has not appealed this finding and, therefore, we need not review it.

552. Accordingly, we *uphold* the Panel's findings, in paragraphs 7.1088, 7.1097-7.1098 and 8.1(f) of the Panel Report, that Step 2 payments to domestic users of United States upland cotton, under Section 1207(a) of the FSRI Act of 2002, are subsidies contingent on the use of domestic over imported goods that are inconsistent with Articles 3.1(b) and 3.2 of the *SCM Agreement*.

B. Step 2 Payments to Exporters

553. We turn to the United States' claim that the Panel erred in finding that Step 2 payments provided to *exporters* of United States upland cotton, under Section 1207(a) of the FSRI Act of 2002, are subsidies contingent on exportation and, therefore, are inconsistent with Articles 3.3 and 8 of the *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement*. We described the Step 2 payments program in the previous Section of this Report, where we examined the Panel's findings relating to Step 2 payments provided to *domestic users* of United States upland cotton.⁷⁹⁴

554. Before the Panel, Brazil argued that Step 2 payments to exporters are *per se* export subsidies listed in Article 9.1(a) of the *Agreement on Agriculture* and are inconsistent with Article 3.3 and/or Article 8 of the *Agreement on Agriculture*, as well as with Articles 3.1 and 3.2 of the *SCM Agreement*.⁷⁹⁵ The United States denied that Step 2 payments constitute export subsidies for purposes of the *Agreement on Agriculture* or Articles 3.1(a) and 3.2 of the *SCM Agreement*, arguing that these payments are available not only to exporters, but also to domestic users of upland cotton.⁷⁹⁶

⁷⁹² Panel Report, para. 7.1082.

⁷⁹³ *Ibid.*, para. 7.1086.

⁷⁹⁴ See also *ibid.*, paras. 7.209-7.211.

⁷⁹⁵ *Ibid.*, para. 7.649(i). Brazil also made an alternative claim under Article 10.1 of the *Agreement on Agriculture*, but the Panel found it unnecessary to examine this claim because of its findings under Article 9. (*Ibid.*, para. 7.750)

⁷⁹⁶ *Ibid.*, para. 7.651(i).

555. Because Brazil challenged the alleged United States export subsidies under the *Agreement on Agriculture* and the *SCM Agreement*, the Panel first examined the relationship between these Agreements. The Panel explained what it considered to be the proper order of analysis as follows:

... it is appropriate to examine an alleged export subsidy in respect of an agricultural product first under the *Agreement on Agriculture* before, if and as appropriate, turning to any examination of the same measure under the *SCM Agreement*.⁷⁹⁷

556. Accordingly, the Panel began its examination of Brazil's claims against the Step 2 payments to exporters with Article 9.1 of the *Agreement on Agriculture*. In this respect, the Panel observed that the United States did not appear to dispute that Step 2 payments are subsidies provided by a government to producers of agricultural products, or to cooperatives or associations of such producers for purposes of Article 9.1(a) of the *Agreement on Agriculture*.⁷⁹⁸ The "key issue" before it, the Panel explained, was whether Step 2 payments to exporters are subsidies "contingent on export performance" within the meaning of Article 9.1(a) of the *Agreement on Agriculture*.⁷⁹⁹

557. The Panel then noted that the *Agreement on Agriculture* does not define the phrase "contingent on export performance". Given that a similar phrase is used in the *SCM Agreement*, the Panel saw no reason to read the phrase differently in the *Agreement on Agriculture*.⁸⁰⁰ The Panel also equated Brazil's claim that Step 2 payments to exporters are "per se" export subsidies with a claim that the subsidies are *de jure* export contingent under Article 3.1(a) of the *SCM Agreement*.⁸⁰¹ Such a claim of *de jure* export contingency had to be demonstrated, according to the Panel, "on the basis of the words of the relevant legislation, regulation or other legal instrument"⁸⁰² or "where the condition to export can be derived by necessary implication from the words actually used in the measure".⁸⁰³

⁷⁹⁷Panel Report, para. 7.673. The order of analysis was not an issue on appeal.

⁷⁹⁸*Ibid.*, para. 7.695. The Panel also conducted its own assessment and concluded that the measure meets the description in Article 9.1(a). (*Ibid.*, para. 7.696)

⁷⁹⁹*Ibid.*, para. 7.697.

⁸⁰⁰*Ibid.*, para. 7.700 and footnote 872 thereto (relying on Appellate Body Report, *US – FSC*, para. 141 and Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 192).

⁸⁰¹*Ibid.*, para. 7.702.

⁸⁰²*Ibid.*, (relying on Appellate Body Report, *Canada – Aircraft*, para. 167).

⁸⁰³*Ibid.*, para. 7.702 (relying on Appellate Body Report, *Canada – Autos*, para. 100 and Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 112).

558. In assessing whether the Step 2 payments to exporters are contingent on export performance under Article 9.1(a) of the *Agreement on Agriculture*, the Panel found:

It is undeniable that a condition of the receipt of user marketing (Step 2) payments to exporters under section 1207(a) of the FSRI Act of 2002 will always and inevitably be proof of exportation. The only way to receive such a payment is through exportation. Export performance is, therefore, a condition of receipt for this discrete segment of eligible recipients.

Every user marketing (Step 2) payment to an eligible exporter is contingent upon export.⁸⁰⁴

559. The Panel rejected the United States' contention that Step 2 payments are not contingent on export performance because they are available to both exporters and domestic users. According to the Panel, the program under which Step 2 payments are granted "involves payment to two distinct sets of recipients (exporters or domestic users) in two distinct factual situations (export or domestic use)".⁸⁰⁵ In the Panel's view, "[t]he fact that the subsidies granted in the second situation may not be export contingent does not dissolve the export contingency arising in the first situation".⁸⁰⁶

560. Having found that Step 2 payments to exporters are mandatory when certain market conditions exist⁸⁰⁷, the Panel concluded:

We therefore find that section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to exporters constitutes a subsidy "contingent on export performance" within the meaning of Article 9.1(a) of the *Agreement on Agriculture*.⁸⁰⁸

⁸⁰⁴Panel Report, paras. 7.734 and 7.735.

⁸⁰⁵*Ibid.*, para. 7.732.

⁸⁰⁶*Ibid.*, para. 7.739 and footnote 907 thereto (relying on Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 119).

⁸⁰⁷*Ibid.*, paras. 7.7745 and 7.746.

⁸⁰⁸*Ibid.*, para. 7.748.

561. Consequently, the Panel also found:

User marketing (Step 2) payments to exporters under section 1207(a) of the FSRI Act of 2002 are an export subsidy listed in Article 9.1 of the *Agreement on Agriculture*. In providing such subsidies, the United States has acted inconsistently with its obligation under Article 3.3 of the *Agreement on Agriculture* to "not provide subsidies in respect of any agricultural product not specified in ... its Schedule". The United States has furthermore acted inconsistently with its obligation in Article 8 of the *Agreement on Agriculture* "not to provide export subsidies otherwise than in conformity with [the *Agreement on Agriculture*] and with the commitments as specified in [its] Schedule".⁸⁰⁹

562. As for Brazil's claims under the *SCM Agreement*, the Panel found "that section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to exporters is inconsistent with Article 3.1(a) of the *SCM Agreement*".⁸¹⁰ The Panel additionally found that "[t]o the extent that section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to exporters is inconsistent with Article 3.1(a), it is, consequently, also inconsistent with Article 3.2 of the *SCM Agreement*".⁸¹¹

563. On appeal, the United States requests us to reverse the Panel's findings that Step 2 payments provided to exporters of United States upland cotton are export subsidies within the meaning of Article 9.1(a) of the *Agreement on Agriculture* and, therefore, are inconsistent with Articles 3.3 and 8 of that Agreement. The United States also requests that we reverse the Panel's finding that Step 2 payments to exporters are inconsistent with Articles 3.1(a) and 3.2 of the *SCM Agreement*, because they are not exempted from action by Article 13(c) of the *Agreement on Agriculture*.⁸¹²

564. The United States does not contest that Step 2 payments are subsidies to producers of an agricultural product for purposes of Article 9.1(a) of the *Agreement on Agriculture*; nor does it contest the Panel's finding in this regard. The focus of the United States' appeal is the Panel's finding that Step 2 payments are contingent on export performance under Article 9.1(a).⁸¹³ In support of its claim, the United States reiterates on appeal the arguments that it made before the Panel. The United States asserts that Step 2 payments are not contingent on export performance because Step 2 payments

⁸⁰⁹Panel Report, para. 7.749.

⁸¹⁰*Ibid.*, para. 7.760.

⁸¹¹*Ibid.*, para. 7.761.

⁸¹²United States' appellant's submission, para. 516(6).

⁸¹³*Ibid.*, para. 442.

are also available to domestic users of United States upland cotton.⁸¹⁴ The United States contends that the payments are contingent on use, not exportation.

565. Brazil requests that we uphold the Panel's finding that Step 2 payments to exporters are contingent upon export performance.⁸¹⁵ According to Brazil, the measure pursuant to which Step 2 payments are granted establishes two mutually exclusive conditions of payment that address two different factual situations where a Step 2 payment can be made.⁸¹⁶ These situations are mutually exclusive because the same bale of cotton cannot be both opened for domestic use and exported.⁸¹⁷ In one situation under the Step 2 measure, proof of exportation is required as a condition of payment. This export contingency is not dissolved because the payment can also be made in another situation to domestic users, on other conditions.⁸¹⁸

566. In addition, Brazil rejects the United States' contention that Step 2 payments are contingent on use and not on exportation. Brazil explains that Step 2 payments do not apply to all United States production of upland cotton because domestic brokers, resellers and other persons not regularly engaged in opening bales of cotton for manufacturing are not eligible to receive the payments.⁸¹⁹ Furthermore, Brazil asserts that, in the case of Step 2 payments to exporters, the payment is not contingent on use because the measure is indifferent to whether, how or when the upland cotton is used so long as it is exported.⁸²⁰

567. The issue raised on appeal is whether the Step 2 payments provided to exporters of United States upland cotton, under Section 1207(a) of the FSRI Act of 2002, are contingent on export performance within the meaning of Article 9.1(a) of the *Agreement on Agriculture* and Article 3.1(a) of the *SCM Agreement*.

⁸¹⁴United States' appellant's submission, para. 443. The United States submits that its position is consistent with the reasoning of the panel in *Canada – Dairy*. (*Ibid.*, para. 444 (relying on Panel Report, *Canada – Dairy*, para. 7.41))

⁸¹⁵Brazil's appellee's submission, para. 872.

⁸¹⁶*Ibid.*, para. 888.

⁸¹⁷*Ibid.*

⁸¹⁸Brazil finds support for its argument in the Appellate Body's reasoning in *US – FSC (Article 21.5 – EC)*. See *supra*, footnote 806. (Brazil's appellee's submission, paras. 883-884)

⁸¹⁹Brazil's appellee's submission, para. 886.

⁸²⁰*Ibid.*, para. 891.

568. Article 9.1(a) of the *Agreement on Agriculture* reads :

[T]he provision by governments or their agencies of direct subsidies, including payments-in-kind, to a firm, to an industry, to producers of an agricultural product, to a cooperative or other association of such producers, or to a marketing board, contingent on export performance[.]

569. Article 3.1(a) of the *SCM Agreement* provides:

Article 3
Prohibition

Except as provided in the Agreement on Agriculture, the following subsidies, within the meaning of Article 1, shall be prohibited:

- (a) subsidies contingent, in law or in fact⁴, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I⁵;

⁴ This standard is met when the facts demonstrate that the granting of a subsidy, without having been made legally contingent upon export performance, is in fact tied to actual or anticipated exportation or export earnings. The mere fact that a subsidy is granted to enterprises which export shall not for that reason alone be considered to be an export subsidy within the meaning of this provision.

⁵ Measures referred to in Annex I as not constituting export subsidies shall not be prohibited under this or any other provision of this Agreement.

570. In previous appeals, the Appellate Body has explained that the WTO-consistency of an export subsidy for agricultural products has to be examined, in the first place, under the *Agreement on Agriculture*⁸²¹; the examination under the *SCM Agreement* would follow if necessary. Turning, then, to the *Agreement on Agriculture*, we note that Article 1(e) of that Agreement defines "export subsidies" as "subsidies contingent upon export performance, including the export subsidies listed in Article 9 of this Agreement".

571. Although an export subsidy granted to agricultural products must be examined, in the first place, under the *Agreement on Agriculture*, we find it appropriate, as has the Appellate Body in previous disputes, to rely on the *SCM Agreement* for guidance in interpreting provisions of the *Agreement on Agriculture*. Thus, we consider the export-contingency requirement in Article 1(e) of

⁸²¹See, for example, Appellate Body Report, *Canada – Dairy (Article 21.5 – New Zealand and US)*, para. 123.

the *Agreement on Agriculture* having regard to that same requirement contained in Article 3.1(a) of the *SCM Agreement*.⁸²²

572. The Appellate Body has indicated, in this regard, that the ordinary meaning of "contingent" is "conditional" or "dependent"⁸²³ and that Article 3.1(a) of the *SCM Agreement* prohibits subsidies that are conditional upon export performance, or are dependent for their existence on export performance.⁸²⁴ It has also emphasized that "a 'relationship of conditionality or dependence', namely that the granting of a subsidy should be 'tied to' the export performance, lies at the 'very heart' of the legal standard in Article 3.1(a) of the *SCM Agreement*".⁸²⁵ We are also mindful that in demonstrating export contingency in the case of subsidies that are contingent in law upon export performance, the "existence of that condition can be demonstrated on the basis of the very words of the relevant legislation, regulation or other legal instrument constituting the measure".⁸²⁶

573. It is clear that the legal provisions pursuant to which Step 2 payments are granted to exporters of United States upland cotton, on their face, apply to exporters of United States upland cotton. Section 1207(a) of the FSRI Act of 2002 provides that, when certain market conditions exist, the United States Secretary of Agriculture:

... shall issue marketing certificates or cash payments, at the option of the recipient, to domestic users and exporters for documented purchases by domestic users and sales for export by exporters. (emphasis added)

The regulations define "eligible exporters" as:

A person, including a producer or a cooperative marketing association ... regularly engaged in selling eligible upland cotton for exportation from the United States (exporter), who has entered into an agreement with CCC⁸²⁷ to participate in the upland cotton user marketing certificate program.⁸²⁸

⁸²² Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 192.

⁸²³ Appellate Body Report, *Canada – Aircraft*, para. 166.

⁸²⁴ Appellate Body Report, *Canada – Aircraft (Article 21.5 – Brazil)*, para. 47. See also Appellate Body Report, *Canada – Aircraft*, para. 166.

⁸²⁵ Appellate Body Report, *Canada – Aircraft (Article 21.5 – Brazil)*, para. 47 (quoting Appellate Body Report, *Canada – Aircraft*, para. 171).

⁸²⁶The legal instrument does not have to provide expressly for the export contingency; the conditionality may be derived by necessary implication from the text of the measure. (Appellate Body Report, *Canada – Autos*, para. 100)

⁸²⁷Additional information about the CCC is provided, *infra*, footnote 859; see also Panel Report, para. 7.702.

⁸²⁸7 CFR Section 1427.104(a)(2).

"Eligible upland cotton" is defined as "domestically produced baled upland cotton which bale is opened by an eligible domestic user ... or exported by an eligible exporter."⁸²⁹

574. Furthermore, in order to claim Step 2 payments, exporters must submit an application and provide supporting documentation to the CCC, including "proof of export of eligible cotton by the exporter."⁸³⁰ This provision confirms that the payment is "tied to" exportation. As the Panel explained, "a condition of the receipt of user marketing (Step 2) payments to exporters under section 1207(a) of the FSRI Act of 2002 will always and inevitably be proof of exportation."⁸³¹ Thus, on the face of the statute and regulations pursuant to which Step 2 payments are granted to exporters, the payments are "conditional upon export performance" or "dependent for their existence on export performance."⁸³²

575. The United States directed the Panel's attention to the fact that the same statute and regulations also provide for similar payments to domestic users conditioned on the domestic use of United States upland cotton. According to the United States, Step 2 payments to exporters and domestic users are governed by a single legislative provision and a single set of regulations. In addition, the form and payment rate to domestic users and exporters are identical, and the payments are made from a single fund.⁸³³ As Step 2 payments are available to both domestic users and exporters, the United States submits that exportation is not a condition to receive payment and, therefore, the payments are not export-contingent.⁸³⁴

576. We are not persuaded by the United States' arguments. Like the Panel, we recognize that Step 2 payments to exporters and domestic users are governed by a single legislative provision and a single set of regulations, that the form and rate of payment to exporters and domestic users are identical, and that the fund from which payments are made is a single fund.⁸³⁵ Nevertheless, we agree with the Panel that the statute and regulations pursuant to which Step 2 payments are granted do not establish a "single class" of recipients of the payments; rather, the statute and regulations clearly distinguish between two types of eligible recipients, namely, eligible exporters and eligible domestic users.⁸³⁶ As we have seen, an eligible exporter must be "[a] person, including a producer or a

⁸²⁹7 CFR Section 1427.103(a). (emphasis added)

⁸³⁰7 CFR Section 1427.108(d).

⁸³¹Panel Report, para. 7.734.

⁸³²See Appellate Body Report, *Canada – Aircraft (Article 21.5 – Brazil)*, para. 47.

⁸³³United States' appellant's submission, para. 442.

⁸³⁴*Ibid.*, para. 454.

⁸³⁵Panel Report, para. 7.709.

⁸³⁶*Ibid.*, paras. 7.721-7.723.

cooperative marketing association ... regularly engaged in selling eligible upland cotton for exportation from the United States".⁸³⁷ In contrast, an "eligible domestic user" is "[a] person regularly engaged in the business of opening bales of eligible upland cotton for the purpose of manufacturing such cotton into cotton products in the United States".⁸³⁸ Thus, the statute and regulations themselves clearly distinguish between exporters and domestic users.

577. In addition, the statute and regulations establish different conditions that eligible exporters and eligible domestic users must meet to receive Step 2 payments. An eligible domestic user must "open" a bale of cotton to qualify for payment.⁸³⁹ For its part, an eligible exporter must demonstrate the upland cotton has been exported. These are distinct conditions that the statute and regulations themselves set out for the two distinct recipients of Step 2 payments. Because the conditions to qualify for payment are different, the documentation required from eligible domestic users and eligible exporters is also different. An eligible exporter must submit proof of exportation; an eligible domestic user must provide documentation indicating the number of bales opened.⁸⁴⁰ We agree, therefore, with the Panel's view that the statute and regulations pursuant to which Step 2 payments are granted "involve[] payment to two distinct sets of recipients (exporters or domestic users) in two distinct factual situations (export or domestic use)".⁸⁴¹

578. Furthermore, we agree with the Panel's conclusion that the fact that the subsidy is also available to domestic users of upland cotton does not "dissolve" the export-contingent nature of the Step 2 payments to exporters.⁸⁴² The Panel's reasoning is consistent with the approach taken by the Appellate Body in *US – FSC (Article 21.5 – EC)*.⁸⁴³ In that case, the United States argued that the tax exclusion at issue was not an export-contingent subsidy because it was available for both (i) property produced within the United States and held for use outside the United States and (ii) property produced outside the United States and held for use outside the United States. The United States

⁸³⁷7 CFR Section 1427.104(a)(2). (emphasis added)

⁸³⁸7 CFR Section 1427.104(a)(1).

⁸³⁹United States' response to questioning at oral hearing. 7 CFR Section 1427.103(a).

⁸⁴⁰Panel Report, para. 7.727.

⁸⁴¹*Ibid.*, para. 7.732.

⁸⁴²*Ibid.*, para. 7.739.

⁸⁴³The Panel also found support for its reasoning in the Appellate Body's statement, in *Canada – Aircraft*, that:

... the fact that some of TPC's contributions, in some industry sectors, are not contingent upon export performance, does not necessarily mean that the same is true for all of TPC's contributions. It is enough to show that one or some of TPC's contributions do constitute subsidies "contingent ... in fact ... upon export performance".

(Appellate Body Report, *Canada – Aircraft*, para. 179) (original emphasis)

asserted that, as the tax exemption was available in both circumstances, it was "export-neutral".⁸⁴⁴ According to the United States, the panel's separate examination of each situation in which the tax exemption was available "artificially bifurcat[ed]" the measure.⁸⁴⁵

579. The Appellate Body rejected the United States' contention in *US – FSC (Article 21.5 – EC)* because it considered it necessary, under Article 3.1(a) of the *SCM Agreement*, "to examine separately the conditions pertaining to the grant of the subsidy in the two different situations".⁸⁴⁶ It then confirmed the Panel's finding that the tax exemption in the first situation, namely for property produced within the United States and held for use outside the United States, is an export-contingent subsidy.⁸⁴⁷ In its reasoning, the Appellate Body explained that whether or not the subsidies were export-contingent in both situations envisaged by the measure would not alter the conclusion that the tax exemption in the first situation was contingent upon export:

Our conclusion that the ETI measure grants subsidies that are export contingent in the first set of circumstances is not affected by the fact that the subsidy can also be obtained in the second set of circumstances. The fact that the subsidies granted in the second set of circumstances *might* not be export contingent does not dissolve the export contingency arising in the first set of circumstances. Conversely, the export contingency arising in these circumstances has no bearing on whether there is an export contingent subsidy in the second set of circumstances.⁸⁴⁸

580. As in *US – FSC (Article 21.5 – EC)*, the Panel in this case found that Step 2 payments are available in two situations, only one of which involves export contingency.⁸⁴⁹ The Panel's conclusion, therefore, is consistent with the Appellate Body's holding in *US – FSC (Article 21.5 – EC)* quoted above that "the fact that the subsidies granted in the second set of circumstances *might* not be export contingent does not dissolve the export contingency arising in the first set of circumstances".

581. The United States submits that the facts in this case are similar to those before the panel in *Canada – Dairy*.⁸⁵⁰ In that dispute, the complaining parties argued that the provision of milk to exporters/processors under various mechanisms (described as "special milk classes") constituted

⁸⁴⁴ Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 110.

⁸⁴⁵ *Ibid.*

⁸⁴⁶ *Ibid.*, para. 115.

⁸⁴⁷ *Ibid.*, para. 120.

⁸⁴⁸ *Ibid.*, para. 119. (original emphasis; footnote omitted)

⁸⁴⁹ See, *supra*, para. 577.

⁸⁵⁰ United States' appellant's submission, paras. 444–445 (referring to Panel Report, *Canada – Dairy*, para. 7.41 and footnote 496 to para. 7.124).

export-contingent subsidies. The panel in *Canada – Dairy* found, nevertheless, that certain special milk classes were *not* export-contingent because the "milk under such other classes is also available (often exclusively) to processors which produce for the domestic market".⁸⁵¹ The Panel, in this dispute, did not see any relevance in the Panel Report in *Canada – Dairy* because, in that case, "there was no explicit condition limiting a discrete segment of the payments of the subsidies concerned to exporters".⁸⁵² Brazil also seeks to distinguish the factual situation in *Canada – Dairy*, explaining that it involved a single regulatory class of milk instead of two mutually exclusive regulatory categories, as is the case in the present dispute.⁸⁵³ We agree with the Panel and Brazil that the facts in *Canada – Dairy* differ from those of the present dispute. In this case, we have before us a statute and regulations that clearly distinguish between two sets of recipients—that is, eligible exporters and eligible domestic users—that must meet different conditions to receive payment.⁸⁵⁴ In the case of one set of recipients, eligible exporters, exportation is a necessary condition to receive payment.

582. In sum, we agree with the Panel's view that Step 2 payments are export-contingent and, therefore, an export subsidy for purposes of Article 9 of the *Agreement on Agriculture* and Article 3.1(a) of the *SCM Agreement*. The statute and regulations pursuant to which Step 2 payments are granted, on their face, condition payments to exporters on exportation.⁸⁵⁵ In order to claim payment, an exporter must show proof of exportation. If an exporter does not provide proof of exportation, the exporter will not receive a payment. This is sufficient to establish that Step 2 payments to exporters of United States upland cotton are "conditional upon export performance" or "dependent for their existence on export performance".⁸⁵⁶ That domestic users may also be eligible to receive payments under different conditions does not eliminate the fact that an exporter will receive payment only upon proof of exportation.

583. For these reasons, we *uphold* the Panel's findings, in paragraphs 7.748–7.749 and 8.1(e) of the Panel Report, that Step 2 payments to exporters of United States upland cotton, pursuant to Section 1207(a) of the FSRI Act of 2002, constitute subsidies contingent upon export performance within the meaning of Article 9.1(a) of the *Agreement on Agriculture* and that, therefore, in providing such subsidies the United States has acted inconsistently with its obligations under Articles 3.3 and 8 of the *Agreement on Agriculture*.

⁸⁵¹ Panel Report, *Canada – Dairy*, para. 7.41.

⁸⁵² Panel Report, para. 7.718.

⁸⁵³ Brazil's appellee's submission, paras. 898–899.

⁸⁵⁴ See *supra*, para. 577.

⁸⁵⁵ Panel Report, para. 7.734.

584. Having explained that there is no reason to read the export-contingency requirement in the *Agreement on Agriculture* differently from that contained in Article 3.1(a) of the *SCM Agreement*,⁸⁵⁷ and having found that Step 2 payments to exporters of United States upland cotton are contingent upon export performance within the meaning of Article 9.1 of the *Agreement on Agriculture*, we also find that such payments are export-contingent for purposes of Article 3.1(a) of the *SCM Agreement*.⁸⁵⁸ Consequently, we uphold the Panel's findings, in paragraphs 7.760-7.761 and 8.1(e) of the Panel Report, that Step 2 payments provided to exporters of United States upland cotton, pursuant to Section 1207(a) of the FSRI Act of 2002, are inconsistent with Articles 3.1(a) and 3.2 of the *SCM Agreement*.

C. *Export Credit Guarantees – Article 10.2 of the Agreement on Agriculture*

585. We turn next to the United States' and Brazil's appeals of the Panel's findings relating to the United States' export credit guarantee programs.

I. United States' Export Credit Guarantee Programs

586. Brazil challenges three types of export credit guarantee programs. The first two programs, GSM 102 and GSM 103, provide guarantees to exporters when credit is extended by foreign financial institutions. The third type, the SCGP, applies when credit is extended by the exporter to the purchaser of United States agricultural products.⁸⁵⁹

587. The GSM 102 program is available to cover commercial exports of United States agricultural commodities on credit terms of between 90 days and 3 years. To obtain the credit guarantee under GSM 102, the exporter must have received a letter of credit in its favour from the foreign bank and must apply for the guarantee before making the exportation. The exporter will pay a fee for the

⁸⁵⁶See Appellate Body Report, *Canada – Aircraft (Article 21.5 – Brazil)*, para. 47.

⁸⁵⁷See *supra*, para. 571.

⁸⁵⁸As the Panel observed, pursuant to Article 13(c)(ii) of the *Agreement on Agriculture*, "to the extent that the export subsidy at issue does not conform fully to the provisions of Part V of the *Agreement on Agriculture*, it is not exempt from actions based on Articles 3.1(a) and 3.2 of the *SCM Agreement*". (Panel Report, para. 7.751)

⁸⁵⁹These export credit guarantee programs are established under Section 5622 of Title 7 of the United States Code and implemented in Part 1493 of Title 7 of the United States Code of Federal Regulations. (See Panel Report, para. 7.250(vii)) Subpart B of Part 1493 relates to the GSM 102 and the GSM 103 programs and Subpart D deals with the SCGP program. GSM 102 and 103 export credit guarantees have been issued since late 1980, while the SCGP program began in 1996. (United States' first written submission to the Panel, paras. 151 and 152 and footnote 133 thereto) Export credit guarantee programs are administered through the CCC, created under the Commodity Credit Corporation Charter Act of 1948. The CCC is a federal corporation established within the USDA. (Panel Report, para. 7.236 and footnote 346 thereto) A further description of the GSM 102, GSM 103 and SCGP is provided in Panel Report, paras. 7.236-7.244.

guarantee based on a schedule of rates that vary according to the credit period, but are capped by law at one per cent of the guaranteed dollar value of the transaction. In the event that the foreign bank fails to make a payment, the exporter informs the CCC of the default and "[t]he CCC generally covers 98 per cent of the principal and a portion of the interest".⁸⁶⁰

588. The GSM 103 is similar to the GSM 102. The difference between the two programs is that GSM 103 guarantees export credits that have longer terms. Specifically, GSM 103 guarantees credits with terms of between 3 and 10 years. An additional difference is that, contrary to GSM 102, the fee that an exporter must pay to obtain a guarantee under GSM 103 is not capped by law.

589. The SCGP guarantees credits extended by the exporter itself to foreign buyers of United States agricultural commodities. Under the SCGP, the United States exporter is required to submit to the CCC a promissory note signed by the importer prior to exportation. The exporter will pay a fee at a rate that varies according to the term of the loan, and, like GSM 102, is capped by law at one per cent of the guaranteed dollar value of the transaction. If the importer defaults on the promissory note, then the CCC will pay the exporter 65 per cent of the dollar value of the exported product (excluding interest).

2. Panel Findings

590. Before the Panel, Brazil asserted that these three United States export credit guarantee programs—GSM 102, GSM 103 and SCGP—violate Articles 10.1 and 8 of the *Agreement on Agriculture* and are therefore not exempt, under Article 13(c)(ii) of the *Agreement on Agriculture*, from actions based on Articles 3.1(a) and 3.2 of the *SCM Agreement*.⁸⁶¹ Brazil also argued that the three programs violate Articles 3.1(a) and 3.2 of the *SCM Agreement*.⁸⁶²

591. The United States responded that Article 10.2 of the *Agreement on Agriculture* makes it clear that the export subsidy disciplines in the *Agreement on Agriculture* and the *SCM Agreement* are not applicable to export credit guarantee programs. According to the United States, Article 10.2 of the *Agreement on Agriculture* "reflects the deferral of disciplines on export credit guarantee programs contemplated by WTO Members".⁸⁶³ The United States argued that, even if the export subsidy disciplines in the *SCM Agreement* were applicable, its export credit guarantee programs are not prohibited export subsidies under Article 3.1(a) because they do not meet the criteria in item (j) of

⁸⁶⁰Panel Report, para. 7.242.

⁸⁶¹Panel Report, para. 7.765.

⁸⁶²*Ibid.*, para. 7.765.

⁸⁶³United States' first written submission to the Panel, para. 160 (quoted in Panel Report, para. 7.770).

the Illustrative List of Export Subsidies attached to the *SCM Agreement* as Annex I, namely that the premiums are inadequate to cover the programs' long-term operating costs and losses.⁸⁶⁴

592. At the outset of its analysis, the Panel observed that it would adopt the parties' shared view that "export credit guarantees are not included in the non-exhaustive list of export subsidies in Article 9.1, and that Article 10 of the *Agreement on Agriculture* is the relevant provision".⁸⁶⁵ The Panel then stated that Article 10.1 "covers any subsidy contingent on export performance that is not listed in Article 9.1".⁸⁶⁶ The Panel observed that, other than the list of export subsidies listed in Article 9.1, the *Agreement on Agriculture* does not specify what is a subsidy contingent upon export performance.⁸⁶⁷ Thus, the Panel sought contextual guidance in the *SCM Agreement*, to assist it in its interpretation of the term "export subsidies" in Article 10.1 of the *Agreement on Agriculture*. In particular, the Panel looked at item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement*, observing that "there is no disagreement between the parties ... that, if an export credit guarantee programme meets the elements of item (j), it is a *per se* export subsidy".⁸⁶⁸

593. The Panel then examined whether the United States' export credit guarantee programs challenged by Brazil met the criteria set out in item (j) and concluded that:

On the basis of the totality of the record evidence, including approaches regularly relied upon by the United States government itself, we find that Brazil has established that the United States CCC provides the GSM 102, GSM 103 and SCGP export credit guarantee programmes "at premium rates which are inadequate to cover the long-term operating costs and losses of the programmes" within the meaning of item (j) of the Illustrative List of Export Subsidies in Annex I of the *SCM Agreement*.⁸⁶⁹

594. Having reached this general conclusion, the Panel next examined Brazil's claims that the United States' export credit guarantees "result[] in" or "threaten[] to lead to" circumvention of the United States' export subsidy commitments, contrary to Article 10.1 of the *Agreement on Agriculture*. In its analysis, the Panel distinguished between, on the one hand, "supported" and "unsupported" products, and, on the other, "scheduled" and "unscheduled" products. The Panel used the term "supported products" to refer to products for which there was evidence in the record showing that they

were not only eligible under the programs, but that export credit guarantees were in fact received in connection with exports of those products.⁸⁷⁰ "Scheduled products" are those for which a WTO Member has assumed a commitment to limit the amount of export subsidies in terms of budgetary outlays and quantities exported pursuant to Articles 3, 8, and 9 of the *Agreement on Agriculture*.⁸⁷¹

595. The Panel found that, "in respect of upland cotton and other such [supported] *unscheduled* agricultural products on record, the United States applies export credit guarantees constituting export subsidies in a manner which results in circumvention of its export subsidy commitments inconsistently with Article 10.1 of the *Agreement on Agriculture*".⁸⁷² In addition, the Panel found that "the United States has applied export credit guarantees constituting export subsidies within the meaning of Article 10.1 – and therefore, necessarily, not listed in Article 9.1 – in a manner which results in circumvention of export subsidy commitments in respect of" rice (a scheduled commodity).⁸⁷³ The Panel, nonetheless, found that "[i]t has not been established, however, that such actual circumvention has resulted in respect of the twelve other United States scheduled commodities".⁸⁷⁴ Finally, the Panel "decline[d] to find that the export credit guarantee programmes at issue are generally applied to scheduled agricultural products other than rice and other unscheduled agricultural products (not supported under the programmes) in a manner which threatens to lead to circumvention of United States' export subsidy commitments within the meaning of Article 10.1 of the *Agreement on Agriculture*".⁸⁷⁵

596. After making these findings, the Panel turned to the United States' argument that "the text of Article 10.2 of the *Agreement on Agriculture* reflects the deferral of disciplines on export credit guarantee programmes contemplated by [WTO] Members".⁸⁷⁶ This argument was rejected by the

⁸⁷⁰*Ibid.*, para. 6.32; see also footnote 1056 to para. 7.875. At the oral hearing, the participants confirmed that this is also their understanding of what the Panel meant by the distinction that it drew between "supported" and "unsupported" products. In respect of "supported" products, the Panel stated that "[t]o the extent that it identifies products within the product coverage of the *Agreement on Agriculture* that are within our terms of reference, we consider Exhibit BRA-73 to be the relevant record evidence of such products for the purposes of this dispute". (Panel Report, footnote 1056 to para. 7.875; see also *ibid.*, footnote 1575 to para. 8.1(d)(i))

⁸⁷¹The Panel noted that "[t]he United States has scheduled export subsidy reduction commitments in respect of the following thirteen commodities: wheat, coarse grains, rice, vegetable oils, butter and butter oil, skim milk powder, cheese, other milk products, bovine meat, pigmeat, poultry meat, live dairy cattle, eggs". (Panel Report, footnote 1057 to para. 7.876 (referring to Schedule XX of the United States of America, Part IV, Section II, entitled "Export Subsidies: Budgetary Outlays and Quantitative Reduction Commitments", reproduced in Exhibit BRA-83 and Exhibit US-13))

⁸⁷²Panel Report, para. 7.875. (original emphasis)

⁸⁷³Panel Report, para. 7.881.

⁸⁷⁴*Ibid.*

⁸⁷⁵*Ibid.*, para. 7.896.

⁸⁷⁶*Ibid.*, para. 7.900.

⁸⁶⁴Panel Report, para. 7.772.

⁸⁶⁵*Ibid.*, para. 7.788.

⁸⁶⁶*Ibid.*, para. 7.796.

⁸⁶⁷*Ibid.*, para. 7.797.

⁸⁶⁸*Ibid.*, para. 7.803.

⁸⁶⁹Panel Report, para. 7.867.

Panel, which was of the opposite view, namely, that the text of Article 10.1 "clearly indicat[es] that export credit guarantee programmes constituting export subsidies for the purposes of Article 10.1 must not be applied in a manner which results in, or which threatens to lead to, circumvention of export subsidy commitments".⁸⁷⁷ The Panel found support for this interpretation in the provision's context and in its object and purpose, emphasizing in particular that Article 10.2 is a subparagraph of Article 10. According to the Panel, "[t]he title of Article 10, and the text of Article 10.1, indicates an intention to prevent Members from circumventing or 'evading' their 'export subsidy commitments'".⁸⁷⁸ The Panel also rejected the United States' arguments based on subsequent practice and the drafting history.⁸⁷⁹ In respect of the United States' argument on subsequent practice, the Panel stated that "[t]he record ... does not suggest that there is a discernible pattern of acts or pronouncements implying an agreement among WTO Members on the United States' interpretation of Article 10.2".⁸⁸⁰ Although the Panel did not see a need to examine the drafting history, it found that "nothing in the drafting history of [Article 10.2] would compel [the Panel] to reach a different conclusion".⁸⁸¹

597. Finally, the Panel turned to Brazil's claims under Articles 3.1(a) and 3.2 of the *SCM Agreement*, and found:

To the extent that the United States export credit guarantee programmes at issue – GSM 102, GSM 103 and SCGP – do not conform fully to these provisions in Part V of the *Agreement on Agriculture* and do not benefit from the exemption from actions provided by Article 13(c)(ii) of the *Agreement on Agriculture*, they are also export subsidies prohibited by Article 3.1(a) ...

To the extent that the three United States export credit guarantee programmes at issue are inconsistent with Article 3.1(a), they are, consequently, also inconsistent with Article 3.2 of the *SCM Agreement*.⁸⁸²

⁸⁷⁷ *Ibid.*, para. 7.901.

⁸⁷⁸ *Ibid.*, para. 7.912. (footnote omitted)

⁸⁷⁹ *Ibid.*, paras. 7.928-7.944.

⁸⁸⁰ *Ibid.*, para. 7.929. (footnotes omitted)

⁸⁸¹ Panel Report, para. 7.933. The Panel did not see a need to examine the drafting history because it considered that its "examination of the text of Article 10.2 of the *Agreement on Agriculture*, in its context and in light of the object and purpose of that agreement leads to a clear interpretation of the text". (Panel Report, para. 7.933)

⁸⁸² *Ibid.*, paras. 7.947 and 7.948. (footnote omitted)

3. Arguments on Appeal

598. The United States contends that the Panel erred in analyzing whether export credit guarantees are export subsidies subject to the disciplines of Article 10.1 solely by reference to the *SCM Agreement*. According to the United States, the proper context in which to analyze the meaning of Article 10.1 with respect to export credit guarantees is Article 10.2 of the *Agreement on Agriculture*.⁸⁸³ This provision reflects the fact that, during the Uruguay Round, WTO Members did not agree on disciplines to be applied to agricultural export credits, export credit guarantees, and insurance programs, opting instead to continue discussions, deferring the imposition of substantive disciplines until a consensus was achieved.

599. According to the United States, this interpretation of Article 10.2 is consistent with Article 10 as a whole.⁸⁸⁴ Article 10.2 contributes to the prevention of circumvention of export subsidy commitments by imposing two obligations on Members: first, they must undertake to work toward the development of internationally agreed disciplines on export credit guarantees; and second "after agreement on such disciplines", they must provide export credit guarantees "only in conformity therewith".⁸⁸⁵ Moreover, excluding export credit guarantees from the application of Article 10.1 is also consistent with the treatment of food aid transactions under Article 10. Because Article 10.4 of the *Agreement on Agriculture* does not explicitly exempt food aid transactions from the applicability of Article 10.1, the Panel's interpretative approach would mean that all food aid transactions constitute export subsidies under Article 10.1.⁸⁸⁶

600. The United States submits that the negotiating history confirms its interpretation that Article 10.2 makes the export subsidy disciplines in Article 10.1 inapplicable to export credit guarantees.⁸⁸⁷ In addition, the United States argues that it defies logic, as well as the object and purpose of the *Agreement on Agriculture*, to take the view of the Panel whereby export credit guarantees, export credits and insurance programs would be treated as already disciplined export subsidies, yet would not be permitted to be included within the applicable reduction commitments expressly contemplated by the text.⁸⁸⁸ The United States therefore requests that we reverse the Panel's finding that export credit guarantees are subject to the disciplines of Article 10.1. In addition, the United States requests that we reverse the Panel's findings that export credit guarantees to

⁸⁸³ United States' appellant's submission, para. 341.

⁸⁸⁴ *Ibid.*, para. 346.

⁸⁸⁵ Quoting Article 10.2 of the *Agreement on Agriculture*.

⁸⁸⁶ United States' appellant's submission, paras. 349 and 358.

⁸⁸⁷ *Ibid.*, paras. 367-380.

⁸⁸⁸ *Ibid.*, paras. 384-385.

agricultural commodities are subject to Articles 3.1 and 3.2 of the *SCM Agreement*. The United States asserts that, because export credit guarantees currently are not subject to export subsidy disciplines under the *Agreement on Agriculture*, the export subsidy disciplines of the *SCM Agreement* are also inapplicable to these measures pursuant to Article 21.1 of the *Agreement on Agriculture* and the introductory language of Article 3.1 of the *SCM Agreement*.⁸⁸⁹

601. Brazil requests that we reject the United States' appeal from the Panel's finding that export credit guarantees are subject to the export subsidy disciplines in Article 10.1 of the *Agreement on Agriculture*. Brazil asserts that subsidized export credit guarantees are covered by the general definition of "export subsidies" under Article 1(e) of the *Agreement on Agriculture* and that these measures are, therefore, subject to Article 10.1 of the *Agreement on Agriculture*, unless an exception is provided in Article 10.2.⁸⁹⁰ The text of Article 10.2 establishes two obligations, but does not provide an exception.⁸⁹¹

602. According to Brazil, the Panel's interpretation is consistent with the context and object and purpose of Article 10.2. Each of the paragraphs in Article 10 pursues the aim of "preventing circumvention" of export subsidy commitments and, thereby, contributes to the purpose of the *Agreement on Agriculture* of establishing specific binding commitments on export competition. Therefore, Article 10.2 also must be interpreted in a manner that ensures that it contributes to the purpose of preventing circumvention of commitments on export competition.⁸⁹² The United States' interpretation of Article 10.2 would tend in the opposite direction, leaving Members free to grant unlimited export subsidies in the form of export credit guarantees and would permit wholesale circumvention of commitments.⁸⁹³ Brazil, furthermore, disagrees with the United States' assertion that the Panel's interpretation is an "assault" on international food security.⁸⁹⁴ According to Brazil, food aid is subject to the specific disciplines in Article 10.4 of the *Agreement on Agriculture*, as well as to the general disciplines in Article 10.1.⁸⁹⁵

603. In addition, Brazil disagrees with the conclusions drawn by the United States from the negotiating history of the *Agreement on Agriculture*.⁸⁹⁶ Brazil also rejects the United States'

contention that the Panel's reading of Article 10.2 is "manifestly unreasonable".⁸⁹⁷ Brazil explains that, at the close of the Uruguay Round, Members agreed that they would calculate their respective export subsidy commitment levels using exclusively the export subsidies listed in Article 9.1 and thus chose to leave out of the calculation export subsidies referred to in Article 10.1. Finally, Brazil emphasizes that the Panel's interpretation does not mean that Members cannot grant export credit guarantees. Instead, it means that subsidized export credit guarantees are subject to disciplines as trade-distorting measures, and cannot be used to override export subsidy commitments.⁸⁹⁸

604. Argentina, Australia, Canada, and New Zealand are of the view that Article 10.2 of the *Agreement on Agriculture* does not provide an exception from WTO export subsidy disciplines for export credit guarantees, export credits or insurance programs, and assert that the Panel correctly interpreted this provision.⁸⁹⁹ Before the Panel, the European Communities submitted that Article 10.2 of the *Agreement on Agriculture* cannot be seen as exempting export credit guarantees granted to agricultural products from WTO disciplines as this provision makes it clear that export credit guarantees are not one of the types of export subsidies listed in Article 9.1 that a Member is given a limited authorization to apply⁹⁰⁰, the European Communities did not express a view on this issue on appeal.

4. Does Article 10.2 Exempt Export Credit Guarantee Programs from Export Subsidy Disciplines?⁹⁰¹

605. The United States argues that because export credit guarantees are specifically dealt with in Article 10.2, and this provision expressly acknowledges that Uruguay Round negotiators did not reach an agreement on the disciplines that apply to them, they cannot properly be considered to be included within the "export subsidies" covered by Article 10.1.

606. As usual, our analysis begins with the text of the provision in question. Article 10.2 reads:

Members undertake to work toward the development of internationally agreed disciplines to govern the provision of export credits, export credit guarantees or insurance programmes and, after

⁸⁸⁹*Ibid.*, paras. 926-934 (referring to the United States' appellant's submission, para. 384).

⁸⁸⁸*Ibid.*, paras. 977-978.

⁸⁸⁹Argentina's third participant's submission, para. 39; Australia's third participant's submission, para. 71; Canada's third participant's submission, para. 42; and New Zealand's third participant's submission, para. 3.65.

⁹⁰⁰Panel Report, para. 7.781.

⁹⁰¹A separate opinion on this issue of one of the Members of the Division is set out *infra*, paras. 631-641. The relevant findings and conclusions for purposes of the recommendations and rulings to be adopted by the DSB in this dispute, pursuant to Article 17.14 of the DSU, are those set out in paragraph 763(e) and (f) of this Report.

agreement on such disciplines, to provide export credits, export credit guarantees or insurance programmes only in conformity therewith.

607. Article 10.2 refers expressly to export credit guarantee programs, along with export credits and insurance programs. Under Article 10.2, WTO Members have taken on two distinct commitments in respect of these three types of measures: (i) to work toward the development of internationally agreed disciplines to govern their provision; and (ii) after agreement on such disciplines, to provide them only in conformity therewith. The text includes no temporal indication with respect to the first commitment. There is no deadline for beginning or ending the negotiations. The second commitment does have a temporal connotation, in the sense that it is triggered only "after agreement on such disciplines". This means that "after" international disciplines have been agreed upon, Members shall provide export credit guarantees, export credits and insurance programs only in conformity with those agreed disciplines. There is no dispute between the parties that, to date, no disciplines have been agreed internationally pursuant to Article 10.2.

608. Article 10.2 does not, however, expressly define the disciplines that *currently* apply to export credits, export credit guarantees and insurance programs under the *Agreement on Agriculture*. The Panel reasoned that "in order to carve out or exempt particular categories of measures from general obligations such as the prevention of circumvention of export subsidy commitments in Article 10.1 of the *Agreement on Agriculture*, it would be reasonable to expect an explicit indication revealing such an intention in the text of the Agreement".⁹⁰² The Panel saw "no language in Article 10.2 which would modify the scope of application of the general export subsidy disciplines in Article 10.1 in the *Agreement on Agriculture* so as to carve out or exempt export credit guarantees from the export subsidy disciplines imposed by that Agreement".⁹⁰³

609. We agree with the Panel's view that Article 10.2 does not expressly exclude export credit guarantees from the export subsidy disciplines in Article 10.1 of the *Agreement on Agriculture*. As the Panel observes, were such an exemption intended, it could have been easily achieved by, for example, inserting the words "[n]otwithstanding the provisions of Article 10.1", or other similar language at the beginning of Article 10.2.⁹⁰⁴ Article 10.2 does not include express language suggesting that it is intended as an exception, nor does it expressly state that the application of any export subsidy disciplines to export credits or export credit guarantees is "deferred", as the United States suggests. Given that the drafters were aware that subsidized export credit guarantees, export credits and insurance programs could fall within the export subsidy disciplines in the *Agreement on Agriculture* and the *SCM Agreement*, it would be expected that an exception would have been clearly provided had this been the drafters' intention.

610. Moreover, as the Panel explained, Article 10.2 "contrasts starkly with the text of other provisions in the covered agreements, which clearly carve out or exempt certain products or measures from certain obligations that would otherwise apply pending the development of further multilateral disciplines".⁹⁰⁵ The Panel referred to Article 6.1(a) and the footnote 24 to Article 8.2(a) of the *SCM Agreement* and Article XIII of the *General Agreement on Trade in Services*, which expressly indicate that existing disciplines do not apply pending the negotiation of future disciplines.⁹⁰⁶ However, Article 10.2 does not expressly exclude the application of the existing disciplines in the *Agreement on Agriculture* until such time as the specific disciplines on export credits, export credit guarantees and insurance programs are internationally agreed upon.

⁹⁰²Panel Report, para. 7.903. (footnote omitted)

⁹⁰³*Ibid.*, para. 7.904.

⁹⁰⁴*Ibid.*, para. 7.909.

⁹⁰⁵*Ibid.*, para. 7.906.

⁹⁰⁶*Ibid.*, paras. 7.907-7.908.

611. The Panel rejected the United States' submission⁹⁰⁷ that Brazil's approach would render Article 10.2 irrelevant.⁹⁰⁸ In the Panel's view, "the purpose of any eventual disciplines could be further to facilitate the determination of when export credit guarantee programmes in respect of agricultural products constitute export subsidies *per se* by developing and refining existing disciplines".⁹⁰⁹ Put another way, "the work envisaged in Article 10.2 would presumably elaborate further and more specific disciplines that could facilitate identification of the extent to which such export credit guarantee programmes constitute export subsidies, or to what extent export credit guarantee programmes are not permitted".⁹¹⁰ The use of the term "development" in Article 10.2 is consistent with this view. The definitions of the term "development" include: "[t]he action or process of developing; evolution, growth, maturation; ... a gradual unfolding, a fuller working-out" and "[a] developed form or product ... an addition, an elaboration".⁹¹¹ This suggests that the disciplines to be internationally agreed will be an elaboration of the export subsidy disciplines that are currently applicable.

612. This interpretation is consistent with the reference in Article 10.2 to internationally agreed disciplines "to govern the provision of" export credits, export credit guarantees or insurance programs; alternatively, Article 10.2 could have referred to internationally agreed disciplines "to govern" export credits, export credit guarantees or insurance programs. The latter formulation ("to govern") would have been broader in scope, whereas the formulation used in Article 10.2 ("to govern the provision") is narrower. If the drafters had intended that currently no disciplines at all would apply to export credit guarantees, export credits and insurance programs, it would have made more sense for them to have chosen the broader formulation "to govern". The drafter's choice of the narrower formulation "to govern the provision of" suggests that export credit guarantees, export credits and insurance programs are not "undisciplined" in all respects, and that the disciplines to be developed have to do *only* with their *provision*. In other words, export credit guarantees, export credits and insurance programs are governed by Article 10.1 of the *Agreement on Agriculture*, but WTO Members will develop specific disciplines on the provision of these instruments.

⁹⁰⁷United States' first written submission to the Panel, paras. 163-165.

⁹⁰⁸Panel Report, para. 7.925.

⁹⁰⁹*Ibid.*

⁹¹⁰*Ibid.*, para. 7.926. (footnote omitted)

⁹¹¹*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 1, p. 662.

613. The Panel's interpretation of Article 10.2, which is based on a plain reading of the text, is confirmed when, in accordance with the customary rules of treaty interpretation codified in Article 31 of the *Vienna Convention*, that provision is examined in its context and in the light of the object and purpose of the *Agreement on Agriculture*, and in particular Article 10, which is entitled "Prevention of Circumvention of Export Subsidy Commitments".

614. We note that Article 10.1 of the *Agreement on Agriculture*, the provision that immediately precedes Article 10.2, reads:

Export subsidies not listed in paragraph 1 of Article 9 shall not be applied in a manner which results in, or which threatens to lead to, circumvention of export subsidy commitments; nor shall non-commercial transactions be used to circumvent such commitments.

615. Although Article 10.2 commits WTO Members to work toward the development of internationally agreed disciplines on export credit guarantees, export credits and insurance programs, it is in Article 10.1 that we find the disciplines that currently apply to export subsidies not listed in Article 9.1. A plain reading of Article 10.1 indicates that the only export subsidies that are excluded from its scope are those "listed in paragraph 1 of Article 9". The United States and Brazil agreed that export credit guarantees are not listed in Article 9.1.⁹¹² Thus, to the extent that an export credit guarantee meets the definition of an "export subsidy" under the *Agreement on Agriculture*, it would be covered by Article 10.1. Article 1(c) of the *Agreement on Agriculture* defines "export subsidies" as "subsidies contingent upon export performance, including the export subsidies listed in Article 9 of this Agreement". (emphasis added) The use of the word "including" suggests that the term "export subsidies" should be interpreted broadly and that the list of export subsidies in Article 9 is not exhaustive. Even though an export credit guarantee may not necessarily include a subsidy component, there is nothing inherent about export credit guarantees that precludes such measures from falling within the definition of a subsidy.⁹¹³ An export credit guarantee that meets the definition of an export subsidy would be covered by Article 10.1 of the *Agreement on Agriculture* because it is not an export subsidy listed in Article 9.1 of that Agreement.

⁹¹²Panel Report, para. 7.788.

⁹¹³For discussion of the definitional elements of a subsidy in the context of the *Agreement on Agriculture*, see Appellate Body Report, *US – FSC*, para. 136, and Appellate Body Report, *Canada – Dairy*, para. 87.

616. We find it significant that paragraph 2 of Article 10 is included in an Article that is titled the "Prevention of Circumvention of Export Subsidy Commitments". As Brazil correctly points out, each paragraph in Article 10 pursues this aim.⁹¹⁴ Article 10.1 provides that WTO Members shall not apply export subsidies not listed in Article 9.1 of the *Agreement on Agriculture* "in a manner which results in, or which threatens to lead to, circumvention of export subsidy commitments; nor shall non-commercial transactions be used to circumvent such commitments". Article 10.3 pursues the aim of preventing circumvention of export subsidy commitments by providing special rules on the reversal of burden of proof where a Member exports an agricultural product in quantities that exceed its reduction commitment level; in such a situation a WTO Member is treated as if it has granted WTO-inconsistent export subsidies for the excess quantities, unless the Member presents adequate evidence to "establish" the contrary.⁹¹⁵ Article 10.4 provides disciplines to prevent WTO Members from circumventing their export subsidy commitments through food aid transactions. Similarly, Article 10.2 must be interpreted in a manner that is consistent with the aim of preventing circumvention of export subsidy commitments that pervades Article 10. Otherwise, it would not have been included in that provision.

617. The United States submits that Article 10.2 contributes to the prevention of circumvention because it commits WTO Members to work toward the development of internationally agreed disciplines and to provide export credit guarantees, export credits and insurance programs only in conformity with these disciplines once an agreement has been reached.⁹¹⁶ We are not persuaded by this argument. The necessary implication of the United States' interpretation of Article 10.2 is that, until WTO Members reach an agreement on international disciplines, export credit guarantees, export credits and insurance programs are subject to no disciplines *at all*. In other words, under the United States' interpretation, WTO Members are free to "circumvent" their export subsidy commitments through the use of export credit guarantees, export credits and insurance programs until internationally agreed disciplines are developed, whenever that may be. We find it difficult to believe that the negotiators would not have been aware of and did not seek to address the potential that subsidized export credit guarantees, export credits and insurance programs could be used to

⁹¹⁴Brazil's appellee's submission, para. 951. See Appellate Body Report, *US – FSC*, para. 148 and Appellate Body Report, *Canada – Dairy (Article 21.5 – New Zealand and US II)*, para. 74.

⁹¹⁵Appellate Body Report, *Canada – Dairy (Article 21.5 – New Zealand and US)*, para. 74. Article 10.3 of the *Agreement on Agriculture* provides:

Any Member which claims that any quantity exported in excess of a reduction commitment level is not subsidized must establish that no export subsidy, whether listed in Article 9 or not, has been granted in respect of the quantity of exports in question.

⁹¹⁶United States' appellant's submission, para. 346.

circumvent a WTO Member's export subsidy reduction commitments. Indeed, such an interpretation would *undermine* the objective of preventing circumvention of export subsidy commitments, which is central to the *Agreement on Agriculture*.

618. The United States submits that, under the Panel's approach, international food aid transactions would be subject to the "full array of export subsidy disciplines" because they are not expressly excluded from Article 10.1.⁹¹⁷ According to the United States, this would adversely affect food security in the less developed world, which cannot be construed as the intent of the drafters.⁹¹⁸ Furthermore, the United States asserts, the Panel's approach would mean that international food aid transactions are subject to both the specific disciplines in Article 10.4 and those in Article 10.1 of the *Agreement on Agriculture*.⁹¹⁹

619. We are unable to subscribe to the United States' arguments because we do not see Article 10.4⁹²⁰ as excluding international food aid from the scope of Article 10.1.⁹²¹ International food aid is covered by the second clause of Article 10.1 to the extent that it is a "non-commercial transaction". Article 10.4 provides specific disciplines that may be relied on to determine whether international food aid is being "used to circumvent" a WTO Member's export subsidy commitments. There is no contradiction in the Panel's approach to Article 10.2 and its approach to Article 10.4. The measures in Article 10.2 and the transactions in Article 10.4 are both covered within the scope of Article 10.1. As Brazil submits, "Article 10.4 provides an example of specific disciplines that have been agreed upon for a particular type of measure and that complement the general export subsidy

⁹¹⁷United States' appellant's submission, para. 349.

⁹¹⁸*Ibid.*, para. 350.

⁹¹⁹*Ibid.*, para. 358.

⁹²⁰Article 10.4 of the *Agreement on Agriculture* provides:

4. Members donors of international food aid shall ensure:
- (a) that the provision of international food aid is not tied directly or indirectly to commercial exports of agricultural products to recipient countries;
 - (b) that international food aid transactions, including bilateral food aid which is monetized, shall be carried out in accordance with the FAO "Principles of Surplus Disposal and Consultative Obligations", including, where appropriate, the system of Usual Marketing Requirements (UMRs); and
 - (c) that such aid shall be provided to the extent possible in fully grant form or on terms no less concessional than those provided for in Article IV of the Food Aid Convention 1986.

A new Food Aid Convention was concluded in 1999.

⁹²¹Brazil's appellee's submission, para. 940.

rules" but, like Article 10.2, it does not "establish any exceptions for the measures that [it] covers".⁹²² WTO Members are free to grant as much food aid as they wish, provided that they do so consistently with Articles 10.1 and 10.4. Thus, Article 10.4 does not support the United States' reading of Article 10.2.

620. The United States also relies on the negotiating history of the *Agreement on Agriculture* to support its position.⁹²³ The Panel identified the drafting history in the record. It referred to paragraph 22 of the Framework Agreement on Agriculture Reform Programme (known as the "DeZeeuw Text"), circulated in July 1990, which envisaged "concurrent negotiations to govern the use of export assistance, including disciplines on export credits".⁹²⁴ There was also a "Note on Options in the Agriculture Negotiations" of June 1991, in which the Chairman of the negotiations "requested decisions by the principals on 'whether subsidized export credits and related practices ... would be subject to reduction commitments unless they meet appropriate criteria to be established in terms of the rules that would govern export competition'".⁹²⁵ An addendum circulated in August of 1991 set out an Illustrative List of Export Subsidy Practices and included, as item (i), "[s]ubsidized export credit guarantees or insurance programs".⁹²⁶ In December 1991, a "Draft Text on Agriculture" was circulated by the Chairman, Article 9.3 of which stated that "[f]or the purposes of this Article, whether export credits, export credit guarantees or insurance programmes provided by governments or their agencies constitute export subsidies shall be determined on the basis of paragraphs (j) and (k) of Annex 1 to the [SCM Agreement]."⁹²⁷ That paragraph was omitted from the "Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations"⁹²⁸, which was circulated later that month. Article 10.2 of the Draft Final Act reads as follows:

⁹²²Brazil's appellee's submission, para. 950.

⁹²³The United States refers to the negotiating history pursuant to Article 32 of the *Vienna Convention*. (United States' appellant's submission, para. 367; see also Panel Report, footnote 1112 to para. 7.933) Article 32 provides that recourse may be had to supplementary means of interpretation, including negotiating history, to determine the meaning when the interpretation according to Article 31 "leads to a result which is manifestly absurd or unreasonable".

⁹²⁴Panel Report, para. 7.934.

⁹²⁵*Ibid.*, para. 7.935.

⁹²⁶*Ibid.*, para. 7.936. Item (h) referred to "[e]xport credits provided by governments or their agencies on less than fully commercial terms."

⁹²⁷Panel Report, para. 7.937. Article 8.2 of that text listed export subsidies subject to reduction commitments "somewhat resembling the current Article 9.1 of the *Agreement on Agriculture*", while Article 9.1 was similar to the current Article 10.1. (Panel Report, para. 7.937)

⁹²⁸MTN.TNC/W/FA (20 December 1991), reproduced in Exhibit US-29.

Participants undertake not to provide export credits, export credit guarantees or insurance programs otherwise than in conformity with internationally agreed disciplines.

This language was subsequently replaced by the current text of Article 10.2.⁹²⁹

621. The Panel did not consider that this negotiating history supported the United States' position that "the drafters intended to defer the application of any and all disciplines on agricultural export credit guarantees".⁹³⁰ According to the Panel, "[t]he omission of paragraph 3 of Article 9 of the December 1991 Draft Text is consistent with a decision that the words were mere surplusage, because export credits, export credit guarantees and insurance programmes were within the disciplines on export subsidies according to the terms of the agreement captured".⁹³¹ "The omission", the Panel added, "is much less consistent with a decision to exclude such programmes from the disciplines altogether, considering the clear textual ability of the disciplines to extend to such programmes and the lack of any attention to an explicit carve-out of such programmes from the disciplines".⁹³²

622. On appeal, the United States again relies on the drafting history of the *Agreement on Agriculture*, which it considers "reflects that the Members very early specifically included export credits and export credit guarantees as a subject for negotiation and specifically elected *not* to include such practices among export subsidies in the WTO Agreements with respect to those goods within the scope of ... the *Agreement on Agriculture*".⁹³³ The United States adds that "[b]y deleting an explicit reference to export credit guarantees from the illustrative list of export subsidies in Article 9.1, Members demonstrated that they had not agreed in the case of agricultural products that export credit guarantees constitute export subsidies that should be subject to export subsidy disciplines".⁹³⁴ Finally, the United States takes issue with the Panel's explanation that draft Article 9.3 was omitted because it was mere surplusage.⁹³⁵

623. We agree with the Panel that the meaning of Article 10.2 is clear from the provision's text, in its context and in the light of the object and purpose of the *Agreement on Agriculture*, consistent with Article 31 of the *Vienna Convention*.⁹³⁶ The Panel did not think it necessary to resort to negotiating history for purposes of its interpretation of Article 10.2. Even if the negotiating history

⁹²⁹Panel Report, paras. 7.938-7.939.

⁹³⁰*Ibid.*, para. 7.939.

⁹³¹*Ibid.*, para. 7.940.

⁹³²*Ibid.*

⁹³³United States' appellant's submission, para. 377. (original emphasis)

⁹³⁴*Ibid.*, para. 378.

⁹³⁵*Ibid.*, para. 379.

were relevant for our inquiry, we do not find that it supports the United States' position. This is because it does not indicate that the negotiators did not intend to discipline export credit guarantees, export credits and insurance programs *at all*. To the contrary, it shows that negotiators were aware of the need to impose disciplines on export credit guarantees, given their potential as a mechanism for subsidization and for circumvention of the export subsidy commitments under Article 9. Although the negotiating history reveals that the negotiators struggled with this issue, it does not indicate that the disagreement among them related to whether export credit guarantees, export credits and insurance programs were to be disciplined at all. In our view, the negotiating history suggests that the disagreement between the negotiators related to which kinds of specific disciplines were to apply to such measures. The fact that negotiators felt that internationally agreed disciplines were necessary for these three measures also suggests that the disciplines that currently exist in the *Agreement on Agriculture* must apply pending new disciplines because, otherwise, it would mean that subsidized export credit guarantees, export credits, and insurance programs could currently be extended without any limit or consequence.

624. The United States contends that the Panel's interpretation leads to a result that is "manifestly absurd or unreasonable".⁹³⁷ According to the United States, it "defies logic ... to take the view of the Panel in which such practices would be treated as already disciplined export subsidies yet not permitted to be included within the applicable reduction commitments expressly contemplated by the text".⁹³⁸ The Panel's interpretation thus results in an enormous "windfall" for Brazil because the United States would have been permitted to grant export credit guarantees had such measures been listed in Article 9 of the *Agreement on Agriculture*.⁹³⁹ The United States also submits that exemption of export credit guarantees from export subsidy disciplines of the *Agreement on Agriculture* is further demonstrated by the fact that "no export credit guarantees are reported in the schedules of the United States or any other Members ... nor are they currently subject to reporting as export subsidies".⁹⁴⁰

625. We do not agree with the United States' submission in this regard. There could have been several reasons why Members chose not to include export credit guarantees, export credits and insurance programs under Article 9.1 of the *Agreement on Agriculture*. One reason, for instance, may be that they considered that their export credit guarantee, export credit or insurance programs did

not include a subsidy component, so that there was no need to subject them to export subsidy reduction commitments. There could have been other reasons. Thus, the fact that export credit guarantees, export credits and insurance programs were not included in Article 9.1 does not support the United States' interpretation of Article 10.2. We also observe that whether WTO Members with export credit guarantee programs have reported them in their export subsidy notifications is not determinative for purposes of our inquiry into the meaning of Article 10.2. In any event, the United States and Brazil disagree about whether such programs are subject to notification requirements.⁹⁴¹

626. Accordingly, we do not believe that Article 10.2 of the *Agreement on Agriculture* exempts export credit guarantees, export credits and insurance programs from the export subsidy disciplines in the *Agreement on Agriculture*. This does not mean that export credit guarantees, export credits and insurance programs will necessarily constitute export subsidies for purposes of the *Agreement on Agriculture*. Export credit guarantees are subject to the export subsidy disciplines in the *Agreement on Agriculture* only to the extent that such measures include an export subsidy component. If no such export subsidy component exists, then the export credit guarantees are not subject to the Agreement's export subsidy disciplines. Moreover, even when export credit guarantees contain an export subsidy component, such an export credit guarantee would not be inconsistent with Article 10.1 of the *Agreement on Agriculture* unless the complaining party demonstrates that it is "applied in a manner which results in, or which threatens to lead to, circumvention of export subsidy commitments". Thus, under the *Agreement on Agriculture*, the complaining party must first demonstrate that an export credit guarantee program constitutes an export subsidy. If it succeeds, it must then demonstrate that such export credit guarantees are applied in a manner that results in, or threatens to lead to, circumvention of the responding party's export subsidy commitments within the meaning of Article 10.1 of the *Agreement on Agriculture*.

627. For these reasons, we *uphold* the Panel's finding, in paragraphs 7.901, 7.911 and 7.932 of the Panel Report, that Article 10.2 of the *Agreement on Agriculture* does not exempt export credit guarantees from the export subsidy disciplines in Article 10.1.

⁹⁴⁰*Ibid.*, para. 385. (footnote omitted) The United States makes this argument within the context of its assertion that the Panel's interpretation leads to a result that is "manifestly absurd or unreasonable".

⁹⁴¹The notification requirements are set out in *Notification Requirements and Formats under the WTO Agreement on Agriculture* (PC/IPL/12, 2 December 1994), submitted by the United States to the Panel as Exhibit US-99. The United States argues that the absence of a reporting requirement for export credit guarantees provides further proof that such measures are not subject to export subsidy disciplines under the *Agreement on Agriculture*. (United States' appellant's submission, paras. 384-385) Brazil disagrees and submits that, to the extent export credit guarantees constitute export subsidies, such measures are subject to notification requirements. (Brazil's appellee's submission, para. 934)

⁹³⁶Panel Report, para. 7.933.

⁹³⁷United States' appellant's submission, para. 383.

⁹³⁸*Ibid.*, para. 384.

⁹³⁹*Ibid.*

628. Before proceeding further, we refer to the order followed by the Panel in its analysis of Brazil's claims against the United States' export credit guarantee programs. We do not find that the Panel's order of analysis was wrong or that it constituted legal error. Nor has the United States made such a claim on appeal. Nevertheless, we are struck by the fact that the Panel addressed Article 10.2 only at the end of its analysis, especially given that this provision constituted the core of the United States' defence that the disciplines of the *Agreement on Agriculture* currently do not apply to export credit guarantees at all.

5. Articles 3.1 and 3.2 of the *SCM Agreement*

629. We turn to the United States' appeal of the Panel's findings under Articles 3.1 and 3.2 of the *SCM Agreement*. According to the United States, "Article 3 of the *SCM Agreement* ... is subject in its application to Article 21.1 of the *Agreement on Agriculture*".⁹⁴² The United States then argues that, because "export credit guarantees are not subject to the disciplines of export subsidies for purposes of the *Agreement on Agriculture*, Article 21.1 of that Agreement renders Article 3.1(a) of the *SCM Agreement* inapplicable to such measures".⁹⁴³ Furthermore, the United States asserts that "the exemption from action under Article 13(c) is inapplicable, because it only is effective with respect to export subsidies disciplined under the *Agreement on Agriculture*".⁹⁴⁴

630. The United States' argument is premised on the proposition that Article 10.2 of the *Agreement on Agriculture* exempts export credit guarantees from the export subsidy disciplines in that Agreement. The Panel rejected this proposition and we have upheld the Panel's finding in this regard. Therefore, because it is premised on an incorrect interpretation of Article 10.2 of the *Agreement on Agriculture*, we reject the United States' argument. We examine the United States' appeals from other aspects of the Panel's assessment of the export credit guarantee programs under Article 3 of the *SCM Agreement* in the following section of our Report.

6. Separate Opinion

631. One Member of the Division hearing this appeal wishes to set out a brief separate opinion. At the outset, I would like to make it absolutely clear that I agree with the findings and conclusions and reasoning set out in all preceding Sections of this Report, but one, namely, Section C above, which relates to Article 10.2 of the *Agreement on Agriculture*. It is only on the interpretation of Article 10.2 that I must respectfully disagree.

⁹⁴²United States' appellant's submission, para. 393.

⁹⁴³*Ibid.*

⁹⁴⁴*Ibid.*, para. 395.

632. First I wish to point out that although Article 10.1 of the *Agreement on Agriculture* covers a range of export subsidies that do not fall within the ambit of Article 9.1 of the Agreement, Members considered that it was necessary to carve out three types of programs, namely export credit guarantees, export credits and insurance programs, and to spell out in Article 10.2 their commitments with respect to those three areas. The fact that they chose to deal with these three types of measures in Article 10.2 shows that this special treatment of the three types of measures must be given meaning and weight. Put differently, Article 10.2 is the only provision in the *Agreement on Agriculture* that speaks directly to export credit guarantees, export credits and insurance programs provided in connection with agricultural goods. I read Article 10.2 as saying that WTO Members have committed to two specific undertakings: (1) "to work toward the *development*" of international agreed disciplines and (2) to provide export credit guarantees in conformity with these disciplines "after agreement on such disciplines". (emphasis added) Thus, the text of Article 10.2 obliges Members to "work toward the *development*" of internationally agreed disciplines to regulate the provision of export credit guarantees, as well as export credits and insurance programs.

633. A specific provision that calls on Members to "work toward the development" of disciplines strongly suggests to me that disciplines do not yet exist. Certainly reference is not made in Article 10.2 to any other disciplines found in the *Agreement on Agriculture* that apply to export credit guarantees, export credits and insurance programs provided in connection with agricultural goods. Furthermore, the second part of Article 10.2 clearly limits the application of disciplines to *after* such time as the international disciplines have been agreed upon. This is a further indication that there are no current disciplines under the *Agreement on Agriculture* that apply to export credit guarantees, export credit and insurance programs.

634. I recognize that the language of this provision is not free from ambiguity. As noted by my colleagues on the Division, the drafters could have—dare I say, should have—made their intentions even more plain. If there were no Article 10.2, then I might concur with my colleagues that to the extent that an export credit guarantee provided an export subsidy then the *Agreement on Agriculture* envisions that that subsidy portion should be addressed by Article 10.1. However, Article 10.2 does exist and the meaning of the words as I read them is entirely prospective, at least with respect to the existence of applicable disciplines.

635. I do not see my reading of Article 10.2 to be inconsistent with the provision's context and with the object and purpose of the *Agreement on Agriculture*. Article 10 is entitled "Prevention of Circumvention of Export Subsidy Commitments". I see the first part of Article 10.1 as setting out a catch-all provision, designed to potentially cover an export subsidy that is used to circumvent the reduction commitments under Article 9. In contrast, as discussed above, Article 10.2 is designed to

specifically deal with export credit programs, export credits and insurance programs, and its provisions are controlling with respect to any such programs. Although it speaks to prospective development and application of agreed disciplines, Article 10.2 is also consistent with the objective of prevention of circumvention. Its placement in Article 10 suggests a recognition that export credits, export credit guarantees and insurance programs can have the potential to circumvent export subsidy commitments.⁹⁴⁵ Article 10.3 pursues the aim of preventing circumvention of export subsidy commitments by providing special rules on reversal of burden of proof when a Member's exports exceed the quantitative reduction commitments, and Article 10.4 itemizes a series of specific commitments or disciplines that apply in the area of international food aid. It is accurate, as my colleagues reason, that the language of Article 10.2 is quite different from that used in Article 10.4. While Article 10.4 establishes disciplines for food aid transactions, Article 10.2 merely foresees that disciplines will be established, in the future, for export credit guarantees, export credits and insurance programs. The fact that a single Article contains commitments with varying degrees of temporal effect and both specific and general provisions, does not support an interpretation that the general undertaking (Article 10.1) overrides the specific and prospective provision (that is, Article 10.2).

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636. I also find support for my view in the negotiating history. Of course, care must be taken in relying on negotiating history and I do not wish to imply that resort to Article 32 of the *Vienna Convention* is strictly necessary in these circumstances.⁹⁴⁶ Nevertheless, as I read it this history confirms my view that at the end of the Uruguay Round, negotiators had not agreed to subject export credit guarantees, export credits and insurance programs provided in connection with agricultural goods to the disciplines of the *Agreement on Agriculture* or to any other disciplines that existed at that time. Article 10.2, in my view, was intended to reflect this outcome. At one point in the negotiations, there was a proposal for applying to agricultural products the disciplines in the Illustrative List of Export Subsidies annexed to the *SCM Agreement*.⁹⁴⁷ This proposal was dropped in the Draft Final Act in favour of an "undertak[ing] not to provide export credits, export credit

⁹⁴⁵In this sense, I find the United States' term "deferral" to be more meaningful than "exception" in thinking about the nature of Article 10.2 in that it acknowledges that Members are already under an obligation to develop such disciplines, albeit in the future.

⁹⁴⁶I also recognize that the negotiating materials referred to by the Panel may not formally constitute *travaux préparatoires* for purposes of Article 32 of the *Vienna Convention*.

⁹⁴⁷Panel Report, para. 7.937. Specifically, in December 1991, a "Draft Text on Agriculture" was circulated by the Chairman. Article 9.3 of the draft text stated that "[f]or the purposes of this Article, whether export credits, export credit guarantees or insurance programmes provided by governments or their agencies constitute export subsidies shall be determined on the basis of paragraphs (j) and (k) of Annex 1 to the [SCM Agreement]". (*Ibid.*, para. 7.937) Later, the Draft Final Act was circulated and it omitted paragraph 3 of Article 9 that had appeared in the previous draft. (*Ibid.*, para. 7.938)

guarantees or insurance programs otherwise than in conformity with internationally agreed disciplines"⁹⁴⁸, which in turn was replaced by the current version of Article 10.2. The previous version of Article 10.2 (in the Draft Final Act) reflected an immediate undertaking "not to provide export credit guarantees, export credits or insurance programs otherwise than in conformity with internationally agreed disciplines", whatever those may have been. In contrast, no immediate commitment is evident from the current version of Article 10.2, which instead calls for continued negotiations and for WTO Members to provide export credits, export credit guarantees or insurance programs only in conformity with internationally agreed disciplines *after* agreement on such disciplines. This suggests to me that the negotiators were aware of the need to impose disciplines on export credit guarantees, given their potential as a mechanism for circumvention, but they were unable to agree upon and identify the disciplines that were to apply to such measures until disciplines were developed in the future. Thus, in my view, the negotiating history supports an interpretation that Article 10.2 was inserted to commit WTO Members to continue negotiating on the disciplines that would apply, in the future, and that no disciplines would apply to such measures until such time as disciplines were internationally agreed upon.

637. As noted by my colleagues on the Division, the United States argues that "it defies logic, as well as the obvious object and purpose of the agreement, to take the view of the Panel in which such practices would be treated as already disciplined export subsidies yet not permitted to be included within the applicable reduction commitments expressly contemplated by the text".⁹⁴⁹ Brazil argues that the United States was never willing to accept that its export credit guarantee programs constituted an export subsidy and took a calculated risk by not including them under its Article 9 reduction commitments.⁹⁵⁰

638. I agree with my colleagues on the Division that the decisions of WTO Members regarding how to schedule their export subsidy commitments have limited value for purposes of an interpretation of Article 10. However, it seems anomalous that WTO Members with export credit guarantee programs would not have sought to preserve some flexibility to provide subsidies through such programs, which flexibility would have been available to them had such programs been included under Article 9 of the *Agreement on Agriculture*. My colleagues' reading of Article 10 perceives that WTO Members intended to impose upon themselves the more onerous obligation of immediately subjecting export credit guarantees, export credits and insurance programs to the export subsidy disciplines of the *Agreement on Agriculture* rather than the less demanding obligation of working

⁹⁴⁸Panel Report, para. 7.938.

⁹⁴⁹United States' appellant's submission, para. 384.

⁹⁵⁰Brazil's response to questioning at the oral hearing.

toward the development of such disciplines. We are bound to rely upon what we have before us in the treaty provisions, and I find the same text and context leads me in the opposite direction. Namely, that the absence of reference in Article 9 to export credit guarantees, export credits and insurance programs suggests that it was believed that such measures would not be subject to any disciplines until such time as disciplines were internationally agreed upon pursuant to Article 10.2.

639. In conclusion, for these reasons and particularly my reading of the text, it is my view that, pursuant to Article 10.2, export credit guarantees, export credits and insurance programs are not currently subject to export subsidy disciplines under the *Agreement on Agriculture*, including the disciplines found in Article 10.1. In the light of Article 21.1 of the *Agreement on Agriculture* and the introductory language to Article 3.1 of the *SCM Agreement*, I am also of the view that export credit guarantees, export credits and insurance programs provided in connection with agricultural goods are not subject to the prohibition in Article 3.1(a) of the *SCM Agreement*.

640. I recognize that this interpretation of Article 10.2 perceives a significant gap in the *Agreement on Agriculture* with respect to export credit guarantees, export credits and insurance programs that apply to agricultural products. This underscores the importance of working "toward the development of international disciplines" as envisioned by Article 10.2.

641. I also recognize that this interpretation of Article 10.2 has consequential results for some of the other claims on appeal brought by both the United States and Brazil in connection with the United States' export credit guarantee programs. As to the other Sections of this Report dealing with export credit guarantees⁹⁵¹, I agree that the legal interpretation and analyses contained therein follow logically from the view of my colleagues on the Division with respect to Article 10.2, as set forth in paragraphs 605 through 630 of this Report.⁹⁵²

D. *Export Credit Guarantees – Burden of Proof*

642. The United States submits that the Panel erred in three different ways in respect of the application of the burden of proof in assessing the United States' export credit guarantee programs under item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement*. First, the United States asserts that the Panel erred by applying the special rules on the burden of proof provided

⁹⁵¹I am referring to Sections D, *Export Credit Guarantees – Burden of Proof*, E, *Export Credit Guarantees – Necessary Findings of Fact*, F, *Export Credit Guarantees – Circumvention*, G, *Export Credit Guarantees – Articles 1.1 and 3.1(a) of the SCM Agreement* of this Report.

⁹⁵²The relevant findings and conclusions for purposes of the recommendations and rulings to be adopted by the DSB in this dispute, pursuant to Article 17.14 of the DSU, are those set out in paragraph 763(e) and (f) of this Report.

in Article 10.3 of the *Agreement on Agriculture* in its examination of Brazil's claim under the *SCM Agreement*. The United States emphasizes that "the burden of proof articulated in ... Article 10.3 has no application to the *SCM Agreement*".⁹⁵³ Secondly, the United States argues that the Panel erred by applying the special rules on burden of proof in Article 10.3 of the *Agreement on Agriculture* in examining whether the United States circumvented its export subsidy commitments in respect of upland cotton and certain other *unscheduled* agricultural products.⁹⁵⁴ According to the United States, Article 10.3 does not apply at all in respect of export subsidies to an agricultural good for which the respondent has no reduction commitments.⁹⁵⁵ Finally, the United States refers to three specific instances in which the Panel allegedly applied the wrong burden of proof.⁹⁵⁶

643. Brazil responds by highlighting the Panel's finding that, whichever party bore the burden of proof, Brazil had demonstrated that the export credit guarantee programs constitute export subsidies under the terms of item (j) of the Illustrative List of Export Subsidies.⁹⁵⁷

644. Before examining the specific points raised by the United States on appeal relating to the Panel's application of the burden of proof, we recall the general rule that "the burden of proof rests upon the party, whether complaining or defending, who asserts the affirmative of a particular claim or defence".⁹⁵⁸ Article 10.3 of the *Agreement on Agriculture*, however, "provides a special rule for proof of export subsidies that applies in certain disputes under Articles 3, 8, 9 and 10 of the *Agreement on Agriculture*".⁹⁵⁹ The text of Article 10.3 reads:

Any Member which claims that any quantity exported in excess of a reduction commitment level is not subsidized must establish that no export subsidy, whether listed in Article 9 or not, has been granted in respect of the quantity of exports in question.

This provision "cleaves the complaining Member's claim" into two parts: a quantitative aspect, and an export subsidization aspect, "allocating to different parties the burden of proof with respect to the two parts".⁹⁶⁰

⁹⁵³United States' appellant's submission, para. 400. (emphasis omitted)

⁹⁵⁴*Ibid.*, para. 403.

⁹⁵⁵*Ibid.*, para. 404.

⁹⁵⁶*Ibid.*, paras. 405-408.

⁹⁵⁷Brazil's appellee's submission, paras. 95 and 1015 (referring to Panel Report, para. 7.793 and footnote 948 thereto and para. 7.867).

⁹⁵⁸Appellate Body Report, *US – Wool Shirts and Blouses*, p. 14, DSR 1997:1, 323 at 335.

⁹⁵⁹Appellate Body Report, *Canada – Dairy (Article 21.5 – New Zealand and US II)*, para. 69.

⁹⁶⁰*Ibid.*, para. 71.

645. As the Appellate Body has explained in a previous dispute, the burden of proof under Article 10.3 operates in the following manner:

... where a Member exports an agricultural product in quantities that exceed its quantity commitment level, that Member will be treated as if it has granted WTO-inconsistent export subsidies, for the excess quantities, unless the Member presents adequate evidence to "establish" the contrary. This reversal of the usual rules obliges the responding Member to bear the consequences of any doubts concerning the evidence of export subsidization.⁹⁶¹ (original emphasis)

Pursuant to Article 10.3 "the complaining Member ... is relieved of its burden, under the usual rules, to establish a *prima facie* case of export subsidization, provided that [it] has established the quantitative part of [its] claim".⁹⁶²

646. Having briefly set out the applicable rules on the burden of proof, we now turn to the specific points raised by the United States in this appeal. First, the United States alleges that the Panel erred by applying the "special rule" on the burden of proof set out in Article 10.3 of the *Agreement on Agriculture* to its examination of the export credit guarantees under the *SCM Agreement*, where such a rule "has no application at all".⁹⁶³ To support its contention that the Panel applied Article 10.3 in the context of examining Brazil's claim under the *SCM Agreement*, the United States points to the following statement by the Panel:

Moreover, recalling the burden of proof articulated in Article 10.3 of the *Agreement on Agriculture*, the United States has not established that it does not provide these export credit guarantee programmes at premium rates which are inadequate to cover the long-term operating costs and losses of the programmes.⁹⁶⁴

647. We agree with the United States that Article 10.3 of the *Agreement on Agriculture* does not apply to claims brought under the *SCM Agreement*. However, the Panel did not make the error attributed to it by the United States. The Panel made the statement relied on by the United States in the context of its assessment of the United States' export credit guarantee program under the *Agreement on Agriculture*. Although the Panel made use of the criteria set out in item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement* (providing these programs at premium rates inadequate to cover long-term operating costs and losses) it did so as contextual

⁹⁶¹Appellate Body Report, *Canada – Dairy (Article 21.5 – New Zealand and US II)*, para. 74.

⁹⁶²*Ibid.*, para. 75.

⁹⁶³United States' appellant's submission, para. 399. (emphasis added)

⁹⁶⁴Panel Report, para. 7.868.

guidance for its analysis under the *Agreement on Agriculture*, and both the United States and Brazil appear to have agreed with the appropriateness of this approach.⁹⁶⁵ Thus, the Panel's reference to Article 10.3 did not relate to its assessment of the United States' export credit guarantee programs under the *SCM Agreement*.

648. Moreover, we note that in the immediately preceding paragraph, which the United States fails to mention, the Panel stated:

We have conducted a detailed examination of the relevant evidence and argumentation submitted by the parties. On the basis of the totality of the record evidence, including approaches regularly relied upon by the United States government itself, we find that Brazil has established that the United States CCC provides the GSM 102, GSM 103 and SCGP export credit guarantee programmes "at premium rates which are inadequate to cover the long-term operating costs and losses of the programmes" within the meaning of item (j) of the Illustrative List of Export Subsidies in Annex I of the *SCM Agreement*. Our view is based on a careful consideration of the evidence, taken as a whole, and no one element, in isolation, is determinative.⁹⁶⁶ (underlining added)

It is clear from this paragraph that the Panel placed the burden of proof on Brazil and determined that Brazil met its burden of proving that the United States' export credit guarantees are provided at premium rates that are inadequate to cover long-term operating costs and losses. The Panel's statement on which the United States relies simply makes the point that the United States did not rebut the case that was made out by Brazil. The reference to Article 10.3 does not, by itself, change the fact that the Panel ultimately placed the burden of proof on Brazil.

649. After making its findings under the *Agreement on Agriculture*, the Panel examined the United States' export credit guarantees under the *SCM Agreement*. There is no reference to Article 10.3 of the *Agreement on Agriculture* in this discussion.⁹⁶⁷ We are aware that the Panel applied the "contextual" analysis" that it had conducted "under item (j) of the Illustrative List of Export Subsidies ... for the purposes of determining whether or not an export subsidy exists within the meaning of Article 10.1 of the *Agreement on Agriculture*" to its examination of "Brazil's claims under item (j)/Article 3.1(a) of the *SCM Agreement*".⁹⁶⁸ In doing so, it would have been useful for the Panel to have clarified that the special rules on the burden of proof in Article 10.3 of the *Agreement on Agriculture*, to which it had referred previously in its "contextual" analysis of item (j) under the

⁹⁶⁵Panel Report, para. 7.803.

⁹⁶⁶*Ibid.*, para. 7.867.

⁹⁶⁷See *ibid.*, paras. 7.946-7.948.

⁹⁶⁸*Ibid.*, para. 7.946 (footnote omitted)

Agreement on Agriculture, were not applicable for purposes of its analysis under the *SCM Agreement*.⁹⁶⁹ Because we have found that the Panel did not ultimately relieve Brazil of its burden of proof in determining that the United States' export credit guarantee programs constituted export subsidies under the *Agreement on Agriculture*, we do not believe that the Panel's failure to clarify that Article 10.3 of the *Agreement on Agriculture* did not apply to its examination of the same measures under the *SCM Agreement* constitutes reversible legal error.

650. Secondly, the United States submits that the Panel erred by applying the special rules on the burden of proof in Article 10.3 of the *Agreement on Agriculture* in examining whether the United States circumvented its export subsidy commitments in respect of upland cotton and certain other *unscheduled* agricultural products.⁹⁷⁰ According to the United States, Article 10.3 applies only to agricultural products for which a WTO Member has assumed export subsidy reduction commitments in its schedule, pursuant to Article 9.1 of the *Agreement on Agriculture*.⁹⁷¹

651. The Panel's view was that Article 10.3 does apply to *unscheduled* products:

With respect to upland cotton and other *unscheduled* products, the Panel considers that the United States' reduction commitment level, for the purposes of Article 10.3, is zero for each *unscheduled* product. By virtue of the second clause of Article 3.3, that is the level to which a Member must reduce any Article 9.1 export subsidies that were not in fact specifically made subject to "scheduled" reduction commitments. Accordingly, in the case of upland cotton and other *unscheduled* products the same sequence is to be followed, with Brazil as the complaining party first having to prove that United States' exports of *unscheduled* products exceed that "zero" level.⁹⁷²

652. We disagree with the Panel's view that Article 10.3 applies to *unscheduled* products. Under the Panel's approach, the only thing a complainant would have to do to meet its burden of proof when bringing a claim against an *unscheduled* product is to demonstrate that the respondent has exported that product. Once that has been established, the respondent would have to demonstrate that it has not provided an export subsidy.⁹⁷³ This seems to us an extreme result. In effect, it would mean that any

⁹⁶⁹Panel Report, paras. 7.946-7.948.

⁹⁷⁰United States' appellant's submission, para. 403 (referring to Panel Report, para. 7.875).

⁹⁷¹*Ibid.*, para. 404.

⁹⁷²Panel Report, para. 7.793. (footnote omitted)

⁹⁷³As the Appellate Body explained, when the special rule on burden of proof in Article 10.3 applies, then "the complaining party is not required to lead in the presentation of evidence to panels, and it might well succeed in its claim even if it presents no evidence—should the responding Member fail to meet its legal burden to establish that no export subsidy has been granted with respect to the excess quantity". (Appellate Body Report, *Canada – Dairy (Article 21.5 – New Zealand and the US II)*, para. 75)

export of an *unscheduled* product is *presumed* to be subsidized. In our view, the presumption of subsidization when exported quantities exceed the reduction commitments makes sense in respect of a *scheduled* product because, by including it in its schedule, a WTO Member is reserving for itself the right to apply export subsidies to that product, within the limits in its schedule. In the case of *unscheduled* products, however, such a presumption appears inappropriate. Export subsidies for both *unscheduled* agricultural products and industrial products are completely prohibited under the *Agreement on Agriculture* and under the *SCM Agreement*, respectively. The Panel's interpretation implies that the burden of proof with regard to the same issue would apply differently, however, under each Agreement: it would be on the respondent under the *Agreement on Agriculture*, while it would be on the complainant under the *SCM Agreement*.

653. Although we disagree with the Panel's interpretation of Article 10.3 of the *Agreement on Agriculture* in respect of *unscheduled* products, we do not believe that the Panel's ultimate finding is erroneous. This is because the Panel did not rely on its interpretation of Article 10.3. In a footnote to the paragraph quoted above, the Panel stated:

In any event, even if there is *no* reduction commitment level in respect of *unscheduled* products, affecting the rules of burden of proof that apply to Brazil's claims pertaining to *unscheduled* products so as to remove the burden entirely from Brazil or to place the entire burden on Brazil to prove not only that exports have been made, but even that export subsidies have been provided in respect of such exported products, this would not materially affect our analysis, as we are of the view that Brazil has discharged this burden as well, and the United States has failed to discharge its burden in this respect. (original emphasis)

Thus the Panel placed the burden on Brazil to establish that the United States provided export subsidies, through export credit guarantees, to upland cotton and other *unscheduled* products. This is confirmed in the following paragraph:

⁹⁷⁴Panel Report, footnote 948 to para. 7.793.

Recalling our discussion of the applicable burden of proof, we find that Brazil has shown that export credit guarantees – constituting export subsidies within the meaning of Article 10.1 (and therefore, necessarily, not listed in Article 9.1) – have been provided under the programmes in question during the period we have examined in respect of exports of upland cotton and certain other unscheduled agricultural products. The United States has not shown that no export subsidy has been granted in respect of such products. We therefore conclude that, in respect of upland cotton and other such *unscheduled* agricultural products on record, the United States applies export credit guarantees constituting export subsidies in a manner which results in circumvention of its export subsidy commitments inconsistently with Article 10.1 of the *Agreement on Agriculture*.⁹⁷⁵ (footnote omitted; original emphasis)

654. It is clear from the first sentence in this paragraph that the Panel imposed on Brazil the burden of demonstrating that export subsidies have been granted to upland cotton and other unscheduled agricultural products supported under the programs. The second sentence, on which the United States relies in its submission, simply indicates that the United States did not rebut the evidence and arguments put forward by Brazil; it does not indicate that the Panel erroneously placed the burden of proof on the United States.

655. Finally, the United States refers to three specific instances in which the Panel allegedly erred by improperly placing the burden of proof on the United States. The first example cited by the United States is the Panel's statement that the premiums charged by the CCC for the export credit guarantees "are not geared toward *ensuring* adequacy to cover long-term operating costs and losses for the purposes of item (j)".⁹⁷⁶ The United States assert that this is "a much higher threshold" than that provided in text of item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement*.⁹⁷⁷ Next, the United States takes issue with the Panel's statements that "[i]n terms of the structure, design, and operation of the export credit guarantee programmes [we] believe that the programmes are not designed to avoid a net cost to government"⁹⁷⁸ and that the Panel was entitled to inquire whether revenue "would be likely to cover the total of all operating costs and losses under the programme".⁹⁷⁹ According to the United States, "to 'avoid a net cost' prospectively is simply not the requirement of item (j)" and the "likelihood" standard of performance" imposed by the Panel is

⁹⁷⁵Panel Report, para. 7.875.

⁹⁷⁶United States' appellant's submission, para. 406 (referring to Panel Report, para. 7.859). (emphasis added by the United States)

⁹⁷⁷*Ibid.*, para. 406.

⁹⁷⁸*Ibid.*, para. 407 (referring to Panel Report, para. 7.857).

⁹⁷⁹*Ibid.*, para. 407 (referring to Panel Report, paras. 7.805 and 7.835).

"higher than that found in item (j)".⁹⁸⁰ The third example cited by the United States is the Panel's statement that "[w]e have not been persuaded that cohort re-estimates over time, will *necessarily* not give rise to a net cost to the United States government."⁹⁸¹ The United States contends that "[u]nder the applicable burden of proof, however, it is not for the United States to make such incontrovertible demonstrations to the Panel, and the Panel erred in requiring it".⁹⁸²

656. In our view, none of these statements demonstrates that the Panel improperly applied the rules on burden of proof. The United States is selecting statements made by the Panel within its broader analysis of how the United States' export credit guarantee programs operate, reading them in isolation, and disregarding the context in which they were made. As indicated earlier⁹⁸³, it is clear that the Panel imposed on Brazil the overall burden of proving that the premiums charged under the United States' export credit guarantee programs are inadequate to cover long-term operating costs and losses. This approach is consistent with the usual rules on the allocation of the burden of proof whereby the complaining party is responsible for proving its claim.⁹⁸⁴ As for the Panel's rejection of the United States' submissions relating to the cohort re-estimates⁹⁸⁵, we agree with Brazil that "[a]s the party asserting that the trends existed, the United States bore the burden of proving that they existed".⁹⁸⁶ Thus, the Panel cannot be said to have improperly reversed the burden of proof. Accordingly, the isolated statements referred to by the United States do not demonstrate an error by the Panel in the application of the burden of proof.

657. We, therefore, *reject* the United States' allegations that the Panel improperly applied the burden of proof in finding that the United States' export credit guarantee programs are prohibited export subsidies under Article 3.1(a) of the *SCM Agreement* and are consequently inconsistent with Article 3.2 of that Agreement.

⁹⁸⁰United States' appellant's submission, para. 407.

⁹⁸¹*Ibid.*, para. 408 (quoting Panel Report, para. 7.853). (emphasis added by the United States) The United States also mentions the following statement by the Panel: "[w]hile there may be a possibility (based on the experience of certain of other cohorts) that this figure may diminish over the lifetime of the cohort concerned, there is no assurance that this figure will *necessarily* evolve towards, and conclude as, zero or a negative figure." (Panel Report, footnote 1028 to para. 7.853) (emphasis added by the United States)

⁹⁸²United States' appellant's submission, para. 408.

⁹⁸³See *supra*, para. 648 (quoting Panel Report, para. 7.867).

⁹⁸⁴We emphasize that the United States' argument on this specific point is limited to the Panel's application of the burden of proof. The United States has not argued that the Panel incorrectly *interpreted* item (j) as requiring that export credit guarantee programs be "geared toward ensuring adequacy to cover long-term operating costs and losses" or that such programs "avoid a net cost" prospectively".

⁹⁸⁵Panel Report, para. 7.853; see *supra*, para. 655.

⁹⁸⁶Brazil's appellee's submission, para. 1027.

E. *Export Credit Guarantees – Necessary Findings of Fact*

658. We turn to the United States' claim that the Panel erred by failing to make factual findings that were allegedly necessary for the Panel's analysis of whether premiums are adequate to cover the long-term operating costs and losses of the United States' export credit guarantee programs under item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement*.

659. In the United States' view, "the absence of a specific factual finding on the basis for and monetary extent to which the United States has allegedly not covered its long-term operating costs and losses for the CCC export credit guarantee programs, compels the reversal of the Panel's finding in respect of item (j)".⁹⁸⁷ The United States explained that item (j) requires a determination whether premium rates are inadequate to cover long-term costs and losses and that this requires some determination as to what the operating costs and losses are. The United States further argued that the Panel's failure consisted in not making any determination about how to treat the rescheduled debt within operating costs and losses.⁹⁸⁸

660. Brazil responds that the United States has not made a proper claim under Article 11 of the DSU and is thus precluded from challenging the Panel's appreciation of the facts.⁹⁸⁹ In any event, Brazil submits that neither item (j), nor Articles 3.1(a) and 3.2 of the *SCM Agreement*, nor Articles 10.1 and 8 of the *Agreement on Agriculture*, required the Panel to make specific factual findings on the "monetary extent to which" premium rates are inadequate to cover the long-term operating costs and losses of the United States' export credit guarantee programs. It was sufficient for the Panel to have found that, under any and all methodologies that it reviewed and accepted, premium rates are *inadequate* to cover the long-term operating costs and losses of the export credit guarantee programs.⁹⁹⁰

661. In addition, Brazil asserts that the Panel made sufficient factual findings "on the basis for"⁹⁹¹ its conclusion that premium rates are inadequate to cover the long-term operating costs and losses of the export credit guarantee programs. Specifically, the Panel assessed the performance of the export credit guarantee programs under the elements of item (j) in various ways. In its assessment of the *past performance* of the ECG programs during the period 1992-2002, the Panel used two accounting

⁹⁸⁷United States' appellant's submission, para. 419.

⁹⁸⁸United States' response to questioning at the oral hearing.

⁹⁸⁹Brazil's appellee's submission, para. 1065.

⁹⁹⁰*Ibid.*, para. 99.

⁹⁹¹*Ibid.*, para. 100.

methodologies—*net present value accounting*, and *cash basis accounting*—to determine whether premium rates are inadequate to cover the long-term operating costs and losses of the programs.⁹⁹²

662. Before proceeding to the merits of the United States' claim, we examine first Brazil's allegation that the United States had to bring its claim, that the Panel did not make the necessary findings of fact, under Article 11 of the DSU. Article 11 of the DSU provides that a "panel should make an objective assessment of the matter before it, including an objective assessment of the facts of the case".⁹⁹³ The Appellate Body stated in *Canada – Wheat Exports and Grain Imports* that "an appellant is free to determine how to characterize its claims on appeal"⁹⁹⁴, but observed that "due process requires that the legal basis of the claim be sufficiently clear to allow the appellee to respond effectively."⁹⁹⁵

663. The United States has styled its claim as related to the interpretation and application of item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement*. According to the United States, the Panel could not have reached a legal conclusion under item (j) without having necessarily determined what were the long-term operating costs and losses of the United States' export credit guarantee programs, and more specifically, made a determination in respect of the treatment of rescheduled debt. We find no difficulty with the United States' approach. Its claim relates to the Panel's application of item (j) to the specific facts of the case. The United States is not asking us to review the Panel's factual findings, nor is it arguing that the Panel's assessment of the matter was not objective. Instead, the United States' claim relates to the application of the legal standard set out in item (j) of the Illustrative List of Export Subsidies to the specific facts of this case.⁹⁹⁶ It is an issue of legal characterization.⁹⁹⁷ Thus, we do not agree with Brazil's contention that the United States was under an obligation to bring its claim under Article 11 of the DSU. Consequently, our inquiry will be limited to the Panel's application of the law to the facts in this case.

⁹⁹²Brazil's appellee's submission, para. 101.

⁹⁹³The Appellate Body has emphasized that "a claim, by an appellant, that a panel erred under Article 11 of the DSU, and a request for a finding to this effect, must be included in the Notice of Appeal, and clearly articulated and substantiated in an appellant's submission with specific arguments". (Appellate Body Report, *US – Corrosion-Resistant Steel Sunset Review*, footnote 60 to para. 71; see also Appellate Body Report, *Japan – Apples*, para. 127; Appellate Body Report, *US – Steel Safeguards*, para. 498; and Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 177)

⁹⁹⁴Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 177.

⁹⁹⁵The Appellate Body, however, did not need to decide in that appeal whether to reject the appellant's claim on the basis that it was brought under the substantive provision at issue, rather than Article 11 of the DSU. (Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 177)

⁹⁹⁶Appellate Body Report, *Canada – Periodicals*, p. 22, DSR 1997:1, 449 at 468.

⁹⁹⁷Appellate Body Report, *EC – Hormones*, para. 132.

664. Turning to the merits of the United States' allegation, we note that item (j) of the Illustrative List of Export Subsidies, which is attached to the *SCM Agreement* as Annex I, reads:

The provision by governments (or special institutions controlled by governments) of export credit guarantee or insurance programmes, of insurance or guarantee programmes against increases in the cost of exported products or of exchange risk programmes, at premium rates which are inadequate to cover the long-term operating costs and losses of the programmes.

665. The Panel provided the following explanation of the examination that is required under item (j) of the Illustrative List of Export Subsidies:

... item (j) calls for an examination of whether the premium rates of the export credit guarantee programme at issue are inadequate to cover the long-term operating costs and losses of the programmes. Beyond that, item (j) does not set forth, or require us to use, any one particular methodological approach nor accounting philosophy in conducting our examination. Nor are we required to quantify precisely the amount by which costs and losses exceeded premiums paid.⁹⁹⁸

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We agree with the Panel's approach. The text of item (j) does not suggest that this provision requires a Panel to choose one particular basis for the calculation and then to make a precise quantification of the difference between premiums and long-term operating costs and losses on that basis. Indeed, at the oral hearing, the United States acknowledged that the text of item (j) does not, by its own terms, require precise quantification, but asserted that the Panel should have precisely quantified the long-term operating costs and losses "in this particular case".⁹⁹⁹

666. In our view, the focus of item (j) is on the inadequacy of the premiums.¹⁰⁰⁰ To us, this focus suggests that what is required is a finding on whether the premiums are insufficient and thus whether the specific export credit guarantee program at issue constitutes an export subsidy, and not a finding of the precise difference between premiums and long-term operating costs and losses.¹⁰⁰¹

⁹⁹⁸Panel Report, para. 7.804.

⁹⁹⁹United States' response to questioning at the oral hearing.

¹⁰⁰⁰The Panel observed that there was no disagreement between the parties in this case about the meaning of the term "premiums" for purposes of item (j). According to the Panel, "[u]nder the GSM 102, GSM 103 and SCGP export credit guarantee programmes, such 'premiums' are the fees paid by the applicant exporter constituting the consideration for the payment guarantee provided by the CCC". (Panel Report, paras. 7.817-7.818)

¹⁰⁰¹"Inadequate" is defined as "Not adequate; insufficient". (*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 1, p. 1338)

667. Having said this, we recognize that item (j) sets out a test that is essentially financial, as it requires a panel to look at the financial performance of an export credit guarantee program, that is, its revenues from premiums and its long-term operating costs and losses. Our review of the Panel record confirms that, in this case, the Panel conducted a financial analysis of the United States' export credit guarantee programs using three approaches. First, the Panel looked at the method used by the United States government, which "utilizes a 'net present value' approach to budget accounting for its export credit guarantee programmes".¹⁰⁰² The Panel explained that "a positive net present value means that the United States government is extending a 'subsidy' to borrowers; a negative present value means that the programme generates a 'profit' (excluding administrative costs) to the United States government".¹⁰⁰³ Having explained the method used by the United States government, the Panel then observed that:

The annual entries in the "guaranteed loan subsidy" line in the United States budget, 1992-2002 (plus 2003 and 2004 estimates) show us that, according to this formula, there has been a positive "guaranteed loan subsidy" every year. If administrative expenses are added thereto, the annual amount of cost to the United States government increases under this formula by approximately \$39 million.¹⁰⁰⁴

This shows that the Panel viewed the accounting data provided under this method used by the United States government as evidence that the premiums charged for the export credit guarantees are inadequate to cover long-term operating costs and losses.¹⁰⁰⁵

668. Next, the Panel examined data submitted by Brazil based on a constructed "cost" formula.¹⁰⁰⁶ This formula compares the revenues and costs of the export credit guarantee programs.¹⁰⁰⁷ The revenue column includes premiums collected, recovered principal and interest, and interest

¹⁰⁰²Panel Report, para. 7.842. According to the Panel, the United States government adopted the "net present value" approach starting with fiscal year 1992, pursuant to the Federal Credit Reform Act of 1990 (the "FCR Act of 1990"). A specific formula is provided under the FCR Act of 1990 for the "net present value" calculation. (*Ibid.*, footnotes 996 and 997 to para. 7.842)

¹⁰⁰³*Ibid.*, para. 7.842.

¹⁰⁰⁴*Ibid.*, para. 7.842. (footnotes omitted)

¹⁰⁰⁵The Panel recognized that the "net present value" approach relies on "initial estimates of the long-term costs to the United States government". The Panel, however, stated that these were not "random guesses" but rather were based on "[a]ctual historical experience". Furthermore, the Panel reasoned that "[t]he consistently positive numbers in the United States budget guaranteed loan subsidy line indicate to us that the United States government believes, based upon its own assessment, that it may not, even over the long term, be able to operate the export credit guarantee programmes without some net cost to government". (Panel Report, para. 7.843) (original emphasis)

¹⁰⁰⁶*Ibid.*, para. 7.844.

¹⁰⁰⁷In its appellee's submission, Brazil describes this method as following a "cash basis accounting" approach, in which the programs' receipts are netted against disbursements on a fiscal year basis. The data on receipts and disbursements "reflect actual cash flows". (Brazil's appellee's submission, para. 985)

revenue.¹⁰⁰⁸ The costs column includes administrative expenses, default claims, and interest expense.¹⁰⁰⁹ The data used in this formula are "taken from the 'prior year' column of the United States government budget".¹⁰¹⁰ The formula shows that there was a difference of a little more than US\$ 1 billion between premiums and long-term costs and losses for the period 1993-2002.¹⁰¹¹ Accordingly, the data submitted by Brazil showed that the export credit guarantee programs of the United States did not charge premiums that were adequate to cover long-term operating costs and losses.

669. After examining the data submitted by Brazil, the Panel then referred to "fiscal year/cash basis" evidence submitted by the United States. According to the United States, these data reflect "actual performance of the programmes, unlike the data in the US budget to which Brazil alludes ... which ... are based on estimates and re-estimates required under the Federal Credit Reform Act of 1990".¹⁰¹² The data submitted by the United States showed that, during the same period, total revenues exceeded total expenses by approximately US\$ 630 million.¹⁰¹³

670. The Panel proceeded to compare the two sets of data.¹⁰¹⁴ In contrasting the results under the two methods, the Panel came to the conclusion that the difference between the two was mainly due to treatment of rescheduled debt. This rescheduled debt amounted to approximately US\$ 1.6 billion.¹⁰¹⁵ The United States asserts that "the Panel did not make any determination about how to treat rescheduled debt".¹⁰¹⁶ We disagree. In fact, the Panel rejected the approach suggested by the United States for the treatment of rescheduled debt. Under the United States' approach, rescheduled debt is

not treated as an outstanding claim, but rather as a new direct loan.¹⁰¹⁷ In the Panel's view, however, this approach "understates the net cost to the United States government associated with the export credit guarantee programmes at issue".¹⁰¹⁸ Thus, contrary to the United States' submission, the Panel did make a determination in respect of the treatment of rescheduled debt.¹⁰¹⁹ Furthermore, we read this as indicating that the Panel considered that the data submitted by the United States, once rescheduled debt was properly taken into account, also showed that premiums did not offset long-term operating costs and losses.

671. The Panel went further in its analysis and considered the evidence submitted by the United States concerning re-estimates. According to the Panel, this evidence showed a subsidy of approximately US\$ 230 million, without including administrative expenses of approximately US\$ 39 million.¹⁰²⁰ The Panel was not persuaded by the United States' submission that "over time" the re-estimates would necessarily do away with the subsidy shown by the current figures.¹⁰²¹ In addition, we note that the Panel looked not only at the past financial performance of the United States' export credit guarantee programs, but also at the structure, design, and operation of the programs. The Panel concluded that the programs "are not designed to avoid a net cost to government"¹⁰²² and "the premiums are not geared toward ensuring adequacy to cover long-term operating costs and losses for the purposes of item (j)".¹⁰²³

672. In the light of the above, it is clear that the Panel undertook a sufficiently detailed examination of the financial performance of the United States' export credit guarantee programs. Its analysis showed that none of the methods proposed by the parties indicated that the premiums charged under the United States' export credit guarantee programs are adequate to cover long-term costs and

¹⁰⁰⁸Brazil states that this is a "conservative" formula that credits the programs with interest revenue, even though item (j) calls for only an assessment of revenue from premiums. (Brazil's appellee's submission, para. 985)

¹⁰⁰⁹See Table 3 in Panel Report, para. 7.845.

¹⁰¹⁰Panel Report, para. 7.846.

¹⁰¹¹*Ibid.*, paras. 7.845-7.846.

¹⁰¹²United States' response to Question 264 Posed by the Panel (Panel Report, p. I-673, para. 21). The data were presented in a spreadsheet and submitted to the Panel as Exhibit US-128. See also Panel Report, para. 7.846.

¹⁰¹³Panel Report, para. 7.846.

¹⁰¹⁴The Panel acknowledged certain limitations inherent in the comparison, including the fact that some of the data "may not directly correlate", that "United States budget data may not always reflect 'actual performance'" and the need to be especially "sensitive" to "the particular time periods covered by the data". Nevertheless, the Panel concluded that "none of these considerations undermine[s] the comparison made". (Panel Report, footnote 1006 to para. 7.846)

¹⁰¹⁵*Ibid.*, para. 7.846.

¹⁰¹⁶United States' response to questioning at the oral hearing.

¹⁰¹⁷Panel Report, para. 7.851. In its appellee's submission, Brazil states that it "accepted that repayments made pursuant to re-scheduled debt agreements should be included as receipts under the [export credit guarantee] programs ... [but] disagreed that the full amount of re-scheduled debt should be treated as received the moment the re-scheduling agreement is completed". Instead, according to Brazil, "the default claim should continue to be treated as a loss unless the United States receives payment from the debtor, and only then should be credited as a receipt in the amount actually received from the debtor". (Brazil's appellee's submission, para. 988)

¹⁰¹⁸Panel Report, para. 7.851. The Panel was struck by the fact that "no amounts have actually been determined uncollectible, written off or forgiven" after 1992. (*Ibid.*, para. 7.848)

¹⁰¹⁹We recall that the United States has not challenged the Panel's assessment of the matter, including the assessment of the facts of the case, pursuant to Article 11 of the DSU. Thus, the United States has not asked us to review the evidentiary basis on which the Panel relied to reject the treatment of rescheduled debt by the United States.

¹⁰²⁰Panel Report, para. 7.852. The Panel noted that figures submitted by Brazil showed a subsidy of US\$ 211 million, without administrative expenses.

¹⁰²¹*Ibid.*, para. 7.853.

¹⁰²²*Ibid.*, para. 7.857.

¹⁰²³*Ibid.*, para. 7.859.

losses. In these circumstances, we agree with the Panel that, in this particular case, it was not necessary to choose a particular method nor determine the precise amount by which long-term operating costs and losses exceeded premiums. Although it did not provide a final figure for the long-term operating costs and losses of the United States' export credit guarantee programs, as the United States suggests it should have, the Panel found that the various methods put forward by the parties led to the same conclusion, namely, that the premiums for the United States' export credit guarantee programs are inadequate to cover the programs' long-term operating costs and losses. The Panel's decision not to choose between methods or make a finding on the precise difference between premiums and long-term costs and losses does not, in our view, invalidate the Panel's ultimate findings under Articles 3.1(a) and 3.2 of the *SCM Agreement*.

673. For these reasons, we reject the United States' claim that the Panel failed to make the "necessary" findings of fact.

674. Consequently, we *uphold* the Panel's finding in paragraph 7.869 of the Panel Report that "the United States export credit guarantee programmes at issue – GSM 102, GSM 103 and SCGP – constitute a *per se* export subsidy within the meaning of item (j) of the Illustrative List of Export Subsidies in Annex I of the *SCM Agreement*". In addition, we *uphold* the Panel's findings, in paragraphs 7.947 and 7.948 of the Panel Report, that these export credit guarantee programs are export subsidies for purposes of Article 3.1(a) of the *SCM Agreement* and are inconsistent with Articles 3.1(a) and 3.2 of that Agreement.

F. *Export Credit Guarantees – Circumvention*

1. Introduction

675. We turn to the issues raised by Brazil in relation to the Panel's findings under Article 10.1 of the *Agreement on Agriculture*.

676. The Panel divided its analysis of Brazil's claims under Article 10.1 into different categories, distinguishing between scheduled and unscheduled products, and supported and unsupported products (and rice as a result of its finding in respect of this product). "Scheduled products" are those for which a WTO Member has assumed a commitment to limit the amount of export subsidies in terms of budgetary outlays and quantities exported pursuant to Articles 3, 8, and 9 of the *Agreement on*

Agriculture.¹⁰²⁴ The Panel used the term "supported products" to refer to products for which there was evidence in the record showing that they were not only eligible under the programs, but that export credit guarantees were in fact received in connection with exports of those products.¹⁰²⁵

677. The Panel first examined whether the United States' export credit guarantees to exports of upland cotton and other unscheduled agricultural products supported under the export credit guarantee programs are applied in a manner that "results in" circumvention for purposes of Article 10.1 of the *Agreement on Agriculture*. In other words, the Panel examined whether there is actual circumvention with respect to exports of these products. The Panel found that, "in respect of upland cotton and other such *unscheduled* agricultural products on record, the United States applies export credit guarantees constituting export subsidies in a manner which results in circumvention of its export subsidy commitments inconsistently with Article 10.1 of the *Agreement on Agriculture*".¹⁰²⁶ This finding has not been appealed.

678. The Panel next examined whether the United States' export credit guarantees to scheduled products supported under the export credit guarantee programs are applied in a manner that "results in" circumvention for purposes of Article 10.1 of the *Agreement on Agriculture*. The Panel found that "the United States has applied export credit guarantees constituting export subsidies within the meaning of Article 10.1 – and therefore, necessarily, not listed in Article 9.1 – in a manner which results in circumvention of export subsidy commitments in respect of" rice.¹⁰²⁷ In addition, the Panel found, that "[i]t has not been established, however, that such actual circumvention has resulted in respect of the twelve other United States scheduled commodities".¹⁰²⁸ Brazil appeals the latter finding by the Panel. According to Brazil, the Panel erred in finding that the United States' export credit guarantee programs are not applied in a manner that "results in" circumvention of the United States'

¹⁰²⁴The Panel noted that "[t]he United States has scheduled export subsidy reduction commitments in respect of the following thirteen commodities: wheat, coarse grains, rice, vegetable oils, butter and butter oil, skim milk powder, cheese, other milk products, bovine meat, pigmeat, poultry meat, live dairy cattle, eggs". (Panel Report, footnote 1057 to para. 7.876 (referring to Schedule XX of the United States of America, Part IV, Section II, entitled "Export Subsidies: Budgetary Outlays and Quantitative Reduction Commitments", reproduced in Exhibit BRA-83 and Exhibit US-13))

¹⁰²⁵Panel Report, para. 6.32; see also footnote 1056 to para. 7.875. At the oral hearing, the participants confirmed that this is also their understanding of what the Panel meant by the distinction that it drew between "supported" and "unsupported" products. In respect of "supported" products, the Panel stated that "[i]n the extent that it identifies products within the product coverage of the *Agreement on Agriculture* that are within our terms of reference, we consider Exhibit BRA-73 to be the relevant record evidence of such products for the purposes of this dispute". (Panel Report, footnote 1056 to para. 7.875; see also *ibid.*, footnote 1575 to para. 8.1(d)(i))

¹⁰²⁶*Ibid.*, para. 7.875.

¹⁰²⁷*Ibid.*, para. 7.881.

¹⁰²⁸*Ibid.*

export subsidy commitments with respect to pig meat and poultry meat in 2001.¹⁰²⁹ Brazil further submits that "[i]n making this finding, the Panel erred in the interpretation and application of Article 10.1 of the *Agreement on Agriculture*, and also of Article 11 of the DSU".¹⁰³⁰

679. The Panel also examined whether the United States' export credit guarantees to scheduled products other than rice and unscheduled products not supported under the United States' export credit guarantee programs are applied in a manner that "threatens to lead to" circumvention of the United States' export subsidy commitments for purposes of Article 10.1 of the *Agreement on Agriculture*. The Panel "decline[d] to find that the export credit guarantee programmes at issue are generally applied to scheduled agricultural products other than rice and other unscheduled agricultural products (not supported under the programmes) in a manner which threatens to lead to circumvention of United States' export subsidy commitments within the meaning of Article 10.1 of the *Agreement on Agriculture*".¹⁰³¹

680. Brazil makes two claims on appeal in relation to the Panel's examination of threat of circumvention. First, Brazil submits that the Panel erred in the interpretation and application of Article 10.1 in examining Brazil's claims that the United States' export credit guarantee programs "threaten[] to lead to" circumvention of the United States' export subsidy commitments.¹⁰³² If the Appellate Body were to agree with Brazil and modify the Panel's interpretation, Brazil requests that the Appellate Body complete the analysis and determine that, contrary to Article 10.1 of the *Agreement on Agriculture*, export credit guarantees have been applied in a manner that threatens to lead to circumvention of the United States' export subsidy commitments for all agricultural products eligible to receive these subsidies.¹⁰³³ Secondly, Brazil argues that the Panel erred "by confining its examination of threatened circumvention to scheduled products other than rice and unsupported unscheduled products", despite the fact that Brazil's claim "extended to all scheduled and unscheduled agricultural products eligible to receive [export credit guarantees] export subsidies".¹⁰³⁴ We examine Brazil's allegations, in turn, below.

¹⁰²⁹Brazil's other appellant's submission, para. 65. Brazil initially included vegetable oil in this claim. At the oral hearing, however, Brazil indicated that it was no longer pursuing this claim in respect of vegetable oil. See *infra*, para. 683.

¹⁰³⁰*Ibid.*, para. 76.

¹⁰³¹Panel Report, para. 7.896.

¹⁰³²Brazil's other appellant's submission, para. 63.

¹⁰³³*Ibid.*, para. 64.

¹⁰³⁴*Ibid.*, para. 75.

2. Actual Circumvention

681. We begin with Brazil's claim that the Panel erred by failing to find that the United States' export credit guarantees are applied in a manner that led to *actual* circumvention of the United States' export subsidy commitments with respect to pig meat and poultry meat in 2001.¹⁰³⁵

682. The Panel found:

We note that the United States has not specifically discharged its burden of establishing that it did not grant WTO-inconsistent export subsidies, for the excess quantities of rice exported. Therefore, we find that the United States has applied export credit guarantees constituting export subsidies within the meaning of Article 10.1 – and therefore, necessarily, not listed in Article 9.1 – in a manner which results in circumvention of export subsidy commitments in respect of this particular scheduled commodity. It has not been established, however, that such actual circumvention has resulted in respect of the twelve other United States scheduled commodities.¹⁰³⁶

683. In its appellant's submission, Brazil states that "according to uncontested evidence of record, supplied by the United States, actual circumvention also occurred for pig meat and poultry meat in 2001, and for vegetable oils in 2002".¹⁰³⁷ Brazil adds that the Panel "failed to properly apply a proper interpretation of Article 10.1 to the admitted facts".¹⁰³⁸ "By failing to do so", Brazil submits that the Panel "erred in the application of Article 10.1 to uncontested facts", and also "failed to make an objective assessment of the matter, including of admitted and uncontested facts supplied by the United States, as required by Article 11 of the DSU".¹⁰³⁹ In its statement at the oral hearing, Brazil acknowledged that data submitted by the United States indicated that the United States did not exceed its reduction commitment levels for vegetable oil in 2001-2002. We understand from Brazil's statement that it no longer wished to pursue this claim in respect of vegetable oil.

684. The United States responds that Brazil has not made a proper claim under Article 11 of the DSU. According to the United States, Brazil "is contesting findings of the Panel on matters of

¹⁰³⁵The United States has scheduled export subsidy reduction commitments for pig meat and poultry meat. Consequently, the special rule on the burden of proof established in Article 10.3 applies to any quantities exported that exceed the United States' reduction commitment levels. In respect of these quantities, the United States would be "treated as if it has granted WTO-inconsistent export subsidies ... unless the [United States] presents adequate evidence to establish the contrary". (Appellate Body Report, *Canada – Dairy (Article 21.5 – New Zealand and US II)*, para. 74. (original emphasis))

¹⁰³⁶Panel Report, para. 7.881.

¹⁰³⁷Brazil's other appellant's submission, para. 204. (footnote omitted)

¹⁰³⁸*Ibid.*, para. 210.

¹⁰³⁹*Ibid.*, para. 211. (footnote omitted)

disputed fact".¹⁰⁴⁰ Because "Brazil does *not* appeal the Panel's factual findings that the facts did not demonstrate that subsidized exports exceeded U.S. quantitative reduction commitments for poultry, pig meat, and vegetable oils", the United States submits that Brazil's appeal is improper as it does not "stand by itself" and is not "substantiated with respect to the challenged findings".¹⁰⁴¹

685. In addition, the United States points out that Brazil's allegation of actual circumvention related to the period July 2001 through June 2002.¹⁰⁴² In contrast, quantitative data on exports under the United States' export credit guarantee program are maintained on a fiscal year basis, which extends from 1 October to 30 September of the following year.¹⁰⁴³ In any event, even if this difference between periods can be overcome, the United States argues that "the actual data also support[] the Panel's finding that Brazil had not demonstrated actual circumvention for these products".¹⁰⁴⁴

686. We understand Brazil to argue that the Panel erred both in the application of Article 10.1 of the *Agreement on Agriculture* and in its assessment of the matter pursuant to Article 11 of the DSU.¹⁰⁴⁵ As we explained earlier, the application of a legal rule to the specific facts of a case is an issue of legal characterization.¹⁰⁴⁶ In this case, we understand that Brazil's claim under Article 11 of the DSU is additional to its claim of legal error in respect of Article 10.1. We thus turn first to Brazil's claim that the Panel erred in its application of Article 10.1 of the *Agreement on Agriculture* to the facts before it.

687. It will be recalled that Article 10.1 provides:

Export subsidies not listed in paragraph 1 of Article 9 shall not be applied in a manner which results in, or which threatens to lead to, circumvention of export subsidy commitments; nor shall non-commercial transactions be used to circumvent such commitments.

¹⁰⁴⁰United States' appellee's submission, para. 50 (footnote omitted)

¹⁰⁴¹*Ibid.*, para. 50 (referring to Appellate Body Report, *US – Steel Safeguards*, para. 498). (original emphasis; footnote omitted)

¹⁰⁴²*Ibid.*, para. 56 (referring to Panel Report, para. 7.878 and Brazil's first written submission to the Panel, para. 265 and Figure 18). We note that the period from July of one year to June of the next year is the period used in the United States' schedule of concessions for its quantitative export subsidy commitments. See Schedule XX of the United States submitted by Brazil to the Panel as Exhibit BRA-83.

¹⁰⁴³The fiscal year of the United States federal government is designated according to the calendar year in which it ends. Therefore, fiscal year 2001 ran from 1 October 2000 to 30 September 2001.

¹⁰⁴⁴United States' appellee's submission, para. 56.

¹⁰⁴⁵Brazil's response to questioning at the oral hearing; Brazil's other appellant's submission, para. 211.

¹⁰⁴⁶Appellate Body Report, *EC – Hormones*, para. 132.

688. Brazil asserts that "the Panel's legal analysis of the circumstances in which actual circumvention occurs for scheduled products was correct" and draws our attention to the Panel's statement that "where the United States exports an agricultural product in quantities that exceed its quantity commitment level, it will be treated for the purposes of Article 10.1 as if it has granted WTO-inconsistent export subsidies, for the excess quantities, unless it presents adequate evidence to 'establish' the contrary".¹⁰⁴⁷ Brazil adds that although the Panel correctly applied this interpretation to rice, it failed to do so in respect of pig meat and poultry meat.¹⁰⁴⁸

689. We observe that after finding that the United States had circumvented its commitments for rice, the Panel went on to reject Brazil's claim in respect of the other scheduled products supported under the programs without providing an explanation of the basis for its conclusion. Looking at the Panel's analysis, we note that, in paragraph 7.878, the Panel recognized that Brazil's claim of actual circumvention extended to thirteen agricultural products, including pig meat and poultry meat. In the next paragraph, the Panel refers to the United States' submission that it was in compliance with respect to nine of the products mentioned by Brazil", and that, in fiscal year 2002 it would also be true for poultry meat".¹⁰⁴⁹ Pig meat is not mentioned at all. As for poultry meat, the use of the conditional "would also be true" suggests some question about compliance with respect to that product as well, as the condition is not identified. Oddly, however, these issues are not taken up by the Panel, which does not examine any further whether there was actual circumvention for these products.

690. Instead, from that point on, the Panel focused exclusively on rice, in respect of which the Panel found that the United States failed to establish "that it did not grant WTO-inconsistent export subsidies, for the excess quantities of rice exported."¹⁰⁵⁰ It would appear that the Panel satisfied itself with what it considered to be an admission by the United States in respect of rice, and declined to examine further Brazil's claim in respect of the other products. In concluding, the Panel merely stated that "[i]t has not been established, however, that such actual circumvention has resulted in respect of the twelve other United States scheduled commodities".¹⁰⁵¹ There is no further explanation of the reasons leading to this conclusion.

691. The Panel may have decided to satisfy itself with the United States' admission regarding rice because it allowed it to avoid having to resolve the problem posed by the different time periods used, on the one hand, to track exports under the United States' export credit guarantee programs and, on

¹⁰⁴⁷Brazil's other appellant's submission, para. 205 (quoting Panel Report, para. 7.877).

¹⁰⁴⁸*Ibid.*, paras. 206-207.

¹⁰⁴⁹Panel Report, para. 7.879.

¹⁰⁵⁰*Ibid.*, para. 7.881.

¹⁰⁵¹*Ibid.*

the other, to determine the export subsidy reduction commitments under the United States' schedule. Exports under the United States' export credit guarantee programs are tracked on a fiscal year basis, extending from 1 October to 30 September of the following year. Meanwhile, the United States' export reduction commitments are based on a year that extends from 1 July to 30 June of the following year. These periods overlap, albeit only in part.

692. We find nothing wrong in the Panel having relied on an admission by the United States relating to rice to conclude that the United States had failed to rebut Brazil's initial allegation of circumvention.¹⁰⁵² This did not excuse the Panel, however, from specifically analyzing Brazil's claim in respect of the other products. Consequently, we find no basis to support the Panel's finding that "[i]t has not been established, however, that such actual circumvention has resulted in respect of the twelve other United States scheduled commodities".¹⁰⁵³

693. We must determine next whether there are sufficient uncontested facts in the record to permit us to complete the analysis with respect to the other commodities.¹⁰⁵⁴ In our view, there are not. First, the parties disagree about the time period covered by Brazil's claim. The United States asserts that Brazil's claim was limited to the period July 2001 to June 2002, while Brazil contends that its claim was not limited to that period.¹⁰⁵⁵ Second, as we noted previously¹⁰⁵⁶, different time periods are used for the sets of data that have to be compared. The data regarding United States exports under the export credit guarantee programs are maintained on a fiscal year basis, which extends from 1 October to 30 September of the following year.¹⁰⁵⁷ The United States' export subsidy commitments are registered based on a year that extends from 1 July to 30 June of the following year. Both Brazil and the United States have sought to reconcile the data.¹⁰⁵⁸ In each case, Brazil and the United States assert that the data support their position. Given the differences between the participants in respect of the data that we would have to examine to determine whether the United States applied export credit guarantees in a manner that results in circumvention of its export subsidy commitments for pig meat

and poultry meat, we do not believe there are sufficient undisputed facts in the record to enable us to complete the analysis.

694. We recall that Brazil's claim on appeal is limited to the Panel's findings relating to pig meat and poultry meat. For the reasons mentioned above, we *reverse* the Panel's finding, in paragraph 7.881 of the Panel Report, that Brazil did not establish actual circumvention in respect of poultry meat and pig meat. Nevertheless, because there are insufficient uncontested facts in the record to enable us to do so, we do not complete the legal analysis to determine whether the United States' export credit guarantees to poultry meat and pig meat have been applied in a manner that "results in" circumvention of the United States' export subsidy commitments.

695. Brazil has made an additional claim that the Panel failed to make an objective assessment of the matter, as required by Article 11 of the DSU. Having reversed the Panel's ultimate finding, we find that it is not necessary for us to rule on Brazil's additional claim under Article 11 of the DSU. This is because, even if we were to agree with Brazil, it would lead to the same result that we have reached after examining the Panel's application of Article 10.1 of the *Agreement on Agriculture* to the facts before it.

3. Threat of Circumvention

(a) Scheduled Products Other than Rice and Unscheduled Products not Supported under the Export Credit Guarantee Programs

696. We move next to Brazil's two claims on appeal relating to the Panel's examination of *threat* of circumvention. We recall that the Panel examined whether the United States' export credit guarantees are applied in a manner that "threatens to lead to" circumvention of the United States' export subsidy commitments in respect of *scheduled products other than rice* and *unscheduled products not supported* under the export credit programs.

697. For ease of reference, we note again the text of Article 10.1, which reads:

Export subsidies not listed in paragraph 1 of Article 9 shall not be applied in a manner which results in, or which threatens to lead to, circumvention of export subsidy commitments; nor shall non-commercial transactions be used to circumvent such commitments.

¹⁰⁵²Panel Report, footnote 1060 to para. 7.880.

¹⁰⁵³*Ibid.*, para. 7.881.

¹⁰⁵⁴Appellate Body Report, *US – Section 211 Appropriations Act*, para. 343.

¹⁰⁵⁵Brazil's and the United States' responses to questioning at the oral hearing.

¹⁰⁵⁶*Supra*, para. 691.

¹⁰⁵⁷The fiscal year of the United States federal government is designated according to the calendar year in which it ends. Therefore, fiscal year 2001 ran from 1 October 2000 to 30 September 2001.

¹⁰⁵⁸United States' appellee's submission, paras. 58-60; Brazil's statement at the oral hearing.

698. The Panel explained that its conclusion on whether the United States' export credit guarantees are applied in a manner that threatens to lead to circumvention would depend on whether the Panel considered that:

... the United States export credit guarantee programmes require the provision of an 'unlimited amount' of subsidies, so that scheduled commodities other than rice and unscheduled agricultural products not supported under the programmes, therefore, benefit from those subsidies when the reduction commitment levels specified in the United States' Schedule for those agricultural products have been reached.¹⁰⁵⁹

The Panel cautioned, however, that even if it made an affirmative finding, "if these programmes are not such as to necessarily create an *unconditional legal entitlement* to receive them, then there would not necessarily be such a threat".¹⁰⁶⁰ The Panel therefore proceeded to "examine whether an unconditional statutory legal entitlement to an export credit guarantee exists in respect of such products".¹⁰⁶¹

699. In its examination, the Panel noted that "United States export credit guarantee programmes are classified as 'mandatory' under the United States Budget Enforcement Act of 1990."¹⁰⁶² It went on to explain, however, that it did "not believe that the 'mandatory/discretionary' distinction is the sole legally determinative one for [its] examination of whether or not 'threat' of circumvention of export subsidy commitments within the meaning of Article 10.1 of the *Agreement on Agriculture* has been proven to the required standard".¹⁰⁶³ The Panel, moreover, stated that, "[i]n order to pose a 'threat' within the meaning of Article 10.1 of the *Agreement on Agriculture*, [it did] not believe that it is sufficient that an export credit guarantee programme might possibly, or theoretically, be used in a manner which threatens to lead to circumvention of export subsidy commitments".¹⁰⁶⁴

700. After examining the statutory and regulatory framework of the United States' programs under which the export credit guarantees are issued, the Panel concluded that this statutory and regulatory framework "is such that the CCC would not necessarily be required to issue guarantees in respect of any other unscheduled agricultural product (not supported under the programmes), or in respect of

scheduled agricultural products other than rice, in a manner which 'threatens to lead to' circumvention of export subsidy commitments".¹⁰⁶⁵ The Panel, therefore, found:

Keeping the applicable burden of proof in mind, we therefore decline to find that the export credit guarantee programmes at issue are generally applied to scheduled agricultural products other than rice and other unscheduled agricultural products (not supported under the programmes) in a manner which threatens to lead to circumvention of United States export subsidy commitments within the meaning of Article 10.1 of the *Agreement on Agriculture*.¹⁰⁶⁶

701. Brazil asserts that the Panel erred in interpreting and applying Article 10.1 of the *Agreement on Agriculture*. According to Brazil, "[b]y] declaring that a 'possibility' of circumvention was not sufficient for a 'threat' finding under Article 10.1, the Panel mischaracterized the threat obligation, reducing it to situations of near certainty".¹⁰⁶⁷ Brazil explains that the ordinary meaning of the term "threat" can "encompass events that are a possibility or that appear likely; the word can also include events whose occurrence is indicated or portended by circumstances".¹⁰⁶⁸ Furthermore, Brazil asserts, that the meaning of the term "threatens" is clarified by its immediate context, particularly by the use of the word "prevent" in the title of Article 10.¹⁰⁶⁹ Brazil explains that "[f]o give proper meaning to the aim of 'prevention,' the threat obligation should, therefore, be read in a way that it thwarts, forestalls, or stops circumvention from occurring by requiring a Member to take appropriate precautionary action".¹⁰⁷⁰ If, on the contrary, "the degree of likelihood necessary to trigger the threat obligation were set too high, the threat obligation would fail to 'prevent' circumvention, contrary to the express aim of the provision".¹⁰⁷¹

¹⁰⁶⁵Panel Report, para. 7.895.

¹⁰⁶⁶*Ibid.*, para. 7.896.

¹⁰⁶⁷Brazil's other appellant's submission, para. 95. Brazil is referring to the Panel's statement that "[i]n order to pose a 'threat' within the meaning of Article 10.1 of the *Agreement on Agriculture*, we do not believe that it is sufficient that an export credit guarantee programme might possibly, or theoretically, be used in a manner which threatens to lead to circumvention of export subsidy commitments". (Panel Report, para. 7.893)

¹⁰⁶⁸Brazil's other appellant's submission, para. 97.

¹⁰⁶⁹*Ibid.*, paras. 98-99. The title of Article 10 is "Prevention of Circumvention of Export Subsidy Commitments".

¹⁰⁷⁰*Ibid.*, para. 100. According to Brazil, "[i]his reading of Article 10.1 of the *Agreement on Agriculture* is consistent with the Appellate Body's observation, in *US – FSC*, that the FSC measure did not provide a mechanism for "stemming or otherwise controlling" the "flow" of export subsidies. (Appellate Body Report, *US – FSC*, para. 149)

¹⁰⁷¹Brazil's other appellant's submission, para. 101.

702. Having set out its views on the meaning of the term "threatens" as used in Article 10.1 of the *Agreement on Agriculture*, Brazil then distinguishes it from the connotation that the same term is given in other covered agreements. Brazil submits that the *Agreement on Safeguards* and the *Anti-Dumping Agreement* require a higher degree of likelihood because, under both Agreements, the demonstration of "threat" triggers the right of a WTO Member to apply trade remedy measures involving suspension or modification of WTO commitments.¹⁰⁷² In contrast, "Article 10.1 of the *Agreement on Agriculture* aims at the effective *enforcement* of a Member's export subsidy obligations".¹⁰⁷³ Finally, Brazil submits that the assessment of whether a threat exists under Article 10.1 must be done on a case-by-case basis and suggests a list of factors that could be considered as part of the assessment.¹⁰⁷⁴

703. The United States responds by asserting that Brazil mischaracterizes the Panel's findings. Contrary to Brazil's argument, the Panel's finding that the export credit guarantee programs do not threaten circumvention of export subsidy commitments is not an articulation of a broad standard that circumvention of export subsidy commitments would only be "threatened" if beneficiaries had an "absolute" or "unconditional statutory legal entitlement" to receive the subsidies such that the United States would "necessarily" be required to grant subsidies after the commitment level had been reached.¹⁰⁷⁵ Rather, in concluding that the programs did not pose a threat of circumvention, the United States argues, the Panel simply was responding to and declining to adopt Brazil's erroneous factual and legal characterizations of the program.¹⁰⁷⁶ The United States submits, furthermore, that the Panel rightly distinguished these programs from the mandatory subsidies at issue in *US – FSC*, and the Panel's decision presents no conflict with that Appellate Body Report.¹⁰⁷⁷ According to the United States, Brazil effectively argued that a mere possibility of issuance of export credit guarantees presented a threat of circumvention, and the Panel simply did not adopt this theory in the context of the export credit guarantee programs.¹⁰⁷⁸

¹⁰⁷²Brazil's other appellant's submission, para. 103.

¹⁰⁷³*Ibid.*, para. 104. (original emphasis)

¹⁰⁷⁴*Ibid.*, para. 105.

¹⁰⁷⁵United States' appellee's submission, paras. 6 and 27 (referring to Brazil's other appellant's submission, para. 89).

¹⁰⁷⁶*Ibid.*, paras. 6 and 30.

¹⁰⁷⁷*Ibid.*, para. 32.

¹⁰⁷⁸*Ibid.*, paras. 6 and 35.

704. The Appellate Body has explained that "under Article 10.1, it is not necessary to demonstrate actual 'circumvention' of 'export subsidy commitments'".¹⁰⁷⁹ It suffices that "export subsidies" are "applied in a manner which ... threatens to lead to circumvention of export subsidy commitments".¹⁰⁸⁰ We note that the ordinary meaning of the term "threaten" includes "[c]onstitute a threat to", "be likely to injure" or "be a source of harm or danger".¹⁰⁸¹ Article 10.1 is concerned not with injury, but rather with "circumvention". Accordingly, based on its ordinary meaning, the phrase "threaten[]" to lead to ... circumvention" would imply that the export subsidies are applied in a manner that is "likely to" lead to circumvention of a WTO Member's export subsidy commitments. Furthermore, we observe that the ordinary meaning of the term "threaten" refers to a *likelihood* of something happening; the ordinary meaning of "threaten" does not connote a sense of certainty.¹⁰⁸²

705. The concept of "threat" has been discussed by the Appellate Body within the context of the *Agreement on Safeguards* and the *Anti-Dumping Agreement*. It has explained that "threat" refers to something that "has *not* yet occurred, but remains a future event whose actual materialization cannot, in fact, be assured with certainty".¹⁰⁸³ In *US – Line Pipe*, the Appellate Body stated that there is a continuum that ascends from a "threat of serious injury" up to the "serious injury" itself.¹⁰⁸⁴ We emphasize that the Appellate Body's discussion of the concept of "threat" in previous appeals related to the interpretation of other covered agreements that contain obligations relating to injury that differ from those relating to circumvention of export subsidy reduction commitments contained in Article 10.1 of the *Agreement on Agriculture*. Our interpretation of "threat" in Article 10.1 of the *Agreement on Agriculture* is consistent with the Appellate Body's interpretation of the term "threat" in these other contexts.

¹⁰⁷⁹Appellate Body Report, *US – FSC*, para. 148. (original emphasis)

¹⁰⁸⁰*Ibid.*, para. 148.

¹⁰⁸¹*Shorter Oxford English Dictionary*, 5th ed., W.R. Trumble, A. Stevenson (eds.) (Oxford University Press, 2002), Vol. 2, p. 3251.

¹⁰⁸²Both participants agree that the determination of threat of circumvention has to be done on a case-by-case basis. (Brazil's and the United States' responses to questioning at the oral hearing.)

¹⁰⁸³Appellate Body Report, *US – Lamb*, para. 125. (original emphasis) The Appellate Body was interpreting the phrase "threat of serious injury" within the context of Article 4.1(b) of the *Agreement on Safeguards*. Article 4.1(b) defines "threat of serious injury" as "serious injury that is clearly imminent, in accordance with the provisions of paragraph 2. A determination of the existence of a threat of serious injury shall be based on facts and not merely on allegation, conjecture or remote possibility".

¹⁰⁸⁴The Appellate Body explained that "[i]n terms of the rising continuum of an injurious condition of a domestic industry that ascends from a 'threat of serious injury' up to 'serious injury', we see 'serious injury'—because it is something *beyond* a 'threat'—as necessarily *including* the concept of a 'threat' and *exceeding* the presence of a 'threat'". (Appellate Body Report, *US – Line Pipe*, para. 170) (original emphasis)

706. The Panel explained that, in its view, "threat" of circumvention under Article 10.1 requires that there be a "an unconditional legal entitlement".¹⁰⁸⁵ We see no basis for this requirement in Article 10.1. The Panel also stated that "[i]n order to pose a 'threat' within the meaning of Article 10.1 of the *Agreement on Agriculture*, [it did] not believe that it is sufficient that an export credit guarantee programme might possibly, or theoretically, be used in a manner which threatens to lead to circumvention of export subsidy commitments".¹⁰⁸⁶ In both of these statements, the Panel seems to conflate the phrase "threaten to lead to circumvention" with certainty that the circumvention will happen. We find it difficult, moreover, to reconcile the Panel's interpretation with the ordinary meaning of the term "threaten", which, as we indicated earlier, connotes that something is "likely" to happen.¹⁰⁸⁷ We also find it difficult to reconcile these statements of the Panel with its own view that it did "not believe that the 'mandatory/discretionary' distinction is the sole legally determinative one for our examination of whether or not 'threat' of circumvention of export subsidy commitments within the meaning of Article 10.1 of the *Agreement on Agriculture* has been proven to the required standard".¹⁰⁸⁸

707. Nor are we prepared to accept Brazil's suggestion that the concept of "threat" in Article 10.1 should be read in a manner that requires WTO Members to take "anticipatory or precautionary action".¹⁰⁸⁹ The obligation not to apply export subsidies in a manner that "threatens to lead to" circumvention of their export subsidy commitments does not extend that far. There is no basis in Article 10.1 for requiring WTO Members to take affirmative, precautionary steps to ensure that circumvention of their export subsidy reduction commitments does not occur.¹⁰⁹⁰

708. In concluding as it did, the Panel appears to have relied on the Appellate Body Report in *US – FSC* for guidance.¹⁰⁹¹ In our view, however, the Panel misapplies that analysis. We recall that, in *US – FSC*, the Appellate Body underscored the importance of considering "the structure and other characteristics of [the] measure" when examining whether the specific measure at issue is "applied in

¹⁰⁸⁵Panel Report, para. 7.883.

¹⁰⁸⁶*Ibid.*, para. 7.893.

¹⁰⁸⁷Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 85.

¹⁰⁸⁸Panel Report, para. 7.886.

¹⁰⁸⁹Brazil's other appellant's submission, para. 100.

¹⁰⁹⁰We note in this respect that Article 10 is titled "Prevention of Circumvention of Export Subsidy Commitments". Brazil's assertion that Article 10.1 requires WTO Members to take precautionary action would imply that the aim of the provision would also include the prevention of *threat* of circumvention.

¹⁰⁹¹In a footnote, the Panel states that the United States' export credit guarantee programs that it was "examining are of a fundamentally different nature than the mandatory and essentially unlimited subsidy (in the form of revenue forgone that is otherwise due) examined in *US – FSC*". (Panel Report, footnote 1082 to para. 7.894)

a manner which ... threatens to lead to circumvention of export subsidy commitments".¹⁰⁹² The Appellate Body then went on to note that the specific measure at issue in that dispute created "a *legal entitlement* for recipients to receive export subsidies, not listed in Article 9.1, with respect to agricultural products, both scheduled and unscheduled".¹⁰⁹³ This meant that there was "no discretionary element in the provision by the government of the FSC export subsidies".¹⁰⁹⁴ Furthermore, the Appellate Body noted that the "legal entitlement that the FSC measure establishes is unqualified as to the *amount* of export subsidies that may be claimed".¹⁰⁹⁵ This meant that the measure was "unlimited" because there was "no mechanism in the measure for stemming, or otherwise controlling the flow of ... subsidies that may be claimed with respect to any agricultural products".¹⁰⁹⁶

709. A proper reading of the Appellate Body's statement in *US – FSC*, however, reveals that it did not intend to provide an exhaustive interpretation of threat of circumvention under Article 10.1 of the *Agreement on Agriculture*. In noting that the measure at issue in that dispute created a "legal entitlement" and had no "discretionary element", the Appellate Body was merely describing characteristics of the measure at issue in that case that it found relevant for its analysis of "threat". In other words, the Appellate Body did not foreclose, in *US – FSC*, the possibility that a measure that does not create a "legal entitlement" or that has a "discretionary element" could be found to "threaten[]" to lead to circumvention" under Article 10.1 of the *Agreement on Agriculture*.

710. We therefore modify the Panel's interpretation, in paragraphs 7.882-7.883 and 7.896 of the Panel Report, of the phrase "threatens to lead to circumvention" in Article 10.1 of the *Agreement on Agriculture* to the extent that the Panel's interpretation requires "an unconditional legal entitlement" to receive the relevant export subsidies as a condition for a finding of threat of circumvention.

711. Having interpreted the phrase "threatens to lead to ... circumvention", we turn to Brazil's request that we complete the legal analysis and find that, contrary to Article 10.1 of the *Agreement on Agriculture*, the United States' export credit guarantee programs have been applied in a manner that threatens to lead to circumvention of the United States' export subsidy reduction commitments for all

¹⁰⁹²Appellate Body Report, *US – FSC*, para. 149.

¹⁰⁹³*Ibid.* (original emphasis)

¹⁰⁹⁴*Ibid.*, para. 149.

¹⁰⁹⁵*Ibid.* (original emphasis)

¹⁰⁹⁶*Ibid.*, para. 149.

agricultural products eligible to receive these subsidies.¹⁰⁹⁷ According to Brazil, the alleged discretion retained by the CCC, as found by the Panel, does not operate in a manner that "mitigates the threat of circumvention".¹⁰⁹⁸ Brazil submits that the initial allocations by country of funds available for export credit guarantees "are repeatedly increased during the year".¹⁰⁹⁹ "The same is also true", Brazil asserts, "of product allocations, although the CCC makes relatively limited use of these".¹¹⁰⁰ In addition, Brazil points out that "the record does not contain one single example of a situation where the CCC was unable to provide [export credit guarantees] because a country or product allocation had been exhausted ... [I]nstead, the record discloses that country and product allocations are repeatedly increased, by significant amounts, during the fiscal year as demand for [export credit guarantees] exhausts existing allocations".¹¹⁰¹

712. Brazil also questions the significance attributed by the Panel to the fact that, under United States law, export credit guarantees may not be provided in relation to exports to a country that the Secretary of Agriculture determines "cannot adequately service the debt associated with such sale".¹¹⁰² According to Brazil, this statutory provision does not constrain the overall amount of export credit guarantees because "the possible exclusion of a country does not prevent the CCC from using all the [export credit guarantees] that would have gone to that country to support exports to other, eligible countries".¹¹⁰³ Moreover, Brazil submits that the record shows that the Secretary of Agriculture has used this authority "other than sparingly" and that the current list of countries that are eligible under the United States' export credit guarantee programs include "the very large majority of the world's highly indebted poor countries".¹¹⁰⁴

713. We are not persuaded that the arguments put forward by Brazil establish that the United States' export credit guarantee programs are applied in a manner that threatens to lead to circumvention of the United States' export subsidy commitments in respect of scheduled products other than rice and unscheduled products not supported under the programs. In our view, the fact

¹⁰⁹⁷Brazil's other appellant's submission, paras. 63-64 and 140.

¹⁰⁹⁸*Ibid.*, para. 187.

¹⁰⁹⁹*Ibid.*, para. 188.

¹¹⁰⁰*Ibid.*, para. 189. According to Brazil, less than eight percent of allocations were product-specific in 2003.

¹¹⁰¹Brazil's other appellant's submission, para. 191. (footnote omitted)

¹¹⁰²Panel Report, para. 7.888 (quoting 7 USC 5622(f)(1)). The Panel stated that "[w]hile this does not curtail the amount of guarantees that may ultimately be made available, it does indicate to us that there exists a discretion (on the part of the Secretary [of Agriculture]) to determine situations in which guarantees cannot be made available". (*Ibid.*, para. 7.888)

¹¹⁰³Brazil's other appellant's submission, para. 195.

¹¹⁰⁴*Ibid.*, para. 196.

alone that exports of certain products are eligible for export credit guarantees is not sufficient to establish a threat of circumvention. This is particularly the case where there is no evidence in the record that exports of such products have been "supported" by export credit guarantees in the past.¹¹⁰⁵ As we stated earlier, Article 10.1 of the *Agreement on Agriculture* does not require WTO Members to take affirmative, precautionary steps to ensure that circumvention of their export subsidy reduction commitments never happens. Nor is it sufficient for Brazil to have alleged that the United States has provided export credit guarantees to exports of *other* unscheduled products or to exports of scheduled products in excess of its export subsidy reduction commitments. Therefore, we agree with the Panel that Brazil has not established that the United States applies its export credit guarantee programs to scheduled agricultural products other than rice and other unscheduled agricultural products (not "supported" under the programs) "in a manner ... which threatens to lead to ... circumvention" of the United States' export subsidy commitments.

714. We thus *uphold*, albeit for different reasons, the Panel's finding, in paragraph 7.896, that Brazil has not established that "the export credit guarantee programmes at issue are generally applied to scheduled agricultural products other than rice and other unscheduled agricultural products (not supported under the programmes) in a manner which threatens to lead to circumvention of United States export subsidy commitments within the meaning of Article 10.1 of the *Agreement on Agriculture*".

(b) Rice and Unscheduled Products Supported by the Export Credit Guarantee Programs

715. We turn to Brazil's claim that the Panel improperly confined its examination of Brazil's threat claim to scheduled products other than rice and unscheduled products not supported under the programs. Put another way, Brazil submits that the Panel's analysis of "threat" of circumvention should have also included rice (a scheduled product) and unscheduled products supported by the programs (including upland cotton).¹¹⁰⁶

716. As Brazil acknowledges, the products that the Panel allegedly excluded from its "threat" analysis had been the subject of the Panel's analysis of "actual" circumvention.¹¹⁰⁷ In fact, for these products, the Panel had *already* found that the United States' export credit guarantees are applied in a manner that "results in" circumvention. That is, the Panel found *actual* circumvention.¹¹⁰⁸ The

¹¹⁰⁵"Supported" products are described, *supra*, para. 676.

¹¹⁰⁶Brazil's other appellant's submission, para. 75.

¹¹⁰⁷*Ibid.*, para. 135 (referring to Panel Report, paras. 7.875 and 7.881).

¹¹⁰⁸Panel Report, para. 7.875.

Panel, however, explained that it was unnecessary for it to examine whether export credit guarantees for the same products were also applied in a manner that "threatens to lead to" circumvention:

Article 10.1 of the *Agreement on Agriculture* provides that export subsidies not listed in Article 9.1 "shall not be applied in a manner which results in, or which threatens to lead to, circumvention of export subsidy commitments ..." (emphasis added). With respect to rice and to unscheduled agricultural products supported under programmes, we have found, in paragraphs 7.875 and 7.881, that the United States applies export credit guarantee programmes constituting export subsidies in a manner which results in circumvention of its export subsidy commitments inconsistently with Article 10.1. We consider that the "or" in Article 10.1 indicates that either one (resulting in circumvention) or the other (threatening to lead to circumvention) or both in combination would be adequate to trigger the remedies associated with this provision. We also see "resulting in circumvention" as including and exceeding the concept of "threatening to lead to circumvention". ... We therefore do not believe that it is necessary to conduct any additional examination here.¹¹⁰⁹ (original emphasis)

717. We believe the Panel was within its discretion in declining to examine whether scheduled products other than rice and unscheduled products supported by the programs are applied in a manner that "threatens to lead to" circumvention. The Panel had already found that the United States acted inconsistently with Article 10.1 of the *Agreement on Agriculture* because it applied its export credit guarantee program in a manner that "results in" (actual) circumvention of its export subsidy commitments for these products. We do not see why the Panel had to examine also whether the United States acted inconsistently with the *same* provision in respect of the *same* products, but on the basis of there being a *threat* of circumvention, rather than *actual* circumvention.

718. The Appellate Body has stated that panels may exercise judicial economy and refrain from addressing claims beyond those necessary to resolve the dispute.¹¹¹⁰ In this case, the Panel did not expressly state it was exercising judicial economy.¹¹¹¹ We agree with the United States, however, that the Panel's approach can be properly characterized as an exercise of judicial economy.¹¹¹² Moreover, we believe that the Panel was within its discretion in refraining from making additional findings and it

¹¹⁰⁹Panel Report, footnote 1061 to para. 7.882.

¹¹¹⁰Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 133.

¹¹¹¹The Panel stated that it did not believe it "necessary to conduct any additional examination". (Panel Report, footnote 1061 to para. 7.882)

¹¹¹²The United States asserts that "the Panel properly exercised judicial economy in not examining threat of circumvention for agricultural products with respect to which it found actual circumvention". (United States' appellee's submission, para. 42)

was not improper for the Panel to have exercised judicial economy given that its finding of *actual* circumvention resolved the matter.¹¹¹³

719. Therefore, we reject Brazil's appeal that the Panel erred in confining its examination of Brazil's threat of circumvention claim to scheduled products other than rice and unscheduled products not supported under the United States' export credit guarantee programs.

G. *Export Credit Guarantees – Articles 1.1 and 3.1(a) of the SCM Agreement*

720. We turn now to Brazil's allegation that the Panel erred by exercising judicial economy in respect of Brazil's claim that the United States' export credit guarantees are export subsidies within the meaning of Articles 1.1 and 3.1(a) of the *SCM Agreement*.

721. The Panel first examined the United States' export credit guarantees under the *Agreement on Agriculture* using the benchmark provided in item (j) of the Illustrative List of Export Subsidies attached to the *SCM Agreement* as Annex I, albeit as context.¹¹¹⁴ The Panel found:

On the basis of the totality of the record evidence, including approaches regularly relied upon by the United States government itself, we find that Brazil has established that the United States CCC provides the GSM 102, GSM 103 and SCGP export credit guarantee programmes "at premium rates which are inadequate to cover the long-term operating costs and losses of the programmes" within the meaning of item (j) of the Illustrative List of Export Subsidies in Annex I of the *SCM Agreement*.

...

We therefore find that the United States export credit guarantee programmes at issue – GSM 102, GSM 103 and SCGP – constitute a *per se* export subsidy within the meaning of item (j) of the Illustrative List of Export Subsidies in Annex I of the *SCM Agreement*.¹¹¹⁵

722. After completing its examination under the *Agreement on Agriculture*, the Panel moved to Brazil's claims under the *SCM Agreement*. The Panel noted that it had "conducted a 'contextual' analysis under item (j) ... for the purposes of determining whether or not an export subsidy exists within the meaning of Article 10.1 of the *Agreement on Agriculture*" and, therefore, saw "no reason ... why this analysis may not also be applied directly in an examination of the merits of Brazil's claims

¹¹¹³Appellate Body Report, *Australia – Salmon*, para. 223. See also Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 133.

¹¹¹⁴Panel Report, para. 7.803.

¹¹¹⁵*Ibid.*, paras. 7.867 and 7.869.

under item (j)/Article 3.1(a) of the *SCM Agreement* in respect of the export credit guarantee programmes in this factual situation".¹¹¹⁶ The Panel found:

To the extent that the United States export credit guarantee programmes at issue – GSM 102, GSM 103 and SCGP – do not conform fully to these provisions in Part V of the *Agreement on Agriculture* and do not benefit from the exemption from actions provided by Article 13(c)(ii) of the *Agreement on Agriculture*, they are also export subsidies prohibited by Article 3.1(a) for the reasons we have already given.¹¹²⁵

Article 3.2 of the *SCM Agreement* provides: "A Member shall neither grant nor maintain subsidies referred to in paragraph 1" of Article 3. To the extent that the three United States export credit guarantee programmes at issue are inconsistent with Article 3.1(a), they are, consequently, also inconsistent with Article 3.2 of the *SCM Agreement*.¹¹¹⁷

¹¹²⁵ We recall that Article 3.1(a) of the *SCM Agreement* sets out a prohibition on subsidies contingent upon export performance, "including those illustrated in Annex I". Annex I - the Illustrative List of Export Subsidies - contains item (j). We have found that the challenged United States export credit guarantee programmes meet the definitional elements of a *per se* export subsidy in item (j). As they are among those "illustrated in Annex I" for the purposes of Article 3.1(a), they are included in the subsidies contingent upon export performance prohibited by Article 3.1(a) of the *SCM Agreement*.

723. During the interim review, Brazil requested the Panel "to make certain additional 'factual' findings regarding the parties' evidence and argumentation relating to Brazil's allegation that the CCC export credit guarantee programmes at issue constitute prohibited export subsidies under the elements of Articles 1 and 3.1(a) of the *SCM Agreement*".¹¹¹⁸ Brazil asserted that "in the event one of the parties appeals and the Appellate Body reverses the Panel's conclusion on item (j), it might not have the necessary facts at its disposal to 'complete the analysis' with respect to Brazil's claims under Articles 1 and 3.1(a) of the *SCM Agreement*".¹¹¹⁹

724. The United States asked the Panel to reject Brazil's request, asserting that "the Panel ha[d] already made findings on the claims cited by Brazil" and, therefore, Brazil was improperly requesting

¹¹¹⁶Panel Report, para. 7.946. (footnote omitted)

¹¹¹⁷*Ibid.*, paras. 7.947-7.948. (footnote 11.24 omitted)

¹¹¹⁸*Ibid.*, para. 6.31.

¹¹¹⁹*Ibid.*

the Panel "to make unnecessary and unsupported additional factual findings with respect to its *SCM Agreement* claims, and to reverse the applicable burden of proof".¹¹²⁰

725. The Panel declined Brazil's request because, in its view:

Brazil's allegation invoking the elements of Articles 1 and 3.1(a) of the *SCM Agreement* is not a separate claim, but merely another argument, on a different factual basis, as to how the United States export credit guarantee programmes would meet the definition of an export subsidy in Article 3.1(a) of the *SCM Agreement*. Given our finding in paragraphs 7.946-7.948, we do not believe that it is necessary to address Brazil's additional arguments about how the Article 3.1(a) definitional elements would be fulfilled on another factual basis in order to resolve this dispute. For greater clarity, we have inserted footnote 1125.¹¹²¹

726. On appeal, Brazil asserts that the Panel's rejection of Brazil's request constitutes a false exercise of judicial economy. According to Brazil, "[i]n concluding that Brazil's allegations under item (j) and under Articles 1.1 and 3.1(a) of the *SCM Agreement* constitute alternative arguments, on a different factual basis, the Panel failed to recognize the distinct obligations that flow from Article 3.1(a), and the potentially distinct course of implementation triggered by a Member's maintenance of export subsidies within the meaning of Articles 1.1 and 3.1(a)".¹¹²² Brazil explains that "because of the different benchmarks that apply under item (j), on the one hand, and Articles 1.1 and 3.1(a), on the other, a measure that no longer constitutes an export subsidy under item (j) may still constitute an export subsidy under Articles 1.1 and 3.1(a)".¹¹²³

727. Brazil asserts that a "panel is obligated to address all claims on which a finding is necessary to enable the Dispute Settlement Body to make sufficiently precise recommendations and rulings to allow for prompt settlement" of the dispute, and for prompt compliance by a Member with those recommendations and rulings "in order to ensure effective resolution of disputes to the benefit of all Members."¹¹²⁴ It then adds that "[b]ecause a measure that no longer constitutes an export subsidy under item (j) may still constitute an export subsidy under Articles 1.1 and 3.1(a), the Panel's exercise of judicial economy in this case was in error".¹¹²⁵ Brazil further explains that the United States "could comply with its obligations under item (j) but still fail to comply with its obligations under

¹¹²⁰Panel Report, para. 6.31.

¹¹²¹*Ibid.* See *supra*, para. 722.

¹¹²²Brazil's other appellant's submission, para. 22 (quoting Panel Report, para. 6.31).

¹¹²³*Ibid.*, para. 22.

¹¹²⁴*Ibid.*, para. 23 (quoting Articles 3.2 and 21.1 of the DSU). (footnotes omitted)

¹¹²⁵*Ibid.*, para. 23.

Articles 1.1 and 3.1(a)".¹¹²⁶ Therefore, in Brazil's view, the Panel's failure "to examine Brazil's claim ... leaves open a dispute and creates uncertainty concerning the scope of the United States' obligations, and the consistency of its existing measures with those obligations".¹¹²⁷ If the Appellate Body were to agree with Brazil's assertion that the Panel's exercise of judicial economy was improper, then Brazil requests that the Appellate Body complete the analysis, and find that the United States' export credit guarantee programs constitute export subsidies under Articles 1.1 and 3.1(a) of the *SCM Agreement*.¹¹²⁸

728. The United States requests us to reject Brazil's claim. According to the United States, any further findings by the Panel would have been redundant as the Panel had already determined that the export credit guarantees "constitute *per se* export subsidies prohibited by Articles 3.1(a) and 3.2 of the *SCM Agreement*."¹¹²⁹ The United States explains that "[n]either item (j) nor the Illustrative List imposes obligations *per se*".¹¹³⁰ Rather, the obligations regarding export subsidies are found in Articles 3.1(a) and 3.2.¹¹³¹ The United States asserts, furthermore, that an additional finding by the Panel on the issue of whether the export credit guarantees programs confer a "benefit" would not change the United States' compliance obligations.¹¹³²

426 729. In addition, the United States submits that Brazil mischaracterizes what the Panel did as a failure to address a claim by Brazil when, in fact, Brazil's request at the interim review stage was for the Panel to make additional factual findings.¹¹³³ Even if Brazil had made a separate claim before the Panel under Articles 1.1 and 3.1 of the *SCM Agreement*, the United States submits that the Panel could have properly exercised judicial economy, as the Appellate Body recognized, in *US – Wool Shirts and Blouses*, that panels "need only address those *claims* which must be addressed to resolve the matter in issue in the dispute".¹¹³⁴ Finally, the United States rejects the contention that Brazil has demonstrated that the United States' export credit guarantees confer a "benefit".¹¹³⁵

¹¹²⁶Brazil's other appellant's submission, para. 23.

¹¹²⁷*Ibid.*

¹¹²⁸*Ibid.*, para. 42.

¹¹²⁹United States' appellee's submission, para. 62 (referring to Panel Report, para. 8.1(d)(i)).

¹¹³⁰*Ibid.*, para. 66.

¹¹³¹*Ibid.*, para. 66. The United States submits that, under Brazil's reading, the Illustrative List would be deprived of meaning. (*Ibid.*, para. 67)

¹¹³²*Ibid.*, para. 80.

¹¹³³*Ibid.*, paras. 81–82 (referring to Panel Report, para. 6.31).

¹¹³⁴*Ibid.*, para. 85 (referring to Appellate Body Report, *US – Wool Shirts and Blouses*, p. 19, DSR 1997:1, 323 at 339), (emphasis added)

¹¹³⁵*Ibid.*, paras. 92–99.

730. We observe that Brazil premises its claim on appeal on its submission that item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement* is a distinct obligation from that contained in Article 3.1(a), read together with Article 1.1.¹¹³⁶ In other words, Brazil submits that the requirement in item (j) for an export credit guarantee program to charge premiums that are adequate to cover long-term operating costs and losses is distinct from the requirement, under Articles 1.1 and 3.1(a), not to confer a "benefit". The United States rejects the premise of Brazil's argument, asserting instead that the Illustrative List of Export Subsidies, and more specifically item (j), do not establish a separate obligation from that in Article 3.1(a).¹¹³⁷ Rather, the Illustrative List provides examples (hence "illustrative") of the types of measures that constitute "export subsidies" within the meaning of Article 3.1(a) and "to the extent that it does address a practice this constitutes the standard to determine whether a particular practice constitutes a prohibited export subsidy".¹¹³⁸

731. We need not decide, in this case, whether an export credit guarantee program that meets the standard of item (j) of the Illustrative List of Export Subsidies—because the premiums charged are adequate to cover long-term operating costs and losses—may nevertheless be challenged as a prohibited export subsidy under Article 3.1(a) on the basis that it confers a benefit. This is because, even if we were to assume that such a claim were possible, we would conclude that the Panel was within its discretion in exercising judicial economy in respect of Brazil's claim.¹¹³⁹

732. As we explained earlier, panels may refrain from ruling on every claim as long as it does not lead to a "partial resolution of the matter".¹¹⁴⁰ The Panel found that the United States' export credit guarantee programs constitute a prohibited export subsidy under Article 3.1(a) because they do not meet the criteria in item (j) of the Illustrative List of Export Subsidies. This finding, in our view, is sufficient to resolve the matter. Therefore, we are not persuaded that the Panel's exercise of judicial

¹¹³⁶Brazil's other appellant's submission, para. 22.

¹¹³⁷United States' appellee's submission, para. 66.

¹¹³⁸*Ibid.*, para. 70.

¹¹³⁹The Panel did not expressly state that it was exercising judicial economy. Instead, the Panel stated that it did not believe that it was "necessary to address Brazil's additional *arguments*". (Panel Report, para. 6.31) (emphasis added) Brazil initially describes the Panel's failure as an error by the Panel in the "interpretation and application of Article 3.1(a) of the *SCM Agreement*, as well as of Article 3.7 of the DSU". (Brazil's other appellant's submission, para. 22) Later in its submission, however, Brazil describes the Panel's error as a "misapplication of the principle of judicial economy". (*Ibid.*, para. 23; see also *ibid.*, paras. 33 and 39–41)

¹¹⁴⁰Appellate Body Report, *Australia – Salmon*, para. 223.

economy was improper, as Brazil has not demonstrated that it has led to "a partial resolution of the matter".¹¹⁴¹

733. For these reasons, we reject Brazil's claim that the Panel erred by exercising judicial economy in respect of Brazil's allegation that the United States' export credit guarantees are prohibited export subsidies, under Article 3.1(a) of the *SCM Agreement*, because they confer a "benefit" within the meaning of Article 1.1.

H. *ETI Act of 2000*

734. We turn to Brazil's claim that the Panel erred in the "interpretation and application of the burden of proof"¹¹⁴², in connection with its finding that Brazil did not establish a *prima facie* case that the ETI Act of 2000¹¹⁴³ and the subsidies granted thereunder are inconsistent with Articles 8 and 10.1 of the *Agreement on Agriculture* and Articles 3.1 and 3.2 of the *SCM Agreement*, in respect of upland cotton.

735. Before the Panel, Brazil argued that the ETI Act of 2000 provides an export subsidy to upland cotton, within the meaning of Article 10.1 of the *Agreement on Agriculture*, because it eliminates tax liabilities for exporters who sell upland cotton in foreign markets. According to Brazil, the ETI Act of 2000 threatens to circumvent the United States' export subsidy commitments by providing an export subsidy to upland cotton, despite the fact that the United States has not scheduled any export subsidy reduction commitments for that commodity, thereby violating Articles 8 and 10.1 of the *Agreement on Agriculture*. In addition, Brazil asserted that the ETI Act of 2000 provides prohibited export

¹¹⁴¹Appellate Body Report, *Australia – Salmon*, para. 223. As the United States argues, the circumstances of this case are different from those in *Australia – Salmon*. In that case, the panel limited its findings for other Canadian salmon to Article 5.1 of the *SPS Agreement* and "gave no convincing reason why it examined Article 5.5 and 5.6 for only one category of the products in dispute, i.e., ocean-caught Pacific salmon, and did not undertake the same analysis for other categories, i.e., other Canadian salmon". (Appellate Body Report, *Australia – Salmon*, para. 225) The present case does not involve a panel incorrectly limiting its findings under other provisions to certain products. Instead, Brazil is questioning the Panel's refusal to make an additional finding of inconsistency with the same provision for the same products.

¹¹⁴²Brazil's other appellant's submission, para. 7.

¹¹⁴³Public Law 106-519. The ETI Act of 2000 is a measure that was taken by the United States to comply with the recommendations and rulings of the DSB after the original FSC measure was found to be WTO-inconsistent in *US – FSC*. (Appellate Body Report, *US – FSC*, para. 178) It is the same measure that the European Communities challenged in *US – FSC (Article 21.5 – EC)*, part of which the panel and Appellate Body found, in that dispute, to be inconsistent with the United States' WTO obligations. (Appellate Body Report, *US – FSC (Article 21.5 – EC)*, paras. 1 and 256(d)) Brazil acknowledges that, after the Panel Report was circulated, the "United States enacted legislation ... that seems to repeal most of the illegal aspects of the ETI Act of 2000". (Brazil's other appellant's submission, para. 214) Brazil is referring to the American Jobs Creation Act of 2004, enacted as Public Law 108-357.

subsidies to upland cotton within the meaning of Articles 3.1(a) and 3.2 of the *SCM Agreement*.¹¹⁴⁴ Brazil pointed out that, in *US – FSC (Article 21.5 – EC)*, both the panel and Appellate Body found that the ETI Act of 2000 violates Articles 8 and 10.1 of the *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement*. Brazil requested the Panel to apply the reasoning developed by that panel, as modified by the Appellate Body, *mutatis mutandis*, to this dispute.¹¹⁴⁵

736. The United States responded that the Panel should reject Brazil's claim because Brazil failed to make a *prima facie* case.¹¹⁴⁶ According to the United States, "[a]s a result of Brazil's *mutatis mutandis*' approach, the Panel [was] in no position to exercise its judgment to follow, or decline to follow, prior dispute settlement findings concerning the ETI Act of 2000, nor even in a position to make factual findings concerning the Act".¹¹⁴⁷

737. The Panel began its analysis by noting that, apart from referring the Panel to the European Communities' claims and arguments in *US – FSC (Article 21.5 – EC)*, Brazil had submitted no direct evidence reflecting the nature, function or WTO-inconsistency of the ETI Act of 2000.¹¹⁴⁸ It then observed that Brazil appeared to:

... seek a Panel process whereby we would simply apply the reasoning, and findings and conclusions of the panel, as modified by the Appellate Body, in the *US – FSC (Article 21.5 – EC)* dispute, without going through the ordinary procedural steps constituting panel proceedings set out in the *DSU*, including the examination of the legal claims against the measures constituting the matter before this Panel on the basis of direct evidence and argumentation submitted by the complaining and defending parties in this dispute. While Brazil has supplemented the evidence and argumentation that dispute, it has not purported directly to establish the elements comprising the basis of the findings and conclusions in that dispute.¹¹⁴⁹

¹¹⁴⁴Panel Report, para. 7.950. (footnote omitted) Brazil explained that the subsidies granted to upland cotton under the ETI Act of 2000 do not fully conform to Part V of the *Agreement on Agriculture* and, therefore, are not exempt from action under the *SCM Agreement* pursuant to Article 13(c) of the *Agreement on Agriculture*.

¹¹⁴⁵Panel Report, para. 7.949. (footnote omitted) Brazil incorporated by reference into its submissions (i) the Panel Report in *US – FSC (Article 21.5 – EC)*, (ii) the Appellate Body Report in *US – FSC (Article 21.5 – EC)*, and (iii) all submissions of the European Communities in that case. Brazil contends that an approach whereby the complaining Member incorporates by reference the reasoning of another panel, as modified by the Appellate Body, is consistent with the Appellate Body's reasoning in *Mexico – Corn Syrup (Article 21.5 – US)*. (Brazil's other appellant's submission, para. 224 (referring to Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 109))

¹¹⁴⁶Panel Report, para. 7.951.

¹¹⁴⁷*Ibid.*

¹¹⁴⁸*Ibid.*, para. 7.959.

¹¹⁴⁹Panel Report, para. 7.961. (footnote omitted)

The Panel saw "no basis in the text of the DSU ... for such incorporation by reference of claims and arguments made in a previous dispute nor for a quasi-automatic application of findings, recommendations and rulings from a previous dispute".¹¹⁵⁰ In addition, the Panel rejected Brazil's reliance on Article 17.14 of the DSU¹¹⁵¹ to support its claim, reasoning that, because Brazil was not a party in *US – FSC (Article 21.5 – EC)*, the panel and Appellate Body reports in that case "cannot be taken as a providing a final resolution to the part of the matter before [it] concerning the ETI Act of 2000".¹¹⁵²

738. The Panel then identified other differences between the present dispute and *US – FSC (Article 21.5 – EC)*.¹¹⁵³ These differences meant, according to the Panel, that the evidence and argumentation relating to the present dispute are distinct from those in *US – FSC (Article 21.5 – EC)*.¹¹⁵⁴ The differences in the evidence and argumentation, in turn, led the Panel to decide that "no direct transposition or incorporation of the panel and Appellate Body findings and conclusions would, in any event, be appropriate on the basis of the evidence and argumentation submitted in this dispute".¹¹⁵⁵ Moreover, the Panel observed that, in a written communication to the parties after the first meeting, it had "put Brazil on notice that the evidence and arguments submitted up to that point in the Panel proceedings did not provide sufficient basis for [the Panel] to make a finding".¹¹⁵⁶

¹¹⁵⁰*Ibid.*, para. 7.962.

¹¹⁵¹Article 17.14 of the DSU provides:

An Appellate Body report shall be adopted by the DSB and unconditionally accepted by the parties to the dispute unless the DSB decides by consensus not to adopt the Appellate Body report within 30 days following its circulation to the Members. (footnote omitted)

¹¹⁵²Panel Report, para. 7.967. (footnote omitted)

¹¹⁵³The Panel explained that, in *US – FSC (Article 21.5 – EC)*, the claims under the *SCM Agreement* were examined before those under the *Agreement on Agriculture*, an order contrary to that adopted by the Panel in this case. (Panel Report, para. 7.971) Also, the Panel pointed out that, in *US – FSC (Article 21.5 – EC)*, there was no discussion relating to issues under Article 13 of the *Agreement on Agriculture*. (Panel Report, para. 7.972) Finally, the Panel observed that the findings in *US – FSC (Article 21.5 – EC)* were not specific to upland cotton. (Panel Report, para. 7.973)

¹¹⁵⁴*Ibid.*, para. 7.975.

¹¹⁵⁵*Ibid.*

¹¹⁵⁶Panel Report, para. 7.980. The written communication is dated 5 September 2003 and in it the Panel "indicated to the parties that, 'on the basis of the evidence and arguments presented to date, it is unable to form any view on whether the ETI Act of 2000 satisfies the relevant provisions of the *Agreement on Agriculture*'".

The Panel also referred to "its discretionary authority to put questions to the parties to clarify the factual and legal aspects of the matter". (*Ibid.*, para. 7.983) In this respect, the Panel explained that its authority to ask questions or seek information is not conditional on a party having established a *prima facie* case. Nevertheless, the Panel observed that it was "not permitted to make Brazil's case for Brazil". (*Ibid.*, para. 7.985)

739. For these reasons, the Panel concluded:

[O]n the basis of the evidence and arguments submitted, we are not in a position to conclude that Brazil has established a *prima facie* case that the ETI Act of 2000 and subsidies granted thereunder are inconsistent with Articles 8 and 10.1 of the *Agreement on Agriculture* in respect of upland cotton.¹¹⁵⁷

740. On appeal, Brazil asserts that the Panel erred in the "interpretation and application of the burden of proof under Articles 8 and 10.1 of the *Agreement on Agriculture*, and Articles 3.1(a) and 3.2 of the *SCM Agreement*, in light of the goal of the WTO dispute settlement system, under Article 3.3 of the DSU, to provide for the 'prompt settlement' of disputes".¹¹⁵⁸ Brazil submits that it challenged before the Panel exactly the same measure that the panel and the Appellate Body in *US – FSC (Article 21.5 – EC)* held violated the *Agreement on Agriculture* and the *SCM Agreement*. This measure had not changed since it was enacted in 2000¹¹⁵⁹ and thus the legislation that forms the basis for the United States measure that is subject to Brazil's claims is identical to the legislation at issue in *US – FSC (Article 21.5 – EC)*.¹¹⁶⁰ According to Brazil, the United States did not dispute the identity between the measures.¹¹⁶¹

741. In addition, Brazil asserts that the United States never rebutted Brazil's arguments, or the supporting documents that Brazil referenced, that demonstrate the inconsistency of the ETI Act of 2000 with Articles 8 and 10.1 of the *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement*.¹¹⁶² Brazil refers to *Mexico – Corn Syrup (Article 21.5 – US)*, where the Appellate Body held that a panel may incorporate the reasoning of another panel by reference and still meet the requirement in Article 12.7 of the DSU to set out the "basic rationale" for its findings and conclusions.¹¹⁶³ Brazil sees no reason why this reasoning should not also apply to submissions by a

¹¹⁵⁷*Ibid.*, para. 7.986. The Panel also concluded that:

... in accordance with Article 13(c)(ii) of the *Agreement on Agriculture*, to the extent that Brazil has not demonstrated that the United States ETI Act of 2000 is not in conformity with the United States export subsidy commitments under Part V of the *Agreement on Agriculture* in respect of upland cotton, the United States is "exempt from actions based on" Articles 3.1(a) and 3.2 of the *SCM Agreement*. We therefore decline to examine Brazil's claims based on those provisions.

(*Ibid.*, para. 7.987) (footnote omitted)

¹¹⁵⁸Brazil's other appellant's submission, para. 7.

¹¹⁵⁹Brazil notes that legislation "that seems to repeal most of the illegal aspects of the ETI Act of 2000" was enacted in 2004. (Brazil's other appellant's submission, para. 214) See *supra*, footnote 1143.

¹¹⁶⁰Brazil's other appellant's submission, para. 221.

¹¹⁶¹*Ibid.*

¹¹⁶²Brazil's other appellant's submission, para. 222.

¹¹⁶³Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 109.

complaining Member that incorporate by reference the reasoning of another panel, as modified by the Appellate Body, addressing the exact same measure.¹¹⁶⁴

742. Brazil acknowledges that the "United States enacted legislation ... that seems to repeal most of the illegal aspects of the ETI Act of 2000".¹¹⁶⁵ Consequently, Brazil expressly states that, were we to modify the Panels' "interpretation and application of the burden of proof"¹¹⁶⁶, it is not requesting us to complete the legal analysis and find that the export subsidies to upland cotton, provided under the ETI Act of 2000, are inconsistent with Articles 8 and 10.1 of *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement*.¹¹⁶⁷

743. The United States responds that we should not decide Brazil's appeal because Brazil acknowledges that the appeal is not necessary to resolve the dispute between the parties. Brazil explicitly does not ask the Appellate Body to complete the analysis with respect to its claims. The United States argues that the Appellate Body should abstain from deciding this issue because Brazil is not asking "the Appellate Body to make findings that would result in DSB rulings and recommendations with respect to the ETI Act".¹¹⁶⁸ For that reason alone, the Appellate Body should decline to decide Brazil's appeal.¹¹⁶⁹

744. In any event, the United States submits that the Panel correctly concluded that Brazil did not make a *prima facie* case with respect to the ETI Act of 2000. Brazil simply did not present any evidence at all regarding the ETI Act of 2000 itself. According to the United States, the Panel acted properly under the text of the DSU, including Article 11, by declining to find that the "short shrift" that Brazil gave to the ETI Act of 2000 satisfied Brazil's burden to make its *prima facie* case concerning that Act.¹¹⁷⁰

745. At the outset, we observe that Article 17.6 of the DSU provides that appeals "shall be limited to issues of law covered in the panel report and legal interpretations developed by the panel". Furthermore, Article 17.12 of the DSU states that "[t]he Appellate Body shall address each of the

¹¹⁶⁴In addition, Brazil states that it submitted to the Panel arguments and evidence that addressed the specific nature of its claims, in particular with respect to Article 13(c)(ii) of the *Agreement on Agriculture* (Brazil's other appellant's submission, para. 225)

¹¹⁶⁵*Ibid.*, para. 214.

¹¹⁶⁶*Ibid.*, para. 7.

¹¹⁶⁷*Ibid.*, para. 214.

¹¹⁶⁸United States' appellee's submission, para. 100. The United States relies for support on the Appellate Body Reports in *US – Steel Safeguards* and *US – Wool Shirts and Blouses*.

¹¹⁶⁹United States' appellee's submission, para. 100.

¹¹⁷⁰United States' appellee's submission, para. 112.

issues raised in accordance with paragraph 6 during the appellate proceeding". The United States does not argue that Brazil has failed to appeal an issue of law or a legal interpretation. Thus, the United States is not asserting that Brazil could not have brought this claim on appeal or that we are legally precluded from addressing it. The United States' assertion is that it is not *necessary* for us to resolve Brazil's claim because Brazil is not requesting us to make findings that would result in DSB rulings and recommendations.

746. We agree. Article 3.3 of the DSU explains that the aim of the WTO's dispute settlement system is the "prompt settlement of situations in which a Member considers that any benefits accruing to it directly or indirectly under the covered agreements are being impaired by measures taken by another Member". For its part, Article 3.4 of the DSU provides that "[r]ecommendations or rulings made by the DSB shall be aimed at achieving a satisfactory settlement of the matter". Similarly, Article 3.7 states that "[t]he aim of the dispute settlement mechanism is to secure a positive solution to a dispute". The Appellate Body, moreover, has cautioned that "[g]iven the explicit aim of dispute settlement that permeates the DSU, ... Article 3.2 of the DSU is [not] meant to encourage either panels or the Appellate Body to 'make law' by clarifying existing provisions of the *WTO Agreement* outside the context of resolving a particular dispute".¹¹⁷¹

747. In this case, Brazil's claim on appeal is limited to the Panel's application of the burden of proof. Brazil has expressly stated that it is not requesting us to complete the analysis. In view of Brazil's request, our ruling would not result in recommendations or rulings by the DSB in respect of the ETI Act of 2000. In these circumstances, we fail to see how our examination of Brazil's claim would contribute to the "prompt" or "satisfactory settlement" of this matter or would contribute to "secure a positive solution" to this dispute.¹¹⁷² Even if we were to disagree with the manner in which the Panel applied the burden of proof, we would not make any findings in respect of the WTO-consistency of the ETI Act of 2000. We recognize that there may be cases in which it would be useful for us to make a finding on an issue, despite the fact that our decision would not result in rulings and recommendations by the DSB. In this case, however, we find no compelling reason for doing so on this particular issue.

¹¹⁷¹Appellate Body Report, *US – Wool Shirts and Blouses*, p. 19, DSR 1997:1, 323 at 340.

748. For these reasons, we decline Brazil's request that we reverse the Panel's conclusion that Brazil did not make a *prima facie* case that the ETI Act of 2000 is inconsistent with the United States' WTO obligations. In declining to rule on Brazil's request, we neither endorse nor reject the manner in which the Panel applied the burden of proof in the context of examining Brazil's claim against the ETI Act of 2000.

I. *Interpretation of Article XVI:3 of the GATT 1994*

1. Introduction

749. Before the Panel, Brazil claimed that the United States applied its domestic and export subsidies to upland cotton during the 1999-2002 marketing years in a manner that resulted in the United States having more than an equitable share of world export trade within the meaning of Article XVI:3 of the GATT 1994, and thereby caused serious prejudice within the meaning of Article XVI:1 of the GATT 1994.¹¹⁷³

750. In addressing this claim, the Panel considered whether paragraphs 1 and 3 of Article XVI could be considered together, to address both the domestic support and export subsidy measures at issue. The Panel said that "we do not believe that these provisions are susceptible to such joint application", on the grounds that "each provision – Article XVI:1 and Article XVI:3 – requires application in accordance with its own terms in respect of measures that fall within its respective scope of application".¹¹⁷⁴

751. The Panel dealt with Brazil's allegation that the subsidies at issue resulted in the United States enjoying "more than an equitable share of world export trade" under Article XVI:3 of the GATT 1994

¹¹⁷²Our approach is consistent with the approach of the Appellate Body in *US – Steel Safeguards*, where it did not find it necessary to examine the Panel's findings on the causation analysis because it had "already found that the measures before [it] are inconsistent with Article XIX:1(a) of the GATT 1994 and with Articles 2.1, 3.1 and 4.2 of the *Agreement on Safeguards*". (Appellate Body Report, *US – Steel Safeguards*, para. 483)

The Appellate Body noted, in that appeal, that "several participants expressed an interest in having [it] rule on causation as it would provide guidance to Member on applying safeguard measures in the future consistently with their WTO obligations". (Appellate Body Report, *US – Steel Safeguards*, para. 484) Despite this request for guidance, the Appellate Body declined to make a ruling on this specific aspect of the case. (Appellate Body Report, *US – Steel Safeguards*, paras. 485-491)

¹¹⁷³Brazil's further submission to the Panel, para. 277.

¹¹⁷⁴Panel Report, para. 7.992. The Panel thus addressed elements of Brazil's claim in different parts of its Report. The Panel's response to Brazil's allegation of "serious prejudice" under Article XVI:1 of the GATT 1994 is dealt with in the section of the Panel Report addressing "Actionable Subsidies: Claims of 'Present' Serious Prejudice", (*Ibid.*, Section VII:G) In the light of its findings of present serious prejudice under Articles 5(c) and 6.3(c) of the *SCM Agreement*, the Panel exercised judicial economy with respect to Brazil's claim of serious prejudice under Article XVI:1 of the GATT 1994. (*Ibid.*, para. 7.1476)

in the section of the Panel Report dealing with "Export Subsidies".¹¹⁷⁵ The Panel examined whether Article XVI:3 applies only to export subsidies, or whether it also applied to all of the types of subsidies covered by Article XVI:1 as well. The Panel found that:

Article XVI:3 applies only to export subsidies as that term is now defined in the *Agreement on Agriculture* and the *SCM Agreement*.¹¹⁷⁶

752. Because the Panel had concluded that Step 2 payments to exporters and export credit guarantees under the GSM 102, GSM 103 and SCGP programs constituted export subsidies prohibited by the relevant provisions of the *Agreement on Agriculture* and the *SCM Agreement*, the Panel—as it had done in respect of Brazil's claims under Article XVI:1 of the GATT 1994—exercised judicial economy with respect to Brazil's claim under Article XVI:3 of the GATT 1994.¹¹⁷⁷

753. Brazil's appeal regarding the Panel's findings with respect to the application of Article XVI:3 of the GATT 1994 has two elements. First, Brazil appeals the Panel's finding that Article XVI:3 applies only to export subsidies as that term is now defined in the *Agreement on Agriculture* and the *SCM Agreement*. Brazil stresses that its appeal in this regard, that is, the Panel's legal interpretation of the second sentence of Article XVI:3 of the GATT 1994, is *not conditional*.¹¹⁷⁸ Brazil argues that, in reaching the view that Article XVI:3 applies only to export subsidies, as currently defined in the *SCM Agreement* and the *Agreement on Agriculture*, the Panel misinterpreted the second sentence of Article XVI:3, which establishes disciplines upon "any form of subsidy which operates to increase the export of any primary product", that is, all subsidies that have an export-enhancing effect, and not just subsidies that are contingent on export performance. According to Brazil, the focus of Article XVI:3 is upon the effect of subsidies in enhancing exports, and not upon formal distinctions between export contingent and other subsidies.¹¹⁷⁹

754. Secondly, Brazil *conditionally* requests the Appellate Body to complete the analysis of its claim that United States price-contingent subsidies¹¹⁸⁰ result in the United States having a "more than equitable share of world export trade" in upland cotton, in violation of Article XVI:3, second sentence.¹¹⁸¹ Brazil's request to complete the analysis is conditional upon two events: (i) a reversal by

¹¹⁷⁵*Ibid.*, Section VII:E.

¹¹⁷⁶*Ibid.*, para. 7.1016.

¹¹⁷⁷*Ibid.*, para. 7.1017.

¹¹⁷⁸Brazil's other appellant's submission, para. 3.19.

¹¹⁷⁹Brazil's other appellant's submission, paras. 323-327.

¹¹⁸⁰That is, marketing loan payments, Step 2 payments, market loss assistance payments and counter-cyclical payments.

¹¹⁸¹Brazil's other appellant's submission, para. 3.18.

the Appellate Body of the Panel's finding regarding *significant price suppression* (resulting in serious prejudice in terms of Articles 6.3(c) and 5(c) of the *SCM Agreement*); and, (ii) denial by the Appellate Body of Brazil's request for a ruling that the United States' measures at issue resulted in an increase of the United States' *world market share* in upland cotton (resulting in serious prejudice in terms of Articles 6.3(d) and 5(c) of the *SCM Agreement*).¹¹⁸² Brazil submits that there are sufficient factual findings by the Panel or undisputed facts on the record to allow the Appellate Body to complete the analysis of Brazil's claim regarding violation of Article XVI:3 by the United States price-contingent subsidies.¹¹⁸³

755. The United States emphasizes that the text of Article XVI distinguishes between "Subsidies in General" (Section A) and "Additional Provisions on Export Subsidies" (Section B). By locating Article XVI:3 in Section B, Members agreed that Article XVI:3 is a provision on export subsidies.¹¹⁸⁴ The term "export subsidy" is now defined in the *SCM Agreement* and the *Agreement on Agriculture* as referring to subsidies that are contingent on export performance.¹¹⁸⁵ Both the context provided by these Agreements, as well as their negotiating history, confirm that the export subsidies referred to in Article XVI:3 are also subsidies contingent on export performance.¹¹⁸⁶

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756. With respect to Brazil's conditional request to complete the analysis, the United States contends that, even if the Appellate Body reverses the Panel's interpretation regarding the scope of Article XVI:3, there would be insufficient undisputed facts on the record or factual findings by the Panel to complete the analysis. The United States observes that the Panel did not make any findings on causation relative to trade shares. Nor has Brazil put forward a tenable standard for assessing what is more than an "equitable" trade share.¹¹⁸⁷

2. Analysis

757. Article XVI of the GATT 1994 contains two sections. "Section A" lays down certain rules for "Subsidies in General". "Section B", containing paragraphs 2-5 of Article XVI, provides "Additional Provisions on Export Subsidies". In Article XVI:2, the Members "recognize" that the

¹¹⁸² *Ibid.*, para. 319. We observe that Brazil does *not appeal* the Panel's findings with regard to Article XVI:1 and the relationship between Articles XVI:1 and XVI:3 (Panel Report, paras. 7.1470-7.1476), and does not appear to rely to any great extent on Article XVI:1 in its arguments relating to this part of its appeal.

¹¹⁸³ Brazil's other appellant's submission, paras. 371-379.

¹¹⁸⁴ United States' appellee's submission, para. 167.

¹¹⁸⁵ *Ibid.*, para. 168.

¹¹⁸⁶ *Ibid.*, paras. 169-180.

¹¹⁸⁷ United States' appellee's submission, paras. 181-187.

provision of "a subsidy on the export of any product may have harmful effects ...". Article XVI:3, the provision at issue in this part of Brazil's appeal, sets forth that "[a]ccordingly":

Members should seek to avoid the use of subsidies on the export of primary products. *If, however, a Member grants directly or indirectly any form of subsidy which operates to increase the export of any primary product from its territory, such subsidy shall not be applied in a manner which results in that Member having more than an equitable share of world export trade in that product, account being taken of the shares of the Members in such trade in the product during a previous representative period, and any special factors which may have affected or may be affecting such trade in the product.* (ad note omitted; emphasis added)*

758. The Panel found "that Article XVI:3 applies only to export subsidies as that term is now defined in the *Agreement on Agriculture* and the *SCM Agreement*".¹¹⁸⁸ In the light of its rulings under the *Agreement on Agriculture* and the *SCM Agreement* with regard to the United States' export subsidies at issue in the proceedings, the Panel exercised judicial economy with respect to Brazil's claims under Article XVI:3 of the GATT 1994.¹¹⁸⁹

759. Brazil's appeal of these findings has two elements. First, Brazil's appeal focuses on the phrase "any form of subsidy which operates to increase the export of any primary product". It argues that the ordinary meaning of this phrase encompasses all subsidies with an export-enhancing effect, not just those that are *contingent* on export performance. Second, Brazil requests the Appellate Body to complete the analysis and find that the United States' price-contingent subsidies violate Article XVI:3, second sentence, *conditional* upon two events: reversal by the Appellate Body of the Panel's finding of significant price suppression and serious prejudice within the meaning of Articles 6.3(c) and 5(c) of the *SCM Agreement*, as well as denial, by the Appellate Body, of Brazil's appeal concerning the interpretation and application of Articles 6.3(d) and 5(c) of the *SCM Agreement*.

760. With respect to the second element of Brazil's appeal, we note that, above, we upheld the Panel's finding that the effect of the price-contingent subsidies at issue in these proceedings is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*.¹¹⁹⁰ We observe, therefore, that the initial condition upon which Brazil's request to complete the analysis of this claim rests is *not* made out, and thus there is no need for us to complete the analysis and to examine whether or not the United States subsidies challenged by Brazil resulted in the United States having more than an equitable share of world export trade in upland cotton.

¹¹⁸⁸ Panel Report, para. 7.1016.

¹¹⁸⁹ *Ibid.*, para. 7.1017

¹¹⁹⁰ *Supra*, para. 496.

761. Nor do we believe that it is necessary to make a finding on the interpretation of the phrase "any form of subsidy which operates to increase the export of any primary product" in the second sentence of Article XVI:3 of the GATT 1994 in order to resolve this dispute. Given our ruling under Article 6.3(c) of the *SCM Agreement*, we observe that, although any ruling by the Appellate Body on the scope of the subsidies covered by Article XVI:3 of the GATT 1994 in the abstract might at best offer some degree of "guidance", it would not affect the resolution of this dispute.¹¹⁹¹ Indeed, irrespective of whether we were to uphold or reverse the Panel's finding on this issue, upon adoption of the recommendations and rulings by the DSB, the United States would be under no additional obligation regarding implementation. Thus, although we recognize that there may be cases in which it would be useful for us to make a finding on an issue, despite the fact that our finding would not result in recommendations and rulings by the DSB, we find no compelling reason for doing so in this case in respect of this particular issue.

762. We therefore believe that an interpretation of the phrase "any form of subsidy which operates to increase the export" in Article XVI:3 of the GATT 1994 is unnecessary for purposes of resolving this dispute. We emphasize that we neither uphold nor reverse the Panel's interpretation of this phrase in the second sentence of Article XVI:3.

VIII. Findings and Conclusions

763. For the reasons set out in this Report, the Appellate Body:

- (a) as regards procedural matters:
- (i) in relation to production flexibility contract payments and market loss assistance payments:
 - upholds the Panel's finding, in paragraphs 7.118, 7.122, 7.128, and 7.194(ii) of the Panel Report, that Articles 4.2 and 6.2 of the DSU do not exclude expired measures from the potential scope of consultations or a request for establishment of a panel and, therefore, that production flexibility contract payments and market loss assistance payments fell within the Panel's terms of reference; and
 - finds that the Panel set out the findings of fact, the applicability of relevant provisions, and the basic rationale behind this finding, as required by Article 12.7 of the DSU; and
 - (ii) in relation to export credit guarantee programs:
 - upholds the Panel's ruling, in paragraph 7.69 of the Panel Report, that "export credit guarantees to facilitate the export of United States upland cotton, and other eligible agricultural commodities ... are within its terms of reference"; and
 - upholds the Panel's ruling, in paragraph 7.103 of the Panel Report, that "Brazil provided a statement of available evidence with respect to export credit guarantee measures relating to upland cotton and eligible United States agricultural products other than upland cotton, as required by Article 4.2 of the *SCM Agreement*";

(b) as regards the application of Article 13 of the *Agreement on Agriculture* to this dispute:

- (i) in relation to Article 13(a)(ii):
 - upholds the Panel's finding, in paragraphs 7.388, 7.413, 7.414, and 8.1(b) of the Panel Report, that production flexibility contract

¹¹⁹¹We note in this regard that, in *US – Steel Safeguards*, the Appellate Body noted that "several participants expressed an interest in having [it] rule on causation as it would provide guidance to Members on applying safeguard measures in the future consistently with their WTO obligations". (Appellate Body Report, *US – Steel Safeguards*, para. 484) (original emphasis) Despite this request for guidance, the Appellate Body declined to make a ruling on this specific aspect of the case. (Appellate Body Report, *US – Steel Safeguards*, paras. 485–491)

payments and direct payments are not green box measures that fully conform to paragraph 6(b) of Annex 2 of the *Agreement on Agriculture*; and, therefore, are not exempt from actions under Article XVI of GATT 1994 and Part III of the *SCM Agreement* by virtue of Article 13(a)(ii) of the *Agreement on Agriculture*; and

- declines to rule on Brazil's conditional request that the Appellate Body find that the updating of base acres for direct payments under the FSRI Act of 2002 means that direct payments are not green box measures that fully conform to paragraph 6(a) of Annex 2 of the *Agreement on Agriculture*; and, therefore, are not exempt from actions under Article XVI of GATT 1994 and Part III of the *SCM Agreement* by virtue of Article 13(a)(ii) of the *Agreement on Agriculture*; and

(ii) in relation to Article 13(b)(ii):

- modifies the Panel's interpretation, set out in paragraph 7.494 of the Panel Report, of the phrase "support to a specific commodity" in Article 13(b)(ii) of the *Agreement on Agriculture*; but upholds the Panel's finding, in paragraphs 7.518 and 7.520 of the Panel Report, that Step 2 payments to domestic users, marketing loan program payments, production flexibility contract payments, market loss assistance payments, direct payments, counter-cyclical payments, crop insurance payments, and cottonseed payments (the "challenged domestic support measures") granted "support to a specific commodity", namely, upland cotton;

- declines to rule on the United States' appeal that only the price gap methodology described in paragraph 10 of Annex 3 of the *Agreement on Agriculture* may be used to measure the value of marketing loan program payments and deficiency payments for the purposes of the comparison required by Article 13(b)(ii) of the *Agreement on Agriculture*; and

- upholds the Panel's finding, in paragraphs 7.608 and 8.1(c) of the Panel Report, that the "challenged domestic support measures"

granted, in the years 1999, 2000, 2001 and 2002, support to a specific commodity, namely, upland cotton, in excess of that decided during the 1992 marketing year; and, therefore, that these measures are not exempt from actions based on Articles 5 and 6 of the *SCM Agreement* and Article XVI:1 of the GATT 1994 by virtue of Article 13(b)(ii) of the *Agreement on Agriculture*;

(c) as regards serious prejudice:

(i) in relation to Article 6.3(c) of the *SCM Agreement*:

- upholds the Panel's finding, in paragraphs 7.1416 and 8.1(g)(i) of the Panel Report, that the effect of the marketing loan program payments, Step 2 payments, market loss assistance payments, and counter-cyclical payments (the "price-contingent subsidies") is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*, by in turn upholding the Panel's findings:

(A) regarding the "market" and "price" in assessing whether "the effect of the subsidy is ... significant price suppression ... in the same market" within the meaning of Article 6.3(c) of the *SCM Agreement*:

- in paragraphs 7.1238-7.1240 of the Panel Report, that the "same market" may be a "world market";

- in paragraph 7.1247 of the Panel Report, that a "world market" for upland cotton exists; and

- in paragraph 7.1274 of the Panel Report, that "the A-Index can be taken to reflect a world price in the world market for upland cotton"; and

(B) regarding the "effect" of the price-contingent subsidies under Article 6.3(c) of the *SCM Agreement*:

- in paragraphs 7.1312 and 7.1333 of the Panel Report, that "significant price suppression" occurred within the meaning of Article 6.3(c);

- in paragraphs 7.1355 and 7.1363 of the Panel Report, that "a causal link exists" between the price-contingent subsidies and the significant price suppression found by the Panel under Article 6.3(c) and that this link is not attenuated by other factors raised by the United States;
- in paragraphs 7.1173, 7.1186, and 7.1226 of the Panel Report, that it was not required to quantify precisely the benefit conferred on upland cotton by the price-contingent subsidies and, consequently, not identifying the precise amount of counter-cyclical payments and market loss assistance payments that benefited upland cotton; and
- in paragraph 7.1416 of the Panel Report, that the effect of the price-contingent subsidies for marketing years 1999 to 2002 "is significant price suppression ... in the period MY 1999-2002"; and
- finds that the Panel, as required by Article 12.7 of the DSU, set out the findings of fact, the applicability of relevant provisions, and the basic rationale behind its findings, in paragraphs 7.1416 and 8.1(g)(i) of the Panel Report, that the effect of the price-contingent subsidies is significant price suppression within the meaning of Article 6.3(c) of the *SCM Agreement*; and
- (ii) in relation to Article 6.3(d) of the *SCM Agreement*:
- finds it unnecessary, for the purposes of resolving this dispute, to rule on the interpretation of the phrase "world market share" in Article 6.3(d) of the *SCM Agreement*, and neither upholds nor reverses the Panel's findings in this regard; and
- declines to rule on Brazil's conditional request for the Appellate Body to find that the effect of the price-contingent subsidies is an increase in the United States' world market share in upland cotton within the meaning of Article 6.3(d) of the *SCM Agreement*;
- (d) as regards user marketing (Step 2) payments:
- (i) upholds the Panel's findings, in paragraphs 7.1088, 7.1097-7.1098, and 8.1(f) of the Panel Report, that Step 2 payments to *domestic users* of United States upland cotton, under Section 1207(a) of the FSRI Act of 2002, are subsidies contingent on the use of domestic over imported goods that are inconsistent with Articles 3.1(b) and 3.2 of the *SCM Agreement*; and
- (ii) upholds the Panel's findings, in paragraphs 7.748-7.749, 7.760-7.761, and 8.1(e) of the Panel Report, that Step 2 payments to *exporters* of United States upland cotton, pursuant to Section 1207(a) of the FSRI Act of 2002, are subsidies contingent upon export performance within the meaning of Article 9.1(a) of the *Agreement on Agriculture* that are inconsistent with Articles 3.3 and 8 of that Agreement and Articles 3.1(a) and 3.2 of the *SCM Agreement*;
- (e) as regards export credit guarantee programs:
- (i) upholds the Panel's findings, in paragraphs 7.901, 7.911, and 7.932 of the Panel Report, that Article 10.2 of the *Agreement on Agriculture* does not exempt export credit guarantees from the export subsidy disciplines in Article 10.1 of that Agreement¹¹⁹²;
- (ii) finds that the Panel did not improperly apply the burden of proof in finding that the United States' export credit guarantee programs are prohibited export subsidies under Article 3.1(a) of the *SCM Agreement* and are consequently inconsistent with Article 3.2 of that Agreement;
- (iii) declines to find that the Panel erred by failing to make the necessary findings of fact in assessing whether the export credit guarantee programs are provided at premium rates that are inadequate to cover long-term operating costs and losses within the meaning of item (j) of the Illustrative List of Export Subsidies annexed to the *SCM Agreement*; and, consequently,

¹¹⁹²See Separate Opinion, *supra*, paras. 631-641.

(iv) upholds the Panel's finding, in paragraph 7.869 of the Panel Report, that "the United States export credit guarantee programmes at issue—GSM 102, GSM 103 and SCGP—constitute a *per se* export subsidy within the meaning of item (j) of the Illustrative List of Export Subsidies in Annex I of the *SCM Agreement*", and upholds the Panel's findings, in paragraphs 7.947 and 7.948 of the Panel Report, that these export credit guarantee programs are export subsidies for purposes of Article 3.1(a) of the *SCM Agreement* and are inconsistent with Articles 3.1(a) and 3.2 of that Agreement; and

(v) finds that the Panel did not err in exercising judicial economy in respect of Brazil's allegation that the United States' export credit guarantee programs are prohibited export subsidies, under Article 3.1(a) of the *SCM Agreement*, because they confer a "benefit" within the meaning of Article 1.1 of that Agreement;

(f) as regards circumvention of export subsidy commitments:

(i) reverses the Panel's finding, in paragraph 7.881 of the Panel Report, that Brazil did not establish actual circumvention in respect of poultry meat and pig meat; finds, however, that there are insufficient uncontested facts in the record to complete the legal analysis to determine whether the United States' export credit guarantees to poultry meat and pig meat have been applied in a manner that "results in" circumvention of the United States' export subsidy commitments, within the meaning of Article 10.1 of the *Agreement on Agriculture*;

(ii) modifies the Panel's interpretation, in paragraphs 7.882-7.883 and 7.896 of the Panel Report, of the phrase "threatens to lead to circumvention" in Article 10.1 of the *Agreement on Agriculture* to the extent that the Panel's interpretation requires "an unconditional legal entitlement" to receive the relevant export subsidies as a condition for a finding of threat of circumvention, but upholds, for different reasons, the Panel's finding, in paragraph 7.896 of the Panel Report, that Brazil has not established that "the export credit guarantee programmes at issue are generally applied to scheduled agricultural products other than rice and other unscheduled agricultural products (not supported under the programmes) in a manner which threatens to lead to circumvention of United States export subsidy

commitments within the meaning of Article 10.1 of the *Agreement on Agriculture*"; and

(iii) finds that the Panel did not err in confining its examination of Brazil's threat of circumvention claim to scheduled products other than rice and unscheduled products not supported under the United States' export credit guarantee programs;

(g) as regards the ETI Act of 2000, declines Brazil's request that the Appellate Body reverse the Panel's conclusion that Brazil did not make a *prima facie* case that the ETI Act of 2000 is inconsistent with the United States' WTO obligations; and

(h) as regards Article XVI:3 of the GATT 1994:

(i) finds it unnecessary, for the purposes of resolving this dispute, to rule on the interpretation of the phrase "any form of subsidy which operates to increase the export" in Article XVI:3 of the GATT 1994, and neither upholds nor reverses the Panel's findings in this regard; and

(ii) declines to rule on Brazil's conditional request for the Appellate Body to find that the price-contingent subsidies cause the United States to have "more than an equitable share of world export trade" in upland cotton, in violation of the second sentence of Article XVI:3 of the GATT 1994.

764. The Appellate Body recommends that the Dispute Settlement Body request the United States to bring its measures, found in this Report and in the Panel Report as modified by this Report to be inconsistent with the *Agreement on Agriculture* and the *SCM Agreement*, into conformity with its obligations under those Agreements.

Signed in the original in Geneva this 10th day of February 2005 by:

Merit E. Janow
Presiding Member

Luiz Olavo Baptista
Member

A.V. Ganesan
Member

ANNEX 1

**WORLD TRADE
ORGANIZATION**

WT/DS267/17
20 October 2004
(04-4441)

Original: English

UNITED STATES – SUBSIDIES ON UPLAND COTTON

Notification of an Appeal by the United States
under paragraph 4 of Article 16 of the Understanding on Rules
and Procedures Governing the Settlement of Disputes ("DSU")

The following notification, dated 18 October 2004, from the Delegation of the United States, is being circulated to Members.

Pursuant to Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 20 of the Working Procedures for Appellate Review, the United States hereby notifies its decision to appeal to the Appellate Body certain issues of law covered in the Report of the Panel on *United States – Subsidies on Upland Cotton* (WT/DS267/R) and certain legal interpretations developed by the Panel in this dispute.

1. The United States seeks review by the Appellate Body of the Panel's legal conclusion that certain U.S. decoupled income support measures – that is, production flexibility contract payments under the Federal Agricultural Improvement and Reform Act of 1996 ("1996 Act"), direct payments under the Farm Security and Rural Investment Act of 2002 ("2002 Act"), and "the legislative and regulatory provisions which establish and maintain the [direct payments] programme" – are not exempt from actions under Article 13(a) of the *Agreement on Agriculture*.¹ This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations. These erroneous findings include, for example, that these decoupled income support measures do not conform to Annex 2.

2. The United States seeks review by the Appellate Body of the Panel's legal conclusion that certain U.S. domestic support measures² are not exempt from actions under Article 13(b) of the *Agreement on Agriculture*.³ This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations. These erroneous findings include, for example, the Panel's finding that the challenged U.S. measures granted support to a specific commodity in excess of that decided in marketing year 1992 and therefore breached the proviso of Article 13(b) in each year from marketing year 1999-2002.

¹ See, e.g., Panel Report, paras. 8.1(b), 7.337-7.414.

² See Panel Report, para. 7.337.

³ See, e.g., Panel Report, paras. 8.1(c), 7.415-7.647.

3. The United States seeks review by the Appellate Body of the Panel's legal conclusion that U.S. export credit guarantees under the GSM 102, GSM 103, and SCGP export credit guarantee programs in respect of unscheduled agricultural products supported under the programs and one scheduled commodity (rice) are "export subsidies applied in a manner which results in circumvention of United States export subsidy commitments, within the meaning of Article 10.1 of the *Agreement on Agriculture*," are therefore inconsistent with Article 8 of the *Agreement on Agriculture*, and are not exempt from actions under Article 13(c) of the *Agreement on Agriculture*.⁴ This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations. These erroneous findings include, for example, the Panel's finding that export credit guarantees, notwithstanding Article 10.2 of the *Agreement on Agriculture*, constitute measures subject to Article 10.1 of the *Agreement on Agriculture*.

4. The United States seeks review by the Appellate Body of the Panel's legal conclusion that U.S. export credit guarantees under the GSM 102, GSM 103, and SCGP export credit guarantee programs in respect of other scheduled agricultural products constitute export subsidies within the meaning of Article 10.1 of the *Agreement on Agriculture*.⁵ This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations. These erroneous findings include, for example, the Panel's finding that export credit guarantees, notwithstanding Article 10.2 of the *Agreement on Agriculture*, constitute measures subject to Article 10.1 of the *Agreement on Agriculture*.

5. The United States seeks review by the Appellate Body of the Panel's legal conclusion that U.S. export credit guarantees under the GSM 102, GSM 103, and SCGP export credit guarantee programs in respect of unscheduled agricultural products supported under the programs and one scheduled commodity (rice) are *per se* export subsidies prohibited by Articles 3.1(a) and 3.2 of the *Agreement on Subsidies and Countervailing Measures* ("SCM Agreement").⁶ This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations. These erroneous findings include, for example, the Panel's finding that the program for each product constitutes an export subsidy for purposes of the WTO Agreements and is provided by the United States at premium rates which are inadequate to cover long-term operating costs and losses of the programs within the meaning of item (j) of the Illustrative List of Export Subsidies in Annex I of the SCM Agreement.

6. The United States seeks review by the Appellate Body of the Panel's legal conclusion that section 1207(a) of the 2002 Act, which provides for user marketing (Step 2) payments to exporters of upland cotton, is an export subsidy that is listed in Article 9.1(a) of the *Agreement on Agriculture* that is inconsistent with U.S. obligations under Articles 3.3 and 8 of the *Agreement on Agriculture*, is not exempt from actions under Article 13(c) of the *Agreement on Agriculture*, and is inconsistent with Articles 3.1(a) and 3.2 of the SCM Agreement.⁷ This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations. These erroneous findings include, for example, the Panel's finding that payments under the user marketing (Step 2) program are contingent on export performance.

7. The United States seeks review by the Appellate Body of the Panel's legal conclusion that section 1207(a) of the 2002 Act providing for user marketing (Step 2) payments to domestic users of upland cotton is an import substitution subsidy prohibited under Articles 3.1(b) and 3.2 of the

⁴ See, e.g., Panel Report, paras. 8.1(d)(1), 7.762-7.945.

⁵ See, e.g., Panel Report, paras. 8.1(d)(2), 7.762-7.945.

⁶ See, e.g., Panel Report, paras. 8.1(d)(1), 7.787-7.869, 7.946-7.948.

⁷ See, e.g., Panel Report, paras. 7.678-7.761, 8.1(e).

Agreement on Subsidies and Countervailing Measures.⁸ This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations. These erroneous findings include, for example, the Panel's finding that domestic support payments that are consistent with a Member's domestic support reduction commitments under the *Agreement on Agriculture* may nonetheless be prohibited under the SCM Agreement.

8. The United States seeks review by the Appellate Body of the Panel's legal conclusion that "the effect of the mandatory, price contingent United States subsidies at issue – that is, marketing loan programme payments, user marketing (Step 2) payments and MLA payments and CCP payments – is significant price suppression in the same world market for upland cotton in the period MY 1999-2002 within the meaning of Articles 6.3(c) and 5(c)" of the SCM Agreement.⁹ This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations. These erroneous findings include, for example, the following:

- (a) the Panel's finding that Brazil need not demonstrate, and the Panel need not find, the amount of the challenged subsidy that benefits the subsidized product, upland cotton;
- (b) the Panel's finding that subsidies not directly tied to current production of upland cotton (decoupled payments) need not be allocated to all products produced and sold by the firms receiving such subsidies;
- (c) that the Panel could make findings concerning subsidies that no longer existed at the time of panel establishment and that present serious prejudice could be, and was, caused by such subsidies;
- (d) the Panel's finding that the challenged subsidies provided to cotton producers "passed through" to cotton exporters;
- (e) the Panel's finding that there was price suppression "in the same market";
- (f) the Panel's finding that significant price suppression existed;
- (g) the Panel's finding that the price suppression it found under an erroneous legal standard was "significant";
- (h) the Panel's finding that "the effect of" the U.S. subsidies "is" significant price suppression;
- (i) the Panel's finding that "significant price suppression" is sufficient to establish "serious prejudice" for purposes of Articles 5(c) and 6.3 of the SCM Agreement; and
- (j) the Panel's finding that its "present" serious prejudice findings include findings of inconsistency that deal with the FSRI Act of 2002 and subsidies granted thereunder in MY 2002."¹⁰

9. The United States seeks review by the Appellate Body of the Panel's finding that decoupled payments made with respect to non-upland cotton base acres were within its terms of reference.¹¹ This finding is in error and is based on erroneous findings on issues of law and related legal

⁸See, e.g., Panel Report, paras. 7.1018-7.1098, 8.1(f).

⁹Panel Report, paras. 7.1416, 7.1107-7.1416, 8.1(g)(i).

¹⁰See, e.g., Panel Report, para. 7.1501.

¹¹See, e.g., Panel Report, paras. 7.129-7.136.

interpretations. These erroneous findings include, for example, the Panel's finding that these payments were measures at issue within the meaning of Articles 4.4 and 6.2 of the DSU.

10. The United States requests the Appellate Body to find that the Panel failed to set out the findings of fact, the applicability of the relevant provisions, and the basic rationale behind its findings and recommendations, as required by Article 12.7 of the DSU. The Panel's failure to set these out include, for example, the findings or lack of findings concerning the following areas: the amount of the challenged subsidies, including the amount of payments not directly tied to current production of upland cotton (decoupled payments); that significant price suppression existed; the degree of price suppression it deemed "significant"; that "the effect of" the U.S. subsidies "is" significant price suppression; that decoupled payments made with respect to non-upland cotton base acres were within its terms of reference; and the basis for its ability to make findings with respect to subsidies that no longer existed at the time of panel establishment.

11. The United States seeks review by the Appellate Body of the Panel's finding that export credit guarantees to facilitate the export of "other eligible agricultural commodities" besides upland cotton were within its terms of reference.¹² This finding is in error and is based on erroneous findings on issues of law and related legal interpretations. These erroneous findings include, for example, the Panel's finding that such export credit guarantees were included in Brazil's consultation request and its finding that, contrary to Articles 4.2, 4.4, and 6.2 of the DSU, it could examine measures that were not included in Brazil's request for consultations.

12. The United States seeks review by the Appellate Body of the Panel's finding that Brazil provided the statement of available evidence required by Article 4.2 of the SCM Agreement with respect to export credit guarantee measures relating to eligible United States agricultural products other than upland cotton, and that accordingly, Brazil's claims concerning these measures were within the terms of reference of this dispute.¹³ This finding is in error and is based on erroneous findings on issues of law and related legal interpretations.

13. In the event Brazil appeals the Panel's exercise of judicial economy with respect to Brazil's claims concerning the compatibility of U.S. export credit guarantee measures with Part III of the SCM Agreement,¹⁴ in this U.S. appeal the United States conditionally requests the Appellate Body to find that Brazil also failed to provide a statement of available evidence as required by Article 7.2 of the SCM Agreement, and that accordingly, Brazil's claims concerning these measures would not be within the terms of reference of this dispute.

14. The United States seeks review by the Appellate Body of the Panel's legal conclusion that two types of expired measures, production flexibility contract payments and market loss assistance payments, were within the Panel's terms of reference. This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations. These erroneous findings include, for example, the Panel's finding that measures that are no longer in existence as of the date of establishment of a panel are nonetheless within a panel's terms of reference.¹⁵

¹²See, e.g., Panel Report, para. 7.69.

¹³See, e.g., Panel Report, para. 7.103.

¹⁴See, e.g., Panel Report, para. 7.78.

¹⁵See, e.g., Panel Report, para. 7.104-7.122.

ANNEX 2

Table 1: Comparison of Support for Purposes of Article 13(b)(ii) of the Agreement on Agriculture (using budgetary outlays for marketing loan program payments and deficiency payments)

\$ million	MY 1992	MY 1999	MY 2000	MY 2001	MY 2002
Step 2 payments (domestic users) *	102.7	165.8	260	144.8	72.4
Crop insurance payments *	26.6	169.6	161.7	262.9	194.1
Cottonseed payments *	0	79	184.7	0	50
PFC payments +	0	434.9	411.7	329.5	0
MLA payments +	0	432.8	438.3	452.3	0
DP payments +	0	0	0	0	391.8
CCP payments +	0	0	0	0	864.9
Marketing loan program *	866	1761	636	2609	897.8
Deficiency payments *	1017.4	0	0	0	0
Total	2012.7	3043.1	2092.4	3798.5	2471

Table 2: Comparison of Support for Purposes of Article 13(b)(ii) of the Agreement on Agriculture (using price gap methodology for marketing loan program payments and deficiency payments)

\$ million	MY 1992	MY 1999	MY 2000	MY 2001	MY 2002
Step 2 payments (domestic users) *	102.7	165.8	260	144.8	72.4
Crop insurance payments *	26.6	169.6	161.7	262.9	194.1
Cottonseed payments *	0	79	184.7	0	50
PFC payments +	0	434.9	411.7	329.5	0
MLA payments +	0	432.8	438.3	452.3	0
DP payments +	0	0	0	0	391.8
CCP payments +	0	0	0	0	864.9
Marketing loan program §	-84	-133	-136	-162	-130
Deficiency payments §	867	0	0	0	0
Total	912.3	1149.1	1320.4	1027.5	1443.2

Table 3: Values Attributable to the Price-Contingent Subsidies

\$ million	MY 1999	MY 2000	MY 2001	MY 2002
Marketing loan program *	1761	636	2609	897.8
Step 2 payments (domestic users & exporters) #	279.3	445.3	235.7	177.8
MLA payments +	432.8	438.3	452.3	0
CCP payments +	0	0	0	864.9
Total	2473.1	1519.6	3297	1940.5

Notes to Tables:

For the panel's findings regarding the values of support relevant for the analysis under Article 13(b)(ii) of the Agreement on Agriculture, see Panel Report, para. 7.596.

* Panel Report, para. 7.596.

+ The values of production flexibility contract payments, market loss assistance payments, direct payments, and counter-cyclical payments are based on the "cotton to cotton" methodology, discussed *supra*, paras. 377-380. Figures are drawn from Panel Report, para. 7.641.

§ Panel Report, para. 7.564 and footnote 727 to para. 7.565.

For the value of Step 2 payments to domestic users, see Panel Report, para. 7.596. To these figures we have added data submitted by the United States for the value of Step 2 payments to exporters: see United States' response to questions posed by the Panel, Panel Report, p. I-126, para. 211.

World Trade Organization

Mexico – Tax Measures on Soft Drinks and Other Beverages

Report of the Appellate Body, 6 March 2006

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**MEXICO – TAX MEASURES ON SOFT DRINKS
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AB-2005-10

Report of the Appellate Body

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Short Title	Full Case Title and Citation
Argentina – Poultry Anti-Dumping Duties	Panel Report, <i>Argentina – Definitive Anti-Dumping Duties on Poultry from Brazil</i> , WT/DS241/R, adopted 19 May 2003, DSR 2003:V, 1727
Australia – Salmon	Appellate Body Report, <i>Australia – Measures Affecting Importation of Salmon</i> , WT/DS18/AB/R, adopted 6 November 1998, DSR 1998:VIII, 3327
Canada – Aircraft	Appellate Body Report, <i>Canada – Measures Affecting the Export of Civilian Aircraft</i> , WT/DS70/AB/R, adopted 20 August 1999, DSR 1999:III, 1377
Canada – Wheat Exports and Grain Imports	Appellate Body Report, <i>Canada – Measures Relating to Exports of Wheat and Treatment of Imported Grain</i> , WT/DS276/AB/R, adopted 27 September 2004
Dominican Republic – Import and Sale of Cigarettes	Appellate Body Report, <i>Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes</i> , WT/DS302/AB/R, adopted 19 May 2005
EC – Bananas III	Appellate Body Report, <i>European Communities – Regime for the Importation, Sale and Distribution of Bananas</i> , WT/DS271/AB/R, adopted 25 September 1997, DSR 1997:II, 591
EC – Export Subsidies on Sugar	Appellate Body Report, <i>European Communities – Export Subsidies on Sugar</i> , WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R, adopted 19 May 2005
EC – Hormones	Appellate Body Report, <i>EC Measures Concerning Meat and Meat Products (Hormones)</i> , WT/DS26/AB/R, WT/DS48/AB/R, adopted 13 February 1998, DSR 1998:I, 135
India – Patents (US)	Appellate Body Report, <i>India – Patent Protection for Pharmaceutical and Agricultural Chemical Products</i> , WT/DS50/AB/R, adopted 16 January 1998, DSR 1998:I, 9
Korea – Various Measures on Beef	Appellate Body Report, <i>Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef</i> , WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, DSR 2001:I, 5
Mexico – Corn Syrup (Article 21.5 – US)	Appellate Body Report, <i>Mexico – Anti-Dumping Investigation of High Fructose Corn Syrup (HFCS) from the United States – Recourse to Article 21.5 of the DSU by the United States</i> , WT/DS132/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6675
Mexico – Taxes on Soft Drinks	Panel Report, <i>Mexico – Tax Measures on Soft Drinks and Other Beverages</i> , WT/DS308/R, 7 October 2005
US – 1916 Act	Appellate Body Report, <i>United States – Anti-Dumping Act of 1916</i> , WT/DS136/AB/R, WT/DS162/AB/R, adopted 26 September 2000, DSR 2000:X, 4793
US – Corrosion-Resistant Steel Sunset Review	Appellate Body Report, <i>United States – Sunset Review of Anti-Dumping Duties on Corrosion-Resistant Carbon Steel Flat Products from Japan</i> , WT/DS244/AB/R, adopted 9 January 2004
US – FSC (Article 21.5 – EC)	Appellate Body Report, <i>United States – Tax Treatment for “Foreign Sales Corporations” – Recourse to Article 21.5 of the DSU by the European Communities</i> , WT/DS108/AB/RW, adopted 29 January 2002, DSR 2002:I, 55
US – Gambling	Appellate Body Report, <i>United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services</i> , WT/DS285/AB/R, adopted 20 April 2005
US – Gasoline	Appellate Body Report, <i>United States – Standards for Reformulated and Conventional Gasoline</i> , WT/DS2/AB/R, adopted 20 May 1996, DSR 1996:I, 3

Short Title	Full Case Title and Citation
US – Section 337	GATT Panel Report, <i>United States Section 337 of the Tariff Act of 1930</i> , adopted 7 November 1989, BISD 36S/345
US – Shrimp	Appellate Body Report, <i>United States – Import Prohibition of Certain Shrimp and Shrimp Products</i> , WT/DS58/AB/R, adopted 6 November 1998, DSR 1998:VII, 2755
US – Shrimp (Article 21.5 – Malaysia)	Appellate Body Report, <i>United States – Import Prohibition of Certain Shrimp and Shrimp Products – Recourse to Article 21.5 of the DSU by Malaysia</i> , WT/DS58/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6481
US – Wool Shirts and Blouses	Appellate Body Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/AB/R and Corr.1, adopted 23 May 1997, DSR 1997:I, 323

ABBREVIATIONS USED IN THIS REPORT

Abbreviation	Description
Division	Appellate Body Division hearing this appeal
DSB	Dispute Settlement Body
DSU	<i>Understanding on Rules and Procedures Governing the Settlement of Disputes</i>
GATT 1994	<i>General Agreement on Tariffs and Trade 1994</i>
HFCS	high-fructose corn syrup
Inter-American Convention	Inter-American Convention for the Protection and Conservation of Sea Turtles
ITO	International Trade Organization
NAFTA	North American Free Trade Agreement
Panel	Panel in <i>Mexico – Taxes on Soft Drinks</i>
Panel Report	Panel Report, <i>Mexico – Taxes on Soft Drinks</i>
<i>Working Procedures</i>	<i>Working Procedures for Appellate Review</i> , WT/AB/WP/5, 4 January 2005
WTO	World Trade Organization

WORLD TRADE ORGANIZATION
APPELLATE BODY

Mexico – Tax Measures on Soft Drinks and Other Beverages

AB-2005-10

Present:

Mexico, *Appellant*

United States, *Appellee*
Taniguchi, Presiding Member
Janow, Member
Sacerdoti, Member

Canada, *Third Participant*
China, *Third Participant*
European Communities, *Third Participant*
Guatemala, *Third Participant*
Japan, *Third Participant*

I. Introduction

1. Mexico appeals certain issues of law and legal interpretations developed in the Panel Report, *Mexico – Tax Measures on Soft Drinks and Other Beverages* (the "Panel Report").¹ The Panel was established to consider a complaint by the United States concerning certain tax measures and bookkeeping requirements imposed by Mexico on soft drinks and other beverages that use sweeteners other than cane sugar.

2. The measures challenged by the United States include: (i) a 20 per cent tax on the transfer or, as applicable, the importation of soft drinks and other beverages that use any sweetener other than cane sugar (the "soft drink tax"); (ii) a 20 per cent tax on specific services (commission, mediation, agency, representation, brokerage, consignment, and distribution), when such services are provided for the purpose of transferring products such as soft drinks and other beverages that use any sweetener other than cane sugar (the "distribution tax"); and (iii) a number of requirements imposed on taxpayers subject to the soft drink tax and to the distribution tax (the "bookkeeping requirements").² Before the Panel, the United States claimed that these measures are inconsistent with paragraphs 2 and 4 of Article III of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994").

3. In its first written submission to the Panel, Mexico requested that the Panel decide, as a preliminary matter, to "decline to exercise its jurisdiction in this case"³ and that it "recommend to the

¹WT/DS308/R, 7 October 2005.

²These measures are described in more detail in paragraphs 2.2-2.5 of the Panel Report.

³Panel Report, para. 4.2.

parties that they submit their respective grievances to an Arbitral Panel, under Chapter Twenty of the NAFTA⁴], which can address both Mexico's concern with respect to market access for Mexican cane sugar in the United States under the NAFTA and the United States' concern with respect to Mexico's tax measures.⁵ Mexico also stated that, in the event the Panel decided to exercise jurisdiction, the Panel should find that the measures are justified pursuant to Article XX(d) of the GATT 1994.⁶

4. On 18 January 2005, the Panel issued a preliminary ruling in which it rejected Mexico's request.⁷ In doing so, the Panel concluded that, "under the DSU⁸], it had no discretion to decide whether or not to exercise its jurisdiction in a case properly before it."⁹ The Panel added that, "even if it had such discretion, the Panel did not consider that there were facts on record that would justify the Panel declining to exercise its jurisdiction in the present case."¹⁰

5. In its Report, circulated to Members of the World Trade Organization (the "WTO") on 7 October 2005, the Panel concluded that:

(a) With respect to Mexico's soft drink tax and distribution tax:

- (i) As imposed on sweeteners, imported beet sugar is subject to internal taxes in excess of those applied to like domestic sweeteners, in a manner inconsistent with Article III:2, first sentence, of the GATT 1994;
- (ii) As imposed on sweeteners, imported HFCS¹¹ is being taxed dissimilarly compared with the directly competitive or substitutable products, so as to afford protection to the Mexican domestic production of cane sugar, in a manner inconsistent with Article III:2, second sentence, of the GATT 1994;
- (iii) As imposed on sweeteners, imported beet sugar and HFCS are accorded less favourable treatment than that accorded to like products of national origin, in a manner inconsistent with Article III:4 of the GATT 1994;
- (iv) As imposed on soft drinks and syrups, imported soft drinks and syrups sweetened with non-cane sugar sweeteners (including HFCS and beet sugar) are subject to internal taxes in excess of those applied to like domestic products, in a manner inconsistent with Article III:2, first sentence, of the GATT 1994.

⁴North American Free Trade Agreement (the "NAFTA").

⁵Panel Report, para. 3.2.

⁶*Ibid.*

⁷The Panel's preliminary ruling is reproduced as Annex B to the Panel Report.

⁸*Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU").

⁹Panel Report, para. 7.1.

¹⁰*Ibid.*

¹¹High-fructose corn syrup ("HFCS").

- (b) With respect to Mexico's bookkeeping requirements: As imposed on sweeteners, imported beet sugar and HFCS are accorded less favourable treatment than that accorded to like products of national origin, in a manner inconsistent with Article III:4 of the GATT 1994.¹²

The Panel rejected Mexico's defence under Article XX(d) of the GATT 1994, concluding that "the challenged tax measures are not justified as measures that are necessary to secure compliance by the United States with laws or regulations which are not inconsistent with the provisions of the GATT 1994."¹³ The Panel therefore recommended "that the Dispute Settlement Body request Mexico to bring the inconsistent measures ... into conformity with its obligations under the GATT 1994."¹⁴

6. On 6 December 2005, Mexico notified the Dispute Settlement Body (the "DSB") of its intention to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, pursuant to Article 16.4 of the DSU, and filed a Notice of Appeal¹⁵ pursuant to Rule 20(1) of the *Working Procedures for Appellate Review* (the "*Working Procedures*").¹⁶ On 13 December 2005, Mexico filed an appellant's submission.¹⁷ In its appeal, Mexico challenges the Panel's preliminary ruling rejecting Mexico's request that the Panel decline to exercise jurisdiction in this case, as well as the Panel's findings concerning Article XX(d) of the GATT 1994. Mexico did not appeal the Panel's findings under Article III of the GATT 1994. On 6 January 2006, the United States filed an appellee's submission.¹⁸ On the same day, China, the European Communities, and Japan each filed a third participant's submission.¹⁹ Also on the same day, Canada and Guatemala each notified the Appellate Body Secretariat of its intention to appear at the oral hearing as a third participant.²⁰

7. By letter dated 5 January 2006, Mexico requested authorization to correct certain clerical errors in its appellant's submission pursuant to Rule 18(5) of the *Working Procedures*. On 9 January 2006, the Appellate Body Division hearing the appeal ("the Division") invited all participants and third participants to comment on Mexico's request, in accordance with Rule 18(5). On 11 January 2006, the United States responded that, although some of the requested corrections are

¹²Panel Report, para. 9.2. (original underlining)

¹³*Ibid.*, para. 9.3.

¹⁴*Ibid.*, para. 9.5.

¹⁵WT/DS308/10 (attached as Annex I to this Report).

¹⁶WT/AB/WP/5, 4 January 2005.

¹⁷Pursuant to Rule 21(1) of the *Working Procedures*. A courtesy English translation of Mexico's appellant's submission, prepared by Mexico, was provided to the participants and third participants on 16 December 2005.

¹⁸Pursuant to Rule 22(1) of the *Working Procedures*.

¹⁹Pursuant to Rule 24(1) of the *Working Procedures*.

²⁰Pursuant to Rule 24(2) of the *Working Procedures*.

not "clearly clerical", within the meaning of Rule 18(5), "[i]n the circumstances of this dispute", the United States did not object to Mexico's request. No other comments were received. By letter dated 16 January 2006, the Division authorized Mexico to correct the clerical errors in its appellant's submission but emphasized, however, that it had not been requested, and did not make, a finding "as to whether all of the corrections requested by Mexico are 'clerical' within the meaning of Rule 18(5) of the *Working Procedures*."

8. On 13 January 2006, the Appellate Body received an *amicus curiae* brief from *Cámara Nacional de las Industrias Azucarera y Alcohólica* (National Chamber of the Sugar and Alcohol Industries) of Mexico.²¹ The Division did not find it necessary to take the brief into account in resolving the issues raised in this appeal.

9. The oral hearing in this appeal was held on 18 January 2006. The participants and third participants presented oral arguments (with the exception of Guatemala) and responded to questions posed by the Members of the Division hearing the appeal.

II. Arguments of the Participants and the Third Participants

A. *Claims of Error by Mexico – Appellant*

1. Exercise of Jurisdiction

10. Mexico argues that the Panel erred in rejecting Mexico's request that it decline to exercise jurisdiction in the circumstances of the present dispute. According to Mexico, the Panel's decision was primarily based on the Panel's view that Article 11 of the DSU "compels a WTO [p]anel to address the claims" on which a finding is necessary to enable the DSB to make sufficiently precise recommendations or rulings to the parties to the dispute and that, therefore, a WTO panel has no discretion to decline to exercise validly established jurisdiction.²² Mexico submits that this is incorrect and ignores the fact that, like other international bodies and tribunals, WTO panels have certain "implied jurisdictional powers"²³ that derive from their nature as adjudicative bodies. According to Mexico, such powers include the power to refrain from exercising substantive

²¹At the oral hearing, Mexico stated that its arguments are set out in its appellant's and oral submissions. Mexico added, however, that it would not object should the Appellate Body decide to accept the *amicus* brief. The United States noted that the *amicus* brief had been received late in the proceedings and that it presented new arguments and claims of error that were not part of Mexico's Notice of Appeal. Accordingly, while taking the view that the Appellate Body had the authority to accept the brief, the United States argued that it should decline to do so in the circumstances of this dispute.

²²Mexico's appellant's submission, para. 64 ("*obliga a un Grupo Especial de la OMC a abordar las reclamaciones*").

²³*Ibid.*, para. 65 ("*facultades implícitas en relación con su competencia*").

jurisdiction in circumstances where "the underlying or predominant elements of a dispute derive from rules of international law"²⁴ under which claims cannot be judicially enforced in the WTO, such as the NAFTA provisions or when one of the disputing parties refuses to take the matter to the "appropriate forum".²⁵ Mexico contends, in this regard, that the United States' claims under Article III of the GATT 1994 are inextricably linked to a broader dispute²⁶ concerning the conditions provided under the NAFTA for access of Mexican sugar to the United States market, and that only a NAFTA panel could resolve the dispute between the parties.

11. Mexico further emphasizes that there is nothing in the DSU that explicitly rules out the existence of a WTO panel's power to decline to exercise its jurisdiction even in a case that is properly brought before it. Mexico adds that the application by panels of the principle of "judicial economy" illustrates that notwithstanding the requirement of Article 7.2 of the DSU that panels address the relevant provisions in any covered agreement or agreements cited by the parties to the dispute, WTO panels can decide not to address certain claims. Thus, according to Mexico, there is no question that WTO panels have an implicit or inherent competence. As other examples of panels' "implied jurisdictional powers", Mexico points, *inter alia*, to the power of panels to determine whether they have substantive jurisdiction over a matter and the power to decide all matters that are inherent to the "adjudicative function"²⁷ of panels.

12. Finally, referring to the ruling of the Permanent Court of International Justice (the "PCIJ") in the *Factory at Chorzów* case, Mexico calls into question the "applicability" of its WTO obligations towards the United States in the context of this dispute.²⁸

2. Article XX(d) of the GATT 1994

13. Mexico appeals the Panel's finding that the measures at issue are not justified pursuant to Article XX(d) of the GATT 1994. In addition, Mexico requests the Appellate Body to complete the analysis and find that its tax measures are justified under Article XX(d) of the GATT 1994, because

²⁴Mexico's appellant's submission, para. 73 ("*los elementos predominantes de una disputa derivan de reglas del derecho internacional*").

²⁵*Ibid.* ("*foro adecuado*").

²⁶*Ibid.*

²⁷*Ibid.*, para. 67 ("*función jurisdiccional*").

²⁸See *ibid.*, paras. 73-74. The passage of the ruling that Mexico refers to reads as follows:
... one party cannot avail himself of the fact that the other has not fulfilled some obligation ... if the former party has ... prevented the latter ... from having recourse to the tribunal which would have been open to him.

(Permanent Court of International Justice, *Factory at Chorzów (Germany v. Poland)* (Jurisdiction), 1927, PCIJ Series A, No. 9, p. 31) (underlining added by Mexico omitted)

the measures are necessary "to secure compliance" by the United States of its obligations under the NAFTA.

14. Mexico asserts that the Panel erred in finding that the measures at issue are not designed "to secure compliance" within the meaning of Article XX(d). According to Mexico, this finding is based on an erroneous interpretation of the terms "to secure compliance" as involving enforcement action within a *domestic* legal system. Mexico argues that there is no basis to exclude action taken to enforce *international* treaty obligations from the scope of Article XX(d). Mexico adds that, in the broader context of international law, countermeasures are measures aimed at securing compliance with international obligations. Mexico further submits that the Panel erred by equating the concept of "enforcement" with that of "coercion". In Mexico's view, the Panel's effort to distinguish between actions at the domestic level and at the international level based on its understanding of the concept of coercion in this dispute has no textual basis, because Article XX(d) simply does not refer to the use of coercion.

15. Moreover, Mexico asserts that the Panel erred by confusing the issue of the "design" of the measure under Article XX(d) with the issue of its "outcome".²⁹ Rather than examining whether Mexico's measures were put in place in order to secure the United States' compliance with its NAFTA obligations, the Panel considered the effectiveness of those measures. Mexico emphasizes that "even if the outcome of a measure is completely uncertain or unpredictable, the measure in question can, nevertheless be 'designed to secure compliance with laws and regulations' within the meaning of Article XX(d)".³⁰ Contrary to the Panel's finding, the issue of the likely outcome of a given measure is not legally relevant to the assessment of the design of the measure under Article XX(d). Thus, Mexico takes issue with the Panel's finding that the "uncertain outcome of international countermeasures is a reason for disqualifying them as measures eligible for consideration under Article XX(d)".³¹ Mexico notes, in this regard, that nothing in the text of Article XX(d) suggests that any measure is *a priori* ineligible as a measure "to secure compliance with laws and regulations" on the basis of its "uncertain outcome".

16. Turning to the meaning of the terms "laws and regulations" in Article XX(d), Mexico notes that the Panel's interpretation of these terms is based on the erroneous conclusions reached by the Panel with respect to the terms "to secure compliance". Mexico submits that the words "laws" and

²⁹Mexico's appellant's submission, para. 98 ("*destino*"; "*resultado*").

³⁰*Ibid.*, para. 102 ("*aun si el resultado de la medida es totalmente incierto, impredecible, bien puede estar destinada a lograr la observancia de las leyes y reglamentos*" en el sentido del artículo XX(d)").

³¹*Ibid.*, para. 104 ("*el resultado incierto de las contramedidas internacionales es una razón para excluirlas como medidas que pueden ser objeto de consideración, en el marco del inciso (d) del artículo XX*") (quoting Panel Report, para. 8.187).

"regulations" are expressly qualified in other provisions of the covered agreements; the absence of qualifying language in Article XX(d) thus supports the view that the terms are not limited to *domestic* laws or regulations, but include international agreements. Mexico adds that a review of the Article XX exceptions reveals that only three—(paragraphs (c), (g), and (i))—are, expressly or by implication, concerned with an activity that would occur *within* the territory of the Member seeking to justify its measures. This position, according to Mexico, is supported by the Appellate Body's findings in *US—Shrimp (Article 21.5 – Malaysia)*.³²

17. Mexico further requests, in the event the Appellate Body should reverse the Panel's conclusion, that it complete the Panel's analysis and find that the Mexican measures are "necessary" within the meaning of Article XX(d) and meet the requirements of the chapeau of that Article. According to Mexico, the uncontested facts and evidence in the Panel record, and the Panel's acknowledgement that Mexico's measures have "attracted the attention" of the United States, provide an ample basis on which to complete the analysis and conclude that the measures are "necessary" within the meaning of Article XX(d).

18. Mexico observes that, before the Panel, the United States could not identify any alternative measure that Mexico could and should have used in order to attain its legitimate objective. It further explains that the fact that a measure does not or has not yet achieved its objective does not mean that it is not "necessary" within the meaning of Article XX(d). It may mean that it is insufficient to secure compliance, or that it is insufficient to secure immediate compliance, but can do so over time; however, it says nothing about whether the measure is "necessary". Moreover, Mexico submits that the evidence on the record demonstrates that the measures at issue have contributed to securing compliance in the circumstances of this case by changing the dynamics of the NAFTA dispute and forcing the United States to pay attention to Mexico's grievances, and also contradicts the Panel's finding that Mexico's measures do not contribute to securing compliance in this dispute.

19. As regards the chapeau of Article XX of the GATT 1994, Mexico asserts that its measures neither arbitrarily nor unjustifiably discriminate between countries where the same conditions prevail. Rather than constituting "arbitrary or unjustifiable discrimination", the measures constitute "limited

³²Mexico's appellant's submission, paras. 174 and 177-178 (referring to Appellate Body Report, *US—Shrimp (Article 21.5 – Malaysia)*, paras. 123-124 and 128-130).

sectoral retaliation in the relevant market segment (*i.e.*, the sweeteners market).³³ Nor can the measures be said to be a "disguised restriction on [international] trade" because they constitute "a proportionate, legitimate and legally justified response to actions and omissions of the United States"³⁴, and, furthermore, the measures have been published.

20. Finally, Mexico argues that the Panel, "separately and in addition"³⁵ to the previous errors, failed to make "an objective assessment of the facts", as required by Article 11 of the DSU, in finding that "Mexico has not established that its measures contribute to securing compliance in the circumstances of this case."³⁶ According to Mexico, the Panel's finding is based solely on the Panel's view that attracting the attention of the United States is not equivalent to securing compliance with a law or regulation and ignores that "achieving the objectives sought by the countermeasures can take time".³⁷

B. *Arguments of the United States – Appellee*

1. Exercise of Jurisdiction

21. The United States submits that the Panel properly rejected Mexico's request for the Panel to refrain from exercising jurisdiction in the present dispute.

22. Referring to Article 11 of the DSU, the United States observes that, if the Panel had declined to exercise jurisdiction over this dispute, or had agreed to Mexico's request that it refrain from issuing findings and recommendations, the Panel would have made no findings on the United States' claims that Mexico's tax measures are inconsistent with Article III of the GATT 1994. This would have left the DSB "unable to give any rulings or (as is appropriate in this dispute) to make any

³³Mexico's appellant's submission, para. 173 ("*retorsiones sectoriales limitadas al segmento del mercado relevante (i.e. el mercado de los edulcorantes)*"). Mexico asserts that the facts of this case are similar to the situation examined by the Appellate Body in *US – Shrimp (Article 21.5 – Malaysia)*. Mexico explains that, in that dispute, the Appellate Body found that a United States unilateral measure was not inconsistent with the chapeau of Article XX of the GATT 1994. According to Mexico, in that case, the Appellate Body did not require the United States to conclude an international agreement with the disputing parties, but rather required it to have made good faith efforts in that direction. In this case, Mexico argues that it has sought to resolve the dispute through NAFTA and bilateral negotiations, but "the United States has essentially blocked Mexico's ability to have its grievance resolved." (Mexico's appellant's submission, paras. 174-181 ("*Estados Unidos esencialmente ha bloqueado la posibilidad de México para resolver su agravio*"))

³⁴*Ibid.*, para. 182 ("*una respuesta proporcional, legítima y legalmente justificada a las acciones y omisiones de Estados Unidos*").

³⁵*Ibid.*, heading III.E ("*independiente y adicional*").

³⁶Panel Report, para. 8.186. See also, Mexico's Notice of Appeal, para. 3.

³⁷Mexico's appellant's submission, para. 166 ("*la consecución de los objetivos de las contramedidas puede llevar tiempo*").

recommendations"³⁸ in accordance with the rights and obligations under the DSU and the GATT 1994. The United States emphasizes that such a result is incompatible with the text of the DSU and would have required the Panel to disregard the mandate given to it by the DSB. Moreover, the United States observes that the Panel's own terms of reference in this dispute instructed the Panel to examine the matter referred to the DSB by the United States and to make such findings as will assist the DSB in making the recommendations and rulings provided for under the DSU.

23. Referring to Articles 3.2 and 19.2 of the DSU, the United States adds that, if a panel were to decline to exercise jurisdiction over a particular dispute, it would diminish the rights of the complaining Member under the DSU and other covered agreements. The United States further notes that prior reports of panels and the Appellate Body also support the Panel's findings. In this regard, the United States refers to *Mexico – Corn Syrup (Article 21.5 – US)*, where the Appellate Body stated that "panels are required to address issues that are put before them by the parties to a dispute."³⁹

24. The United States observes that Mexico has referred to the principle of judicial economy as an example of "situations where WTO panels have refrained from exercising validly established substantive jurisdiction on certain claims that are before them."⁴⁰ However, the United States submits that, "when a panel exercises judicial economy, it does not decline to exercise substantive jurisdiction either over a dispute or certain claims in a dispute. Rather, the panel ... declines to make findings on certain claims when resolution of such claims is not necessary for the panel to fulfill its mandate under Article 11 of the DSU and its terms of reference."⁴¹ In other words, judicial economy "does not relieve a panel from its duty to carry out its mandate under Articles 7 and 11 of the DSU to resolve the dispute"⁴² before it.

2. Article XX(d) of the GATT 1994

25. The United States submits that the Panel properly found that Mexico's tax measures are not designed "to secure compliance" and, thus, are not justified as measures "to secure compliance with laws or regulations" within the meaning of Article XX(d) of the GATT 1994. It notes that previous GATT and WTO disputes in which Article XX(d) has been invoked have involved domestic laws or regulations.

³⁸United States' appellee's submission, para. 124.

³⁹*Ibid.*, para. 127 (quoting Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 36).

⁴⁰*Ibid.*, para. 129 (quoting Mexico's appellant's submission, para. 68).

⁴¹*Ibid.* (referring to Appellate Body Report, *US – Wool Shirts and Blouses*, p. 19, DSR 1997:1, 323, at 340; and to Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 133).

⁴²*Ibid.*, para. 130.

26. The United States agrees with the Panel's analysis of the terms "laws or regulations" and, therefore, supports the Panel's finding that these terms refer only to *domestic* laws or regulations and not to obligations under international agreements. The United States explains that Article XX(d) refers to "laws" and "regulations" in the plural, while the singular "law" is used when referring to "international law".⁴³ The United States further observes that the terms "laws or regulations" precede the words "which are not inconsistent" in Article XX(d) and explains that the term "inconsistent" appears elsewhere in the GATT 1994 in connection with domestic measures. In contrast, the WTO agreements use the word "conflict" when referring to international obligations.

27. The United States further submits that Mexico's interpretation of the terms "laws or regulations" would undermine Articles 22 and 23 of the DSU, as it would permit action, including the suspension of concessions, by any Member "outside the rules of the DSU".⁴⁴ The United States observes that Article XX(d) was not intended to provide the basis for suspending concessions under the WTO agreements upon a mere allegation of a breach of a non-WTO international agreement. Otherwise, according to the United States, "this would effectively convert WTO dispute settlement into a forum of general dispute resolution for all international agreements."⁴⁵ Furthermore, the United States argues that, if the terms "laws or regulations" are read to include obligations under non-WTO agreements, the WTO dispute settlement system "would become a forum for WTO Members to allege and obtain findings as to the consistency of another Member's measure with any non-WTO agreement."⁴⁶ The United States, therefore, disagrees with Mexico's arguments that the phrase "laws or regulations" in Article XX(d) refers to international agreements.

28. With respect to the Panel's interpretation of the phrase "to secure compliance", the United States notes that the references to coercion were intended "merely [to] reinforce the Panel's view that 'enforcement' does not refer to the international level"⁴⁷ and not, as Mexico argues, to create an additional requirement for justifying a measure under Article XX(d). The United States therefore agrees with the Panel that the terms "to secure compliance" do not apply to measures taken by one Member to induce another Member to comply with obligations under a non-WTO treaty.

29. The United States also rejects Mexico's submission that the "Panel wrongly found that measures with an 'uncertain outcome' are *a priori* ineligible" as measures to secure compliance with

⁴³The United States observes that Article 3.2 of the DSU and Article 17.6 of the *Anti-Dumping Agreement* also use the term "law" in the singular when referring to "public international law".

⁴⁴United States' appellee's submission, para. 37.

⁴⁵*Ibid.*, para. 85. (footnote omitted)

⁴⁶*Ibid.*, para. 41.

⁴⁷*Ibid.*, para. 54 (referring to Panel Report, paras. 8.175 and 8.178).

laws or regulations."⁴⁸ While the United States concedes that the Panel's analysis "could have admittedly been clearer"⁴⁹, it also notes that the Panel did not require certainty, and argues that the Panel's remarks on this point simply characterized Mexico's failure to "put forth *any* evidence that its tax measures were designed to [secure] compliance."⁵⁰ The United States agrees with Mexico that "Article XX(d) does not require the party invoking the defense to establish that its measure will, without a doubt or with certainty, secure compliance with laws or regulations."⁵¹ Nevertheless, the United States submits that Mexico has to provide some evidence that the measure is "designed" to secure such compliance.

30. For all these reasons, the United States submits that the Appellate Body should uphold the Panel's conclusion that Mexico's tax measures are *not* designed to secure compliance and, thus, are *not* justified as measures "to secure compliance with laws or regulations" within the meaning of Article XX(d) of the GATT 1994.

31. In the event the Appellate Body should reverse the Panel's finding and accept Mexico's request to complete the analysis, the United States asserts that Mexico's measures are neither "necessary" for purposes of Article XX(d), nor do they meet the requirements of the chapeau of that Article. According to the United States, Mexico has not demonstrated that the measures at issue contribute to compliance by the United States with its NAFTA obligations and "ignores"⁵² the fact that the trade impact of a measure is one of the factors that must be weighed and balanced when determining whether a measure is "necessary". The impact of Mexico's measures was "essentially [to] prohibit the use of imported HFCS in Mexican soft drinks and other beverages and to reduce import volumes".⁵³ The United States adds that "[i]t is difficult to understand how discriminating against imports from potentially every WTO Member is 'necessary' to secure [the United States'] compliance with [its] obligations under the NAFTA."⁵⁴ The United States further observes that the absence of alternative measures that could be reasonably available does not, in itself, mean that the challenged measures are "necessary". In any event, the United States submits that if Mexico's objective was to attract the attention of the United States, it could have pursued a variety of other actions, including pursuing the diplomatic avenues available under the NAFTA.

⁴⁸United States' appellee's submission, para. 70 (quoting Mexico's appellant's submission, paras. 104-105).

⁴⁹*Ibid.*, para. 71.

⁵⁰*Ibid.* (original emphasis)

⁵¹*Ibid.*, para. 72. (footnote omitted)

⁵²*Ibid.*, para. 96.

⁵³*Ibid.*, para. 97.

⁵⁴*Ibid.*

32. The United States submits, furthermore, that Mexico's measures do not meet the requirements of the chapeau of Article XX of the GATT 1994. The only evidence that Mexico offers to support its contention that the measures do not constitute arbitrary or unjustifiable discrimination is the characterization of the measures as international countermeasures.⁵⁵ This is insufficient, argues the United States, for Mexico to meet its burden of proof. Moreover, the fact that Mexico may have been transparent about its measures is not sufficient to establish that such measures are not a "disguised restriction on trade".⁵⁶

33. Lastly, the United States requests the Appellate Body to reject Mexico's contention that the Panel did not make an objective assessment of the facts, as required by Article 11 of the DSU. According to the United States, the Panel did not "ignore" arguments or evidence submitted by Mexico. The United States further explains that, in any event, the errors alleged by Mexico in support of its claim under Article 11 of the DSU "relate to the interpretation of Article XX, and do not support a conclusion that the Panel breached Article 11."⁵⁷

C. *Arguments of the Third Participants*

1. China

34. Referring to Articles 7 and 11 of the DSU, China argues that a WTO panel does not have an implied power to refrain from performing its "statutory function".⁵⁸ China submits that, if a panel that is "empowered and obligated"⁵⁹ to assist the DSB in the settlement of a dispute declines to exercise jurisdiction, such a decision would create legal uncertainty and be contrary to the aim of providing security and predictability to the multilateral trading system as well as the prompt settlement of disputes as provided for in Article 3.3 of the DSU. China argues, moreover, that the notion of judicial economy is "relevant and applicable"⁶⁰ only if a panel has assumed the jurisdiction defined by its

⁵⁵According to the United States, the Appellate Body rulings in *US – Shrimp (Articles 21.5 – Malaysia)* do not support Mexico's position, because that dispute did not involve a disagreement about the commitments made under an international agreement. (United States' appellee's submission, paras. 109-110)

⁵⁶*Ibid.*, para. 114.

⁵⁷*Ibid.*, para. 118.

⁵⁸China's third participant's submission, para. 5.

⁵⁹*Ibid.*, para. 6.

⁶⁰*Ibid.*, para. 7.

terms of reference and has made "such findings as will assist the DSB" within the meaning of Article 11 of the DSU.

35. China asserts that the terms "laws or regulations" in Article XX(d) do not encompass international agreements. China states that Article X of the GATT 1994 provides contextual guidance for the interpretation of Article XX(d). Article X expressly distinguishes between "[l]aws, regulations, judicial decisions and administrative rulings" and "[a]greements ... between the government or a governmental agency of any Member and the government or governmental agency of any other Member". China adds that interpreting "laws or regulations" to include international agreements would allow a WTO Member to justify under Article XX(d) its deviation from its WTO obligations in the name of any remedial measure in response to any alleged breach of any non-WTO international agreement. Such a scenario, according to China, is not consistent with the object and purpose of the GATT 1994.

2. European Communities

36. The European Communities submits that the Appellate Body should uphold the Panel's finding that it did not have the discretion to decline to exercise jurisdiction in this case. The European Communities submits that "the functions and obligations of WTO Panels must be established on the basis of the DSU, and particularly Article 11 thereof."⁶¹ On this basis, the European Communities agrees that a panel has an inherent power to establish whether it has jurisdiction, and whether a particular matter is within its jurisdiction. However, the European Communities argues that a panel may not freely, or by "the notion of 'judicial economy'", decide to refrain from exercising its jurisdiction "in a case properly brought before it under the DSU."⁶²

37. The European Communities asserts, furthermore, that the Appellate Body should uphold the Panel's finding that only measures made applicable in the domestic legal order of a WTO Member constitute "laws or regulations" within the meaning of Article XX(d). The European Communities disagrees, however, with the Panel's finding that "international agreements, even when incorporated into the domestic law of a WTO Member, can never be regarded as 'laws or regulations' for the purposes of Article XX(d)".⁶³ In addition, the European Communities takes issue with the Panel's interpretation of the terms "to secure compliance" as requiring a degree of certainty in the results that may be achieved through the measure.

⁶¹European Communities' third participant's submission, para. 8.

⁶²*Ibid.*, paras. 10-11.

⁶³*Ibid.*, para. 44.

3. Japan

38. Japan disagrees with the Panel's interpretation of the terms "to secure compliance" in Article XX(d). In this regard, Japan submits that Article XX(d) does not necessarily exclude measures that have, as a purpose, to secure compliance, but are not accompanied by compulsory enforcement. According to Japan, compliance can be secured by a request or a command without being accompanied by any coercion. Japan considers that the Panel erred by indicating that the determination of whether a measure is designed "to secure compliance" should be analyzed based on the degree of certainty of its outcome. Nevertheless, Japan agrees with the Panel's finding that Article XX(d) does not cover international agreements. Japan explains that the terms "laws or regulations", read together with the phrase "to secure compliance", "presuppose a hierarchical structure that is associated with the relation between the state and its subjects"⁶⁴ and, therefore, excludes international agreements.

III. Issues Raised in This Appeal

39. The following issues are raised in this appeal:
- (a) whether the Panel erred in concluding that a WTO panel "has no discretion to decide whether or not to exercise its jurisdiction in a case properly before it"⁶⁵ and, if so, whether the Panel erred in declining to exercise that discretion in the circumstances of this dispute;
 - (b) whether the Panel erred in concluding that Mexico's measures do not constitute measures "to secure compliance with laws or regulations", within the meaning of Article XX(d) of the GATT 1994⁶⁶; and
 - (c) whether the Panel failed to make an objective assessment of the facts of the case, as required by Article 11 of the DSU, in concluding that "even if the assumption were to be made in the abstract that international countermeasures are potentially capable of qualifying as measures designed to secure compliance", within the meaning of Article XX(d) of the GATT 1994, "Mexico has not established that its measures contribute to securing compliance in the circumstances of this case."⁶⁷

⁶⁴Japan's third participant's submission, para. 22.

⁶⁵Panel Report, para. 7.18.

⁶⁶*Ibid.*, para. 8.198.

⁶⁷*Ibid.*, para. 8.186.

IV. The Panel's Exercise of JurisdictionA. *Introduction*

40. In its first written submission to the Panel, Mexico requested that the Panel decide, as a preliminary matter, to decline to exercise jurisdiction "in favour of an Arbitral Panel under Chapter Twenty of the North American Free Trade Agreement (NAFTA)."⁶⁸ In a preliminary ruling, the Panel rejected Mexico's request and found instead that, "under the DSU, it had no discretion to decide whether or not to exercise its jurisdiction in a case properly before it."⁶⁹ The Panel added that even if it had such discretion, it "did not consider that there were facts on record that would justify the Panel declining to exercise its jurisdiction in the present case."⁷⁰

41. In its reasoning, the Panel opined that "discretion may be said to exist only if a legal body has the freedom to choose among several options, all of them equally permissible in law."⁷¹ According to the Panel, "such freedom ... would exist within the framework of the DSU only if a complainant did not have a legal right to have a panel decide a case properly before it."⁷² Referring to Article 11 of the DSU and to the ruling of the Appellate Body in *Australia – Salmon*, the Panel observed that "the aim of the WTO dispute settlement system is to resolve the matter at issue in particular cases and to secure a positive solution to disputes" and that a panel is required "to address the claims on which a finding is necessary to enable the DSB to make sufficiently precise recommendations or rulings to the parties."⁷³ From this, the Panel concluded that a WTO panel "would seem therefore not to be in a position to choose freely whether or not to exercise its jurisdiction."⁷⁴ Referring to Articles 3.2 and 19.2 of the DSU, the Panel further stated that "[i]f a WTO panel were to decide not to exercise its jurisdiction in a particular case, it would diminish the rights of the complaining Member under the DSU and other WTO covered agreements."⁷⁵ The Panel added that Article 23 of the DSU "make[s] it clear that a WTO Member that considers that any of its WTO benefits have been nullified or impaired as a result of a measure adopted by another Member has the right to bring the case before the WTO dispute settlement system."⁷⁶

⁶⁸Panel Report, para. 7.1.

⁶⁹*Ibid.*

⁷⁰*Ibid.*

⁷¹*Ibid.*, para. 7.7.

⁷²*Ibid.*

⁷³*Ibid.*, para. 7.8 (referring to Appellate Body Report, *Australia – Salmon*, para. 223).

⁷⁴*Ibid.*

⁷⁵*Ibid.*, para. 7.9.

⁷⁶*Ibid.*

42. On appeal, Mexico contends that the Panel erred in rejecting Mexico's request that it decline to exercise jurisdiction in the circumstances of the present dispute. Mexico submits that WTO panels, like other international bodies and tribunals, "have certain implied jurisdictional powers that derive from their nature as adjudicative bodies."⁷⁷ Such powers include the power to refrain from exercising substantive jurisdiction in circumstances where "the underlying or predominant elements of a dispute derive from rules of international law under which claims cannot be judicially enforced in the WTO, such as the NAFTA provisions" or "when one of the disputing parties refuses to take the matter to the appropriate forum."⁷⁸ Mexico argues, in this regard, that the United States' claims under Article III of the GATT 1994 are inextricably linked to a broader dispute⁷⁹ regarding access of Mexican sugar to the United States' market under the NAFTA. Mexico further emphasizes that "[t]here is nothing in the DSU ... that explicitly rules out the existence of"⁸⁰ a WTO panel's power to decline to exercise validly established jurisdiction and submits that "the Panel should have exercised this power in the circumstances of this dispute."⁸¹

43. In contrast, the United States argues that, "[t]he Panel's own terms of reference in this dispute instructed the Panel 'to examine ... the matter referred to the DSB by the United States'"⁸² and "to make such findings as will assist the DSB" in making the recommendations and rulings provided for under the DSU. China and the European Communities agree with the United States that the Panel had no discretion to decline to exercise jurisdiction. China submits that if a panel declines to exercise jurisdiction over a dispute, such a decision will create legal uncertainty, contrary to the aim of providing security and predictability to the multilateral trading system and the prompt settlement of disputes as provided for in Article 3.3 of the DSU.⁸³ The European Communities agrees with the Panel's finding that it did not have discretion to decline to exercise jurisdiction in this case, and emphasizes that "the functions and obligations of WTO Panels must be established on the basis of the DSU, and particularly Article 11 thereof."⁸⁴

⁷⁷Mexico's appellant's submission, para. 65 ("*tienen ciertas facultades implícitas en relación con su competencia, las cuales derivan de su propia naturaleza como órganos jurisdiccionales*").

⁷⁸*Ibid.*, para. 73 ("*los elementos predominantes de una disputa derivan de reglas del derecho internacional, cuyo cumplimiento no puede reclamarse en el marco OMC, por ejemplo las disposiciones del TLCAN*"; "*cuanado una de las partes contendientes se rehúsa a someterse al foro adecuado*").

⁷⁹*Ibid.*

⁸⁰*Ibid.*, para. 65 ("*Nada en el ESD ... explícitamente descarta que ... existan*").

⁸¹*Ibid.*, para. 72 ("*el Grupo Especial debió haber ejercido esa facultad en las circunstancias de esta disputa*").

⁸²United States' appellee's submission, para. 125.

⁸³China's third participant's submission, para. 6.

⁸⁴European Communities' third participant's submission, para. 8.

B. Analysis

44. Before addressing Mexico's arguments, we note that "Mexico does not question that the Panel has jurisdiction to hear the United States' claims."⁸⁵ Moreover, Mexico does not claim "that there are legal obligations under the NAFTA or any other international agreement to which Mexico and the United States are both parties, which might raise legal impediments to the Panel hearing this case".⁸⁶ Instead, Mexico's position is that, although the Panel had the authority to rule on the merits of the United States' claims, it also had the "implied power" to abstain from ruling on them⁸⁷, and "should have exercised this power in the circumstances of this dispute."⁸⁸ Hence, the issue before us in this appeal is not whether the Panel was legally precluded from ruling on the United States' claims that were before it, but, rather, whether the Panel could decline, and should have declined, to exercise jurisdiction with respect to the United States' claims under Article III of the GATT 1994 that were before it.

45. Turning to Mexico's arguments on appeal, we note, first, Mexico's argument that WTO panels, like other international bodies and tribunals, "have certain implied jurisdictional powers that derive from their nature as adjudicative bodies"⁸⁹, and thus have a basis for declining to exercise jurisdiction. We agree with Mexico that WTO panels have certain powers that are inherent in their jurisdiction. Mexico's appellant's submission, para. 71 ("*México no discute que el Grupo Especial tiene competencia para resolver la reclamación que Estados Unidos ha interpuesto*") (quoting Mexico's response to questioning 35 posed by the Panel; Panel Report, p. C-16). Mexico confirmed this point in response to questioning at the oral hearing.

⁸⁵Panel Report, para. 7.13. In response to questioning at the oral hearing, Mexico argued that the panel in *Argentina – Poultry Anti-Dumping Duties* "at least contemplated the existence of a situation where an impediment found in another agreement might give rise to declining jurisdiction". The panel in *Argentina – Poultry Anti-Dumping Duties* referred to Article 1 of the Protocol of Olivos, which provides that, once a party decides to bring a case under either the MERCOSUR or WTO dispute settlement forum, that party may not bring a subsequent case regarding the same subject-matter in the other forum, and went on to state:

The Protocol of Olivos ... does not change our assessment, since that Protocol has not yet entered into force, and in any event it does not apply in respect of disputes already decided in accordance with the MERCOSUR Protocol of Brasilia. Indeed, the fact that parties to MERCOSUR need to introduce the Protocol of Olivos suggests to us that they recognised that (in the absence of such Protocol) a MERCOSUR dispute settlement proceeding could be followed by a WTO dispute settlement proceeding in respect of the same measure.

(Panel Report, *Argentina – Poultry Anti-Dumping Duties*, para. 7.38) (footnote omitted)

⁸⁷Thus, Mexico suggested that, in the circumstances of this dispute, it would not have been "appropriate" for the Panel "to issue findings on the merits of the United States' claims." (Panel Report, para. 7.11 (referring to Mexico's first written submission to the Panel, paras. 102-103))

⁸⁸Mexico's appellant's submission, para. 72 ("*debió haber ejercido esa facultad en las circunstancias de esta disputa*").

⁸⁹*Ibid.*, para. 65 ("*tienen ciertas facultades implícitas en relación con su competencia, las cuales derivan de su propia naturaleza como órganos jurisdiccionales*").

adjudicative function. Notably, panels have the right to determine whether they have jurisdiction in a given case, as well as to determine the scope of their jurisdiction. In this regard, the Appellate Body has previously stated that "it is a widely accepted rule that an international tribunal is entitled to consider the issue of its own jurisdiction on its own initiative, and to satisfy itself that it has jurisdiction in any case that comes before it."⁹⁰ Further, the Appellate Body has also explained that panels have "a margin of discretion to deal, always in accordance with due process, with specific situations that may arise in a particular case and that are not explicitly regulated."⁹¹ For example, panels may exercise judicial economy, that is, refrain from ruling on certain claims, when such rulings are not necessary "to resolve the matter in issue in the dispute".⁹² The Appellate Body has cautioned, nevertheless, that "[t]o provide only a partial resolution of the matter at issue would be false judicial economy."⁹³

46. In our view, it does not necessarily follow, however, from the existence of these inherent adjudicative powers that, once jurisdiction has been validly established, WTO panels would have the authority to decline to rule on the entirety of the claims that are before them in a dispute. To the contrary, we note that, while recognizing WTO panels' inherent powers, the Appellate Body has previously emphasized that:

⁹⁰Appellate Body Report, *US – 1916 Act*, footnote 30 to para. 54. See also Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 53. In that dispute, the Appellate Body also stated that:

... panels have to address and dispose of certain issues of a fundamental nature, even if the parties to the dispute remain silent on those issues. ... [P]anels cannot simply ignore issues which go to the root of their jurisdiction—that is, to their authority to deal with and dispose of matters. Rather, panels must deal with such issues—if necessary, on their own motion—in order to satisfy themselves that they have authority to proceed. (Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 36)

⁹¹Appellate Body Report, *EC – Hormones*, footnote 138 to para. 152. See also Appellate Body Report, *US – FSC (Article 21.5 – EC)*, paras. 247-248.

⁹²Appellate Body Report, *US – Wool Shirts and Blouses*, p. 19, DSR 1997:1, 323, at 340. Mexico referred, in its appellant's submission, to a panel's discretion to apply judicial economy as "an example of situations where WTO panels have refrained from exercising validly established jurisdiction on certain claims that are before them." (Mexico's appellant's submission, para. 68 ("*un ejemplo de situaciones en las que grupos especiales de la OMC se han abstenido de resolver ciertas reclamaciones sobre las cuales tienen competencia sustantiva válidamente establecida*")) Mexico clarified at the oral hearing, however, that "it is clear that in the context of the exercise of judicial economy a panel cannot decline entirely to exercise jurisdiction." The United States noted, in this regard, that the doctrine of judicial economy "does not relieve a panel from its duty to carry out its mandate under Articles 7 and 11 of the DSU to resolve the dispute" before it. (United States' appellee's submission, para. 130)

⁹³Appellate Body Report, *Australia – Salmon*, para. 223.

Although panels enjoy some discretion in establishing their own working procedures, *this discretion does not extend to modifying the substantive provisions of the DSU. ... Nothing in the DSU gives a panel the authority either to disregard or to modify ... explicit provisions of the DSU.*⁹⁴ (emphasis added)

47. With these considerations in mind, we examine the scope of a panel's jurisdictional power as defined, in particular, in Articles 3.2, 7.1, 7.2, 11, 19.2, and 23 of the DSU. Mexico argues that "[t]here is nothing in the DSU ... that explicitly rules out the existence of"⁹⁵ a WTO panel's power to decline to exercise its jurisdiction even in a case that is properly before it.

48. We first address Article 7 of the DSU, which governs the terms of reference of panels. Article 7 of the DSU states, in its first paragraph, that panels shall have the following terms of reference:

"To examine, in the light of the relevant provisions in (name of the covered agreement(s) cited by the parties to the dispute), the matter referred to the DSB by (name of party) in document ... and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in that/those agreement(s)."

The Panel in this dispute was established with standard terms of reference⁹⁶, which instructed the Panel to "examine" the United States' claims that were before it and to "make findings" with respect to consistency of the measures at issue with Article III of the GATT 1994.

49. The second paragraph of Article 7 further stipulates that "[p]anels shall address the relevant provisions in any covered agreement or agreements cited by the parties to the dispute." The use of the words "shall address" in Article 7.2 indicates, in our view, that panels are required to address the relevant provisions in any covered agreement or agreements cited by the parties to the dispute.⁹⁷

⁹⁴Appellate Body Report, *India – Patents (US)*, para. 92.

⁹⁵Mexico's appellant's submission, para. 65 ("*Nada en el ESD ... explícitamente descarta que ... existan*").

⁹⁶The Panel's terms of reference in this dispute were as follows:

To examine, in the light of the relevant provisions of the covered agreements cited by the United States in document WT/DS308/4, the matter referred to the DSB by the United States in that document, and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements.

(WT/DS308/5/Rev.1, para. 2)

⁹⁷In this regard, we further note the Appellate Body's statement that, "as a matter of due process, and the proper exercise of the judicial function, panels are required to address issues that are put before them by the parties to a dispute." (Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 36)

50. We turn next to Article 11 of the DSU, which provides that:

The function of panels is to assist the DSB in discharging its responsibilities under this Understanding and the covered agreements. Accordingly, a panel should make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements, and make such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the covered agreements. . . .

51. Article 11 of the DSU states that panels *should* make an objective assessment of the matter before them. The Appellate Body has previously held that the word "should" can be used not only "to imply an exhortation, or to state a preference", but also "to express a duty [or] obligation".⁹⁸ The Appellate Body has repeatedly ruled that a panel would not fulfil its mandate if it were not to make an objective assessment of the matter.⁹⁹ Under Article 11 of the DSU, a panel is, therefore, charged with the *obligation* to "make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements." Article 11 also requires that a panel "make such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the covered agreements." It is difficult to see how a panel would fulfil that obligation if it declined to exercise validly established jurisdiction and abstained from making any finding on the matter before it.

52. Furthermore, Article 23 of the DSU states that Members of the WTO *shall* have recourse to the rules and procedures of the DSU when they "seek the redress of a violation of obligations ... under the covered agreements". As the Appellate Body has previously explained, "allowing measures to be the subject of dispute settlement proceedings ... is consistent with the comprehensive nature of the right of Members to resort to dispute settlement to 'preserve [their] rights and obligations ... under the covered agreements, and to clarify the existing provisions of those agreements'."¹⁰⁰ We also note in this regard that Article 3.3 of the DSU provides that the "prompt settlement of situations in which a Member considers that any benefits accruing to it directly or indirectly under the covered agreements are being impaired by measures taken by another Member is essential to the effective

⁹⁸Appellate Body Report, *Canada – Aircraft*, para. 187 (quoting *The Concise Oxford English Dictionary* (Clarendon Press, 1995), p. 1283).

⁹⁹See, for instance, Appellate Body Report, *EC – Export Subsidies on Sugar*, paras. 329 and 335. See also Appellate Body Report, *Canada – Aircraft*, paras. 187-188; and Appellate Body Report, *EC – Hormones*, para. 133.

¹⁰⁰Appellate Body Report, *US – Corrosion-Resistant Steel Sunset Review*, para. 89. (footnote omitted)

functioning of the WTO".¹⁰¹ The fact that a Member may initiate a WTO dispute whenever it considers that "any benefits accruing to [that Member] are being impaired by measures taken by another Member" implies that that Member is *entitled* to a ruling by a WTO panel.

53. A decision by a panel to decline to exercise validly established jurisdiction would seem to "diminish" the right of a complaining Member to "seek the redress of a violation of obligations" within the meaning of Article 23 of the DSU, and to bring a dispute pursuant to Article 3.3 of the DSU. This would not be consistent with a panel's obligations under Articles 3.2 and 19.2 of the DSU.¹⁰² We see no reason, therefore, to disagree with the Panel's statement that a WTO panel "would seem ... not to be in a position to choose freely whether or not to exercise its jurisdiction."¹⁰³

54. Mindful of the precise scope of Mexico's appeal¹⁰⁴, we express no view as to whether there may be other circumstances in which legal impediments could exist that would preclude a panel from ruling on the merits of the claims that are before it. In the present case, Mexico argues that the United States' claims under Article III of the GATT 1994 are inextricably linked to a broader dispute¹⁰⁵, and

¹⁰¹(emphasis added) Thus, the Appellate Body has explained that there is "little in the DSU that explicitly limits the rights of WTO Members to bring an action". (Appellate Body Report, *EC – Export Subsidies on Sugar*, para. 312) In a similar vein, the Appellate Body has also observed that a WTO "Member has broad discretion in deciding whether to bring a case against another Member under the DSU." (Appellate Body Report, *EC – Bananas III*, para. 135) Further, Article 3.7 of the DSU states that "[b]efore bringing a case, a Member shall exercise its *judgment* as to whether action under these procedures would be fruitful." (emphasis added) Finally, Article 3.10 of the DSU stipulates that "if a dispute arises, *all Members will engage* in these procedures *in good faith in an effort to resolve the dispute*." (emphasis added)

¹⁰²Article 3.2 of the DSU provides that "[r]ecommendations and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements."

Article 19.2 of the DSU states that "[i]n accordance with paragraph 2 of Article 3, in their findings and recommendations, the panel and Appellate Body cannot add to or diminish the rights and obligations provided in the covered agreements."

¹⁰³Panel Report, para. 7.8.

¹⁰⁴See *supra*, para. 44 and footnote 85 thereto.

¹⁰⁵Mexico's appellant's submission, para. 73.

that only a NAFTA panel could resolve the dispute as a whole.¹⁰⁶ Nevertheless, Mexico does not take issue with the Panel's finding that "neither the subject matter nor the respective positions of the parties are identical in the dispute under the NAFTA ... and the dispute before us."¹⁰⁷ Mexico also stated that it could not identify a legal basis that would allow it to raise, in a WTO dispute settlement proceeding, the market access claims it is pursuing under the NAFTA.¹⁰⁸ It is furthermore undisputed that no NAFTA panel as yet has decided the "broader dispute" to which Mexico has alluded. Finally, we note that Mexico has expressly stated that the so-called "exclusion clause" of Article 2005.6 of the NAFTA¹⁰⁹ had not been "exercised".¹¹⁰ We do not express any view on whether a legal impediment

¹⁰⁶In its appellant's submission, Mexico explains that, in 1998, it initiated NAFTA dispute settlement proceedings because it was of the view that the United States was acting inconsistently with its obligation under the NAFTA relating to market access for Mexican sugar to the United States market. In 2000, Mexico requested the establishment of a panel under Article 2008 of the NAFTA. Subsequently, according to Mexico, it appointed its panelists to the NAFTA panel; however, the United States failed to appoint its panelists and also instructed the United States' Section of the NAFTA Secretariat not to appoint panelists. (Mexico's appellant's submission, paras. 15-27)

As a result, "[n]o further step could be taken by Mexico to form the NAFTA panel and have its grievance heard." (Mexico's appellant's submission, para. 28 ("No había otros pasos que México pudiera dar conforme a las disposiciones del tratado para conseguir integrar el panel y que su agravio fuera oído")) Mexico explains that it subsequently adopted the measures at issue in this dispute "to compel the United States to comply with its obligations and [to] protect [Mexico's] own legal and commercial interests." (*Ibid.*, para. 42 ("para mover a Estados Unidos a cumplir con sus obligaciones, a la vez que protegí [los] legítimos intereses jurídicos y comerciales [de México]"))

The United States disputes these arguments by Mexico and argues that "the Appellate Body [should not] undertake itself to assess the correctness of Mexico's assertions as to what the NAFTA requires." (United States' appellee's submission, para. 18) It submits that, if the WTO dispute settlement were to "become a forum for WTO Members to ... obtain findings as to the consistency of another Member's measure with any non-WTO agreement", this "would be a departure from the function the WTO dispute settlement system was established to serve". (*Ibid.*, para. 41) The United States also submits that "it is in full compliance with its obligations under NAFTA's dispute settlement mechanism." (*Ibid.*, para. 84)

While these NAFTA issues have been described by the parties by way of background to the WTO dispute, neither the Panel or the Appellate Body was called upon to examine these issues.

¹⁰⁷Panel Report, para. 7.14. The Panel noted, in this regard, that:

[I]n the present case, the complaining party is the United States and the measures in dispute are allegedly imposed by Mexico. In the NAFTA case, the situation appears to be the reverse: the complaining party is Mexico and the measures in dispute are allegedly imposed by the United States. As for the subject matter of the claims, in the present case the United States is alleging discriminatory treatment against its products resulting from internal taxes and other internal measures imposed by Mexico. In the NAFTA case, instead, Mexico is arguing that the United States is violating its market access commitments under the NAFTA.

¹⁰⁸Mexico's response to questioning at the oral hearing.

¹⁰⁹Article 2005.6 of the NAFTA provides:

Once dispute settlement procedures have been initiated under Article 2007 or dispute settlement proceedings have been initiated under the GATT, the forum selected shall be used to the exclusion of the other, unless a Party makes a request pursuant to paragraph 3 or 4. (emphasis added)

¹¹⁰Mexico's response to questioning at the oral hearing.

to the exercise of a panel's jurisdiction would exist in the event that features such as those mentioned above were present.¹¹¹ In any event, we see no legal impediments applicable in this case.

55. Finally, as we understand it, Mexico's position is that the "applicability" of its WTO obligations towards the United States would be "call[ed] into question"¹¹² as a result of the United States having prevented Mexico, by an illegal act (namely, the alleged refusal by the United States to nominate panelists to the NAFTA panel), from having recourse to the NAFTA dispute settlement mechanism to resolve a bilateral dispute between Mexico and the United States regarding trade in sweeteners.¹¹³ Specifically, Mexico refers to the ruling of the Permanent Court of International Justice (the "PCIJ") in the *Factory at Chorzów* case, and "calls into question the 'applicability' of its WTO obligations towards the United States in the context of this dispute".¹¹⁴

56. Mexico's arguments, as well as its reliance on the ruling in *Factory at Chorzów*, is misplaced. Even assuming, *arguendo*, that the legal principle reflected in the passage referred to by Mexico is applicable within the WTO dispute settlement system, we note that this would entail a determination whether the United States has acted consistently or inconsistently with its NAFTA obligations.¹¹⁵ We see no basis in the DSU for panels and the Appellate Body to adjudicate non-WTO disputes. Article 3.2 of the DSU states that the WTO dispute settlement system "serves to preserve the rights and obligations of Members under the covered agreements, and to clarify the existing provisions of those agreements". (emphasis added) Accepting Mexico's interpretation would imply that the WTO dispute settlement system could be used to determine rights and obligations outside the covered agreements. In light of the above, we do not see how the PCIJ's ruling in *Factory at Chorzów* supports Mexico's position in this case.

¹¹¹In this context, Mexico has alluded to paragraph 7.38 of the Panel Report in *Argentina – Poultry Anti-Dumping Duties*. See also *supra*, footnote 86.

¹¹²Mexico's appellant's submission, para. 73 ("*[e]s] cuestion[able]*").

¹¹³See Panel Report, para. 7.14.

¹¹⁴Mexico's appellant's submission, para. 73 ("*cuestiona que sus obligaciones sean aplicables frente a Estados Unidos a la luz del siguiente principio general del derecho internacional*"). The passage of the ruling that Mexico refers to reads as follows:

... one party cannot avail himself of the fact that the other has not fulfilled some obligation, or has not had recourse to some means of redress, if the former party has, by some illegal act, prevented the latter from fulfilling the obligation in question, or from having recourse to the tribunal which would have been open to him.

(Permanent Court of International Justice, *Factory at Chorzów (Germany v. Poland)* (Jurisdiction), 1927, PCIJ Series A, No. 9, p. 31) (underlining added by Mexico omitted)

¹¹⁵We also note that the ruling of the PCIJ in the *Factory at Chorzów* case relied on by Mexico was made in a situation in which the party objecting to the exercise of jurisdiction by the PCIJ was the party that had committed the act alleged to be illegal. In the present case, the party objecting to the exercise of jurisdiction by the Panel (Mexico) relies instead on an allegedly illegal act committed by the other party (the United States).

57. For all these reasons, we *uphold* the Panel's conclusion, in paragraphs 7.1, 7.18, and 9.1 of the Panel Report, that "under the DSU, it ha[d] no discretion to decline to exercise its jurisdiction in the case that ha[d] been brought before it." Having upheld this conclusion, we *find* it unnecessary to rule in the circumstances of this appeal on the propriety of exercising such discretion.¹¹⁶

V. Article XX(d) of the GATT 1994

A. Introduction

58. We turn now to Mexico's claim that the Panel erred in finding that the challenged measures are not justified under Article XX(d) of the GATT 1994. Before proceeding, we note that Mexico has not appealed the Panel's conclusion that the challenged measures are inconsistent with Article III of the GATT 1994.¹¹⁷

59. Mexico argued before the Panel that its "measures are 'necessary to secure compliance' by the United States with the United States' obligations under the NAFTA, an international agreement that is a law not inconsistent with the provisions of the GATT 1994."¹¹⁸ The United States responded that "the NAFTA is not a 'law or regulation,' and Mexico's taxes are not 'necessary to secure compliance.'"¹¹⁹

60. The Panel began its analysis by looking at the meaning of the terms "to secure compliance". According to the Panel, "to secure compliance" means "to *enforce* compliance".¹²⁰ The Panel noted that "the notion of enforcement contains a concept of action within a hierarchical structure that is associated with the relation between the state and its subjects".¹²¹ It further observed that Article XX(d) "is concerned with action at a domestic rather than international level."¹²² Based on this reasoning, the Panel concluded that "the phrase 'to secure compliance' in Article XX(d) does not apply to measures taken by a Member in order to induce another Member to comply with obligations owed to it under a non-WTO treaty."¹²³

¹¹⁶Panel Report, paras. 7.1 and 7.18.

¹¹⁷Therefore, we express no view on the Panel's interpretation of Article III in this case.

¹¹⁸Panel Report, para. 8.162 (referring to Mexico's first written submission to the Panel, paras. 117-118 and 125).

¹¹⁹*Ibid.*, para. 8.163.

¹²⁰*Ibid.*, para. 8.175. (emphasis added)

¹²¹*Ibid.*, para. 8.178.

¹²²*Ibid.*, para. 8.179.

¹²³*Ibid.*, para. 8.181.

61. Having interpreted the terms "to secure compliance", the Panel proceeded to examine whether Mexico's measures are designed to secure compliance. The Panel explained that "when enforcement action is taken within a Member's legal system there will normally be no doubt, provided the action is pointed at the right target, that it will achieve that target."¹²⁴ In contrast, "the outcome of international countermeasures, such as those adopted by Mexico, is inherently unpredictable".¹²⁵ Therefore, the Panel reasoned, international countermeasures are "not eligible to be considered as measures 'to secure compliance' within the meaning of Article XX(d)."¹²⁶ The Panel added that "even if the assumption were to be made in the abstract that international countermeasures are potentially capable of qualifying as measures designed to secure compliance, the Panel's conclusion would be that Mexico has not established that its measures contribute to securing compliance in the circumstances of this case."¹²⁷ Thus, the Panel rejected Mexico's argument that "the challenged tax measures are *designed* to secure compliance by the United States with laws or regulations."¹²⁸

62. The Panel then examined whether the challenged measures would fall within the meaning of the terms "laws or regulations" in Article XX(d). The Panel underscored the link between the terms "to secure compliance" and the terms "laws and regulations" as set out in Article XX(d). It indicated that the same reasoning that applies in determining whether Mexico's measures are measures "to secure compliance" must also apply in determining whether the measures are "laws or regulations" within the meaning of Article XX(d).¹²⁹ In the Panel's view, "the conclusion that these words refer to enforcement action within a particular domestic legal system, and that they do not extend to international action of the type taken by Mexico, necessarily applies to both parts of this expression."¹³⁰ The Panel further observed that, "even if it were to assume that the expression 'laws or regulations' in Article XX(d) could include international agreements such as the NAFTA, it would in any event conclude that, on the facts of the case, because of the uncertainty of their consequences, the challenged measures are not designed 'to secure compliance with laws or regulations which are not inconsistent with the provisions' of GATT 1994."¹³¹

63. Therefore, the Panel concluded that "Mexico has not demonstrated that the challenged measures are designed 'to secure compliance with laws or regulations', within the meaning of

¹²⁴Panel Report, para. 8.185.

¹²⁵*Ibid.*, para. 8.186.

¹²⁶*Ibid.*

¹²⁷*Ibid.*

¹²⁸*Ibid.*, para. 8.190. (original emphasis)

¹²⁹*Ibid.*, para. 8.194.

¹³⁰*Ibid.*

¹³¹*Ibid.*, para. 8.197.

Article XX(d) of the GATT 1994.¹³² Having made this finding, the Panel did not consider that it needed to examine whether Mexico's measures are "necessary" within the meaning of Article XX(d)¹³³, and whether the measures satisfy the requirements set out in the chapeau of Article XX.¹³⁴ Consequently, the Panel concluded that "Mexico has not established that the challenged measures are justified under Article XX of the GATT 1994."¹³⁵

64. On appeal, Mexico seeks review of the Panel's conclusion that Mexico's measures are not justified under Article XX(d) of the GATT 1994. According to Mexico, the Panel incorrectly interpreted the terms "to secure compliance" as excluding international countermeasures¹³⁶, and this error led the Panel to incorrectly interpret the terms "laws or regulations" in Article XX(d).¹³⁷ Mexico argues that the terms "laws or regulations" are "broad enough to include international agreements such as the NAFTA."¹³⁸ Mexico points out that "the use of the terms 'laws' and 'regulations' elsewhere in the GATT 1994 and in other WTO agreements does not demonstrate that such terms exclude international law rules."¹³⁹

65. The United States responds that the Panel properly found that Mexico's measures are not justified under Article XX(d). It asserts that "the ordinary meaning of 'laws' and 'regulations' is that these are rules (e.g., in the form of a statute) issued by a government and not obligations under an international agreement."¹⁴⁰ The United States further explains that Mexico's interpretation of Article XX(d) is in conflict with Article 23 of the DSU, by allowing a WTO Member to take action outside the rules of the DSU to secure compliance with another Member's obligations under any international agreement, including the WTO agreements.¹⁴¹ It would also undermine Article 22 of the DSU by "permitt[ing] the suspension of concessions ... without DSB authorization and without any requirement to adhere to the rules established" in that provision.¹⁴²

¹³²Panel Report, para. 8.198.

¹³³*Ibid.*, para. 8.202.

¹³⁴*Ibid.*, para. 8.203.

¹³⁵*Ibid.*, para. 8.204.

¹³⁶Mexico's appellant's submission, para. 79 and footnote 49 thereto.

¹³⁷*Ibid.*, para. 126.

¹³⁸*Ibid.*, para. 129 ("suficientemente amplia para incluir tratados internacionales, como el TLCAN").

¹³⁹*Ibid.* ("el empleo de los términos 'leyes' y 'reglamentos' en el resto del GATT de 1994 y en otros Acuerdos de la OMC no demuestran que los tales términos excluyen las reglas del derecho internacional") (footnote omitted).

¹⁴⁰United States' appellee's submission, para. 30 (referring to definitions in *Black's Law Dictionary*, (1990), p. 816).

¹⁴¹*Ibid.*, para. 37.

¹⁴²*Ibid.*, para. 38. (footnote omitted)

B. Analysis

1. Are Mexico's Measures Justified under Article XX(d)?

66. Article XX(d) of the GATT 1994 reads:

General Exceptions

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:

...

(d) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including those relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the protection of patents, trade marks and copyrights, and the prevention of deceptive practices[.]

67. The Appellate Body explained, in *Korea – Various Measures on Beef*, that two elements must be shown "[f]or a measure, otherwise inconsistent with GATT 1994, to be justified provisionally under paragraph (d) of Article XX"¹⁴³. The first element is that "the measure must be one designed to 'secure compliance' with laws or regulations that are not themselves inconsistent with some provision of the GATT 1994", and the second is that "the measure must be 'necessary' to secure such compliance."¹⁴⁴ The Appellate Body also explained that "[a] Member who invokes Article XX(d) as a justification has the burden of demonstrating that these two requirements are met."¹⁴⁵

68. In our view, the central issue raised in this appeal is whether the terms "to secure compliance with laws or regulations" in Article XX(d) of the GATT 1994 encompass WTO-inconsistent measures applied by a WTO Member to secure compliance with another WTO Member's obligations under an international agreement.

¹⁴³Appellate Body Report, *Korea – Various Measures on Beef*, para. 157.

¹⁴⁴*Ibid.*

¹⁴⁵*Ibid.* (referring to Appellate Body Report, *US – Gasoline*, pp. 22-23, DSR 1996:1, 3, at 20-21; Appellate Body Report, *US – Wool Shirts and Blouses*, pp. 14-16, DSR 1997:1, 323, at 335-337; and GATT Panel Report, *US – Section 337*, para. 5.27).

69. In order to answer this question, we consider it more helpful to begin our analysis with the terms "laws or regulations" in Article XX(d) (which we consider to be pivotal here) rather than to begin with the analysis of the terms "to secure compliance", as did the Panel. The terms "laws or regulations" are generally used to refer to domestic laws or regulations. As Mexico and the United States note, previous GATT and WTO disputes in which Article XX(d) has been invoked as a defence have involved domestic measures.¹⁴⁶ Neither disputes that the expression "laws or regulations" encompasses the rules adopted by a WTO Member's legislative or executive branches of government. We agree with the United States that one does not immediately think about international law when confronted with the term "laws" in the plural.¹⁴⁷ Domestic legislative or regulatory acts sometimes may be intended to implement an international agreement. In such situations, the origin of the rule is international, but the implementing instrument is a domestic law or regulation.¹⁴⁸ In our view, the terms "laws or regulations" refer to rules that form part of the domestic legal system of a WTO Member.¹⁴⁹ Thus, the "laws or regulations" with which the Member invoking Article XX(d) may seek to secure compliance do not include obligations of *another* WTO Member under an international agreement.

70. The illustrative list of "laws or regulations" provided in Article XX(d) supports the conclusion that these terms refer to rules that form part of the domestic legal system of a WTO Member.¹⁵⁰ This list includes "[laws or regulations] relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the protection of patents, trade marks and copyrights, and the prevention of deceptive practices". These matters are typically the subject of domestic laws or regulations, even though some of these matters may also be the subject of

¹⁴⁶United States' appellee's submission, footnote 62 to para. 39; Mexico's response to questioning at the oral hearing.

¹⁴⁷Panel Report, footnote 419 to para. 8.193; United States' appellee's submission, para. 31.

¹⁴⁸In some WTO Members, certain international rules may have direct effect within their domestic legal systems without requiring implementing legislation. In such circumstances, these rules also become part of the domestic law of that Member.

¹⁴⁹The European Communities notes that:

[i]t is entirely possible that international agreements may be incorporated into the domestic legal order in such a way that they can be invoked as against individuals, and enforce[d] against them. If this is the case, the international agreement, albeit international in origin, may be regarded as having become an integral part of the domestic legal order of such Member, and thus a law or regulation within the meaning of Article XX (d) [of the] GATT [1994].

(European Communities' third participant's submission, para. 41)

¹⁵⁰The participants agree that the list in Article XX(d) is not exhaustive. (See Mexico's response to Question 67 posed by the Panel after the second Panel meeting; Panel Report, p. C-61; United States' response to Question 31 posed by the Panel after the first Panel meeting; Panel Report, p. C-42; and United States' response to Question 67 posed by the Panel after the second Panel meeting; Panel Report, pp. C-79-C-80)

international agreements. The matters listed as examples in Article XX(d) involve the regulation by a government of activity undertaken by a variety of economic actors (e.g., private firms and State enterprises), as well as by government agencies. For example, matters "relating to customs enforcement" will generally involve rights and obligations that apply to importers or exporters, and matters relating to "the protection of patents, trade marks and copyrights" will usually regulate the use of these rights by the intellectual property right holders and other private actors.¹⁵¹ Thus, the illustrative list reinforces the notion that the terms "laws or regulations" refer to rules that form part of the domestic legal system of a WTO Member and do not extend to the international obligations of another WTO Member.¹⁵²

71. Our understanding of the terms "laws or regulations" is consistent with the context of Article XX(d). As the United States points out¹⁵³, other provisions of the covered agreements refer expressly to "international obligations" or "international agreements". For example, paragraph (h) of Article XX refers to "obligations under any intergovernmental commodity agreement". The express language of paragraph (h) would seem to contradict Mexico's suggestion that international agreements are implicitly included in the terms "laws or regulations".¹⁵⁴ The United States and China also draw our attention to Article X:1 of the GATT 1994¹⁵⁵, which refers to "[l]aws, regulations, judicial decisions and administrative rulings" and to "[a]greements affecting international trade policy which are in force between a government ... of any Member and the government ... of any other Member". Thus, a distinction is drawn in the same provision between "laws [and] regulations" and "international agreements". Such a distinction would have been unnecessary if, as Mexico argues, the terms "laws" and "regulations" were to encompass international agreements that have not been incorporated, or do not have direct effect in, the domestic legal system of the respective WTO Member. Thus, Articles X:1 and XX(h) of the GATT 1994 do not lend support to interpreting the terms "laws or

¹⁵¹European Communities' third participant's submission, para. 38.

¹⁵²The United States also points out that the terms "laws or regulations" are qualified by the requirement that they not be "inconsistent" with the GATT 1994. The United States explains that the word "inconsistent" appears elsewhere in the GATT 1994 in connection with domestic measures. In contrast, when referring to treaty obligations, the WTO agreements use the word "conflict". (United States' appellee's submission, para. 33) In our view, this distinction supports the position that the terms "laws or regulations" refer to the rules that are part of the domestic legal system of a WTO Member, including international rules that have been incorporated or have direct effect in a particular domestic legal system.

¹⁵³United States' appellee's submission, para. 34.

¹⁵⁴If an international commodity agreement contains GATT-inconsistent provisions, Article XX(h) would still serve the purpose of justifying such an agreement, even if it could not be justified under Article XX(d).

¹⁵⁵United States' appellee's submission, para. 35; China's third participant's submission, para. 21.

regulations" in Article XX(d) as including the international obligations of a Member other than that invoking the provision.¹⁵⁶

72. We turn to the terms "to secure compliance", which were the focus of the Panel's reasoning and are the focus of Mexico's appeal. The terms "to secure compliance" speak to the types of measures that a WTO Member can seek to justify under Article XX(d). They relate to the design of the measures sought to be justified.¹⁵⁷ There is no justification under Article XX(d) for a measure that is not designed "to secure compliance" with a Member's laws or regulations. Thus, the terms "to secure compliance" do not expand the scope of the terms "laws or regulations" to encompass the international obligations of another WTO Member. Rather, the terms "to secure compliance" circumscribe the scope of Article XX(d).

73. Mexico takes issue with several aspects of the Panel's reasoning related to the interpretation of the terms "to secure compliance". We recall that, according to the Panel, "[t]he context in which the expression is used makes clear that 'to secure compliance' is to be read as meaning to enforce compliance."¹⁵⁸ The Panel added that, in contrast to enforcement action taken within a Member's legal system, "the effectiveness of [Mexico's] measures in achieving their stated goal—that of bringing about a change in the behaviour of the United States—seems ... to be inescapably uncertain."¹⁵⁹ Thus, the Panel concluded that "the outcome of international countermeasures, such as those adopted by Mexico, is inherently unpredictable".¹⁶⁰

74. It is Mexico's submission that the Panel erred in requiring a degree of certainty as to the results achieved by the measure sought to be justified.¹⁶¹ Mexico also asserts that the Panel, in its reasoning, incorrectly relied on the Appellate Body Report in *US – Gambling*.¹⁶² We agree with

¹⁵⁶The Panel noted that there are examples of international "regulations" within the WTO agreements themselves. The Panel cited, as examples, Article VI of the *Marrakesh Agreement Establishing the World Trade Organization* that refers to "regulations" to be adopted by the Ministerial Conference, and Article VII that refers to "financial regulations" to be adopted by the General Council and to the "regulations" of the GATT 1947. (Panel Report, footnotes 423 and 424 to para. 8.195) Article XXIV of the GATT 1994 also uses the term "regulations" when referring to rules applied by free trade areas or customs unions. Nevertheless, we agree with Japan that, in these instances, the context makes it clear that the regulations are international in character. (Japan's third participant's submission, paras. 17-19)

¹⁵⁷ Appellate Body Report, *Korea – Various Measures on Beef*, para. 157.

¹⁵⁸ Panel Report, para. 8.175.

¹⁵⁹ *Ibid.*, para. 8.185.

¹⁶⁰ *Ibid.*, para. 8.186. See also Mexico's appellant's submission, paras. 104-116.

¹⁶¹ The European Communities and Japan agree with Mexico that the Panel erred in implying that whether a measure falls within the meaning of the phrase "to secure compliance" depends on the degree of certainty that the measure will achieve its intended results. (European Communities' third participant's submission, para. 26; Japan's third participant's submission, para. 10)

¹⁶² Panel Report, paras. 8.187-8.188 (referring to Appellate Body Report, *US – Gambling*, para. 317).

Mexico that the *US – Gambling* Report does not support the conclusion that the Panel sought to draw from it. The statement to which the Panel referred was made in the context of the examination of the "necessity" requirement in Article XIV(a) of the *General Agreement on Trade in Services*, and did not relate to the terms "to secure compliance". As the Appellate Body has explained previously, "the contribution made by the compliance measure to the enforcement of the law or regulation at issue"¹⁶³ is one of the factors that must be weighed and balanced to determine whether a measure is "necessary" within the meaning of Article XX(d). A measure that is not suitable or capable of securing compliance with the relevant laws or regulations will not meet the "necessity" requirement. We see no reason, however, to derive from the Appellate Body's examination of "necessity", in *US – Gambling*, a requirement of "certainty" applicable to the terms "to secure compliance".¹⁶⁴ In our view, a measure can be said to be designed "to secure compliance" even if the measure cannot be guaranteed to achieve its result with absolute certainty.¹⁶⁵ Nor do we consider that the "use of coercion"¹⁶⁶ is a necessary component of a measure designed "to secure compliance". Rather, Article XX(d) requires that the design of the measure contribute "to secur[ing] compliance with laws or regulations which are not inconsistent with the provisions of" the GATT 1994.

75. Nevertheless, while we agree with Mexico that the Panel's emphasis on "certainty" and "coercion" is misplaced, we consider that Mexico's arguments miss the point. Even if "international countermeasures" could be described as intended "to secure compliance", what they seek "to secure compliance with"—that is, the international obligations of another WTO Member—would be outside the scope of Article XX(d). This is because "laws or regulations" within the meaning of Article XX(d) refer to the rules that form part of the domestic legal order of the WTO Member invoking the provision and do not include the international obligations of *another* WTO Member.

¹⁶³ Appellate Body Report, *Korea – Various Measures on Beef*, para. 164.

¹⁶⁴ We note that, at the request of the United States, the Panel clarified in the interim review phase that:

... its reasoning does not focus on whether the achievement of Mexico's objective through the measures at issue is certain or uncertain. Rather, the Panel considers that international countermeasures (as the ones allegedly imposed by Mexico) are intrinsically unable to secure compliance of laws and regulations. In contrast, national measures are, beyond particular factual considerations, usually in a position to achieve [] that objective, through the use of coercion, if necessary.

(Panel Report, para. 6.12) (original italics; underlining added)

¹⁶⁵ The European Communities notes that "even within the domestic legal order of WTO Members, enforcement of laws and regulations may not simply be taken for granted, but may depend on numerous factors". (European Communities' third participant's submission, para. 28)

¹⁶⁶ Panel Report, para. 8.178.

76. Mexico finds support for its interpretation in the Appellate Body's rulings in *US – Shrimp* and *US – Shrimp (Article 21.5 – Malaysia)*.¹⁶⁷ We fail to see how these rulings support Mexico's position. In those cases, the United States sought to justify its measures under Article XX(g) of the GATT 1994, and the measures at issue were domestic laws and regulations of the United States.¹⁶⁸ The reference to the Inter-American Convention for the Protection and Conservation of Sea Turtles (the "Inter-American Convention") was made in the context of the examination of whether the measures constituted "a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail" for purposes of the chapeau of Article XX.¹⁶⁹ The United States, in those cases, did not argue that its measures were justified under Article XX(d) because they were intended to secure compliance with the obligations of another Member under the Inter-American Convention. In the present case, Mexico seeks to justify its measures under paragraph (d) of Article XX, and not under paragraph (g). Moreover, Mexico not only refers to the NAFTA in relation to the chapeau of Article XX, but also seeks justification for its measures under paragraph (d) on the basis that they are allegedly intended to secure compliance with the United States' NAFTA obligations.

77. We observe, furthermore, that Mexico's interpretation of Article XX(d) disregards the fact that the GATT 1994 and the DSU specify the actions that a WTO Member may take if it considers that another WTO Member has acted inconsistently with its obligations under the GATT 1994 or any of the other covered agreements. As the United States points out¹⁷⁰, Mexico's interpretation of the terms "laws or regulations" as including international obligations of another WTO Member would logically imply that a WTO Member could invoke Article XX(d) to justify also measures designed "to secure compliance" with that other Member's WTO obligations. By the same logic, such action under Article XX(d) would evade the specific and detailed rules that apply when a WTO Member seeks to take countermeasures in response to another Member's failure to comply with rulings and recommendations of the DSB pursuant to Article XXIII:2 of the GATT 1994 and Articles 22 and 23 of the DSU.¹⁷¹ Mexico's interpretation would allow WTO Members to adopt WTO-inconsistent measures based upon a *unilateral* determination that another Member has breached its WTO obligations, in contradiction with Articles 22 and 23 of the DSU and Article XXIII:2 of the GATT 1994.

¹⁶⁷Mexico's appellant's submission, paras. 174-178.

¹⁶⁸See Appellate Body Report, *US – Shrimp*, paras. 2-6.

¹⁶⁹See *ibid.*, paras. 169-172; and Appellate Body Report, *US – Shrimp (Article 21.5 – Malaysia)*, para. 128. See also United States' appellee's submission, para. 108.

¹⁷⁰United States' appellee's submission, para. 37.

¹⁷¹Mexico's interpretation would also undermine the limitations in paragraphs 3 and 4 of Article 22 as to the magnitude and the trade sectors in which such countermeasures could be taken. (*Ibid.*, paras. 37-38)

78. Finally, even if the terms "laws or regulations" do not go so far as to encompass the WTO agreements, as Mexico argues¹⁷², Mexico's interpretation would imply that, in order to resolve the case, WTO panels and the Appellate Body would have to assume that there is a violation of the relevant international agreement (such as the NAFTA) by the complaining party, or they would have to assess whether the relevant international agreement has been violated. WTO panels and the Appellate Body would thus become adjudicators of non-WTO disputes.¹⁷³ As we noted earlier¹⁷⁴, this is not the function of panels and the Appellate Body as intended by the DSU.¹⁷⁵

79. For these reasons, we agree with the Panel that Article XX(d) is not available to justify WTO-inconsistent measures that seek "to secure compliance" by another WTO Member with that other Member's international obligations. In sum, while we agree with the Panel's conclusion, several aspects of our reasoning set out above differ from the Panel's own reasoning. First, we conclude that the terms "laws or regulations" cover rules that form part of the domestic legal system of a WTO Member, including rules deriving from international agreements that have been incorporated into the domestic legal system of a WTO Member or have direct effect according to that WTO Member's legal system.¹⁷⁶ Second, we have found that Article XX(d) does not require the "use of coercion" nor that the measure sought to be justified results in securing compliance with absolute certainty. Rather, Article XX(d) requires that the measure be designed "to secure compliance with laws or regulations which are not inconsistent with the provisions of" the GATT 1994.¹⁷⁷ Finally, we do not endorse the Panel's reliance on the Appellate Body's interpretation in *US – Gambling* of the term "necessary" to interpret the terms "to secure compliance" in Article XX(d).¹⁷⁸

¹⁷²At the oral hearing, Mexico argued that the terms "laws or regulations" would not include the WTO agreements because the latter are *lex specialis*.

¹⁷³Article 3.2 of the DSU states that the WTO's dispute settlement system "serves to preserve the rights and obligations of Members under the covered agreements, and to clarify the existing provisions of those agreements". (emphasis added)

¹⁷⁴See *supra*, para. 56.

¹⁷⁵We note that, in its analysis, the Panel also referred to the negotiating history of the GATT 1947, and particularly to the rejection of a proposal presented by India during the negotiations on the International Trade Organization (the "ITO") Charter according to which Members would be permitted to justify, on a temporary basis, retaliatory measures under Article XX. (See Panel Report, para. 8.176 (referring to ITO Doc. E/PC/T/180 (19 August 1947), p. 97; and "Havana Charter for an International Trade Organization"; United Nations Conference on Trade and Employment, Final Act and Related Documents (Lake Success, New York, April 1948), pp. 33-34)

¹⁷⁶See *supra*, paras. 69-71.

¹⁷⁷See *supra*, para. 74.

¹⁷⁸See *supra*, para. 74.

80. Therefore, we *uphold*, albeit for different reasons, the Panel's conclusion, in paragraph 8.198 of the Panel Report, that Mexico's measures do not constitute measures "to secure compliance with laws or regulations", within the meaning of Article XX(d) of the GATT 1994.

2. Mexico's Request to Complete the Analysis

81. Mexico requests the Appellate Body to complete the analysis by examining whether Mexico's measures are "necessary", within the meaning of Article XX(d) of the GATT 1994, and meet the requirements of the chapeau of that Article.¹⁷⁹ Mexico's request is premised on the Appellate Body reversing the Panel's conclusion that the measures are not designed "to secure compliance with laws or regulations" within the meaning of Article XX(d). We have upheld the Panel's conclusion that Mexico's measures do not constitute measures "to secure compliance with laws or regulations" within the meaning of Article XX(d) of the GATT 1994. Therefore, the premise on which Mexico's request is predicated is not fulfilled and, consequently, it is not necessary for us to complete the analysis as requested by Mexico.¹⁸⁰

3. Mexico's Claim under Article 11 of the DSU¹⁸¹

82. Mexico argues, "separately and in addition"¹⁸² to the previous errors, that the Panel failed to make "an objective assessment of the facts", as required by Article 11 of the DSU, in finding that "Mexico has not established that its measures contribute to securing compliance in the circumstances of this case."¹⁸³ Mexico argues that "[t]he evidence on the record demonstrates that the effects of the measures at issue have contributed to securing compliance in the circumstances of this case, by changing the dynamic of the NAFTA dispute and forcing the United States to pay attention to

¹⁷⁹Mexico's appellant's submission, para. 138.

¹⁸⁰See, for example, Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 74.

¹⁸¹In its Notice of Appeal, Mexico claimed that the Panel "failed to make an objective assessment of the matter before it, including the facts of the case, inconsistently with its obligation under Article 11 of the DSU, with respect to Mexico's request for determinations of fact, status and relevance of the NAFTA dispute between the parties." (Mexico's Notice of Appeal (attached as Annex I to this Report), para. 4 (referring to Panel Report, paras. 8.231 and 8.232) (footnote omitted)) Mexico also asserted that "in concluding that international countermeasures cannot qualify for consideration as measures designed to 'secure compliance' within the meaning of Article XX(d) of the GATT 1994, the Panel improperly increased the obligations of WTO Members and reduced the rights of Members under the covered agreements." (*Ibid.*, para. 5 (referring to Panel Report, paras. 8.181 and 8.186) (footnote omitted)) Mexico did not offer arguments to support these two claims in its appellant's submission. In response to questioning at the oral hearing, Mexico confirmed that it did not intend to pursue these claims further.

¹⁸²Mexico's appellant's submission, heading III.E ("independiente y adicional").

¹⁸³Panel Report, paragraph 8.186. See also, Mexico's Notice of Appeal, para. 3.

Mexico's grievances."¹⁸⁴ The United States submits that, contrary to Mexico's contention, the Panel did not "ignore" arguments or evidence submitted by Mexico.¹⁸⁵ The United States further explains that, in any event, Mexico's claim under Article 11 of the DSU "appears to be no more than a reiteration of its legal arguments that its ... measures are designed to 'secure compliance'".¹⁸⁶

83. In Section B.1 above, we held that Mexico's measures do not constitute measures "to secure compliance with laws or regulations", within the meaning of Article XX(d) of the GATT 1994. Therefore, Mexico's claim under Article 11 of the DSU is predicated on an interpretation of Article XX(d) of the GATT 1994 that we have found to be incorrect. Since Mexico's measures cannot be justified under Article XX(d) as a *matter of law*, we reject Mexico's claim under Article 11 of the DSU.

4. Conclusion

84. For the reasons set out above, we *uphold* the Panel's conclusion, in paragraphs 8.204 and 9.3 of the Panel Report, that "Mexico has not established that the challenged measures are justified under Article XX of the GATT 1994".

VI. **Findings and Conclusions**

85. For the reasons set out in this Report, the Appellate Body:

- (a) upholds the Panel's conclusion, in paragraphs 7.1, 7.18, and 9.1 of the Panel Report, that, "under the DSU, it ha[d] no discretion to decline to exercise its jurisdiction in the case that ha[d] been brought before it";
- (b) upholds the Panel's conclusion, in paragraph 8.198 of the Panel Report, that Mexico's measures do not constitute measures "to secure compliance with laws or regulations", within the meaning of Article XX(d) of the GATT 1994;
- (c) rejects Mexico's claim that the Panel failed to fulfil its obligations under Article 11 of the DSU, in finding, in paragraph 8.186 of the Panel Report, that "Mexico has not established that its measures contribute to securing compliance in the circumstances of this case"; and

¹⁸⁴Mexico's appellant's submission, para. 167 ("*Las pruebas en el expediente demuestran que las medidas en cuestión no están desprovistas de efectos que contribuyen a lograr la observancia en las circunstancias de este caso, cambiando la dinámica en la controversia derivada del TLCAN y forzando a Estados Unidos a prestar atención a los agravios de México*").

¹⁸⁵United States' appellee's submission, para. 118.

¹⁸⁶*Ibid.*

(d) as a consequence, upholds the Panel's conclusion, in paragraphs 8.204 and 9.3 of the Panel Report, that "Mexico has not established that the challenged measures are justified under Article XX of the GATT 1994".

86. The Appellate Body recommends that the Dispute Settlement Body request Mexico to bring the measures that were found in the Panel Report to be inconsistent with the *General Agreement on Tariff and Trade 1994* into conformity with its obligations under that Agreement.

Signed in the original in Geneva this 8th day of February 2006 by:

Yasuhei Taniguchi
Presiding Member

Merit E. Janow
Member

Giorgio Sacerdoti
Member

ANNEX I

**WORLD TRADE
ORGANIZATION**

WT/DS308/10
6 December 2005

(05-5832)

Original: Spanish

**MEXICO – TAX MEASURES ON SOFT DRINKS AND
OTHER BEVERAGES**

Notification of an Appeal by Mexico under Article 16.4 and Article 17 of the
Understanding on Rules and Procedures Governing the Settlement of
Disputes (DSU) and Rule 20(1) of the Working
Procedures for Appellate Review

The following notification dated 6 December 2005, from the delegation of Mexico, is being circulated to Members.

Pursuant to Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 20 of the *Working Procedures for Appellate Review*, Mexico hereby notifies its decision to appeal to the Appellate Body certain issues of law dealt with in the Report of the Panel on *Mexico – Tax Measures on Soft Drinks and Other Beverages* (WT/DS308/R) (the "Panel Report") and certain legal interpretations developed by the Panel in this dispute.

1. Mexico seeks review by the Appellate Body of the Panel's legal conclusion that it has no discretion to decline to exercise jurisdiction in this case and its determination that, even if it had such discretion, the facts in the record do not justify a refusal by the Panel to exercise jurisdiction in this case. This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations concerning Articles 3, 7, 11 and 19 of the DSU and Articles XXII and XXIII of the GATT 1994. These errors are contained, *inter alia*, in paragraphs 7.1 to 7.18, 8.215 to 8.230 and 9.1 of the Panel Report.

2. Mexico seeks review by the Appellate Body of the Panel's legal conclusion that the challenged tax measures are not justified under Article XX of the GATT 1994 as measures necessary to secure United States compliance with laws or regulations which are not inconsistent with the provisions of the GATT 1994. This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations concerning Article XX of the GATT 1994. Paragraphs 8.168 to 8.204 and 9.3 of the Panel Report, among others, contain such errors, including the following:

- (a) The Panel's interpretation and application of the expression "to secure compliance" in Article XX(d) of the GATT 1994 and its conclusion that it does not apply to measures taken by a Member in order to induce another Member to comply with obligations owed to it under a non-WTO treaty.¹
 - (b) The Panel's conclusion that the challenged tax measures "are not designed to secure compliance" within the meaning of Article XX(d) of the GATT 1994 and are not eligible for consideration under Article XX(d) of the GATT 1994.²
 - (c) The Panel's interpretation and application of the phrase "laws or regulations" contained in Article XX(d) of the GATT 1994 and its conclusion that this phrase does not cover international treaties such as NAFTA.³
 - (d) The Panel's failure to consider whether the Mexican measures are "necessary" to secure compliance with a law that is not inconsistent with the provisions of the GATT 1994.⁴
3. Mexico seeks review by the Appellate Body, in the light of DSU Article 11, of the Panel's conclusion that "Mexico has not established that its measures contribute to securing compliance in the circumstances of this case".⁵ This conclusion does not reflect an objective approach to analysis of the available evidence on the effects of the Mexican measures, and is inconsistent with the treatment given by the Panel to relevant evidence. Accordingly, this conclusion is inconsistent with the Panel's duty to make an objective assessment of the matter before it.

463 4. Mexico considers that the Panel also failed to make an objective assessment of the matter before it, including the facts of the case, inconsistently with its obligation under Article 11 of the DSU, with respect to Mexico's request for determinations of fact, status and relevance of the NAFTA dispute between the parties.⁶

5. Mexico also considers that, in concluding that international countermeasures cannot qualify for consideration as measures designed to "secure compliance" within the meaning of Article XX(d) of the GATT 1994,⁷ the Panel improperly increased the obligations of WTO Members and reduced the rights of Members under the covered agreements.

6. In the event that the Appellate Body reverses the Panel's conclusion that Mexico's tax measures are not justified under Article XX(d) of the GATT 1994, Mexico requests that the Appellate Body complete the legal analysis under Article XX of the GATT 1994.

Those provisions of the covered agreements which Mexico considers the Panel to have interpreted or applied erroneously include Articles XX, XXII and XXIII of the GATT 1994 and Articles 3, 7, 11 and 19 of the DSU.

¹ Panel Report, paragraphs 8.170 to 8.181.

² Panel Report, paragraphs 8.182 to 8.190 and 8.197 to 8.198.

³ Panel Report, paragraphs 8.191 to 8.197.

⁴ Panel Report, paragraphs 8.199 to 8.202.

⁵ Panel Report, paragraph 8.186.

⁶ Panel Report, paragraphs 8.231 and 8.232.

⁷ Panel Report, paragraphs 8.181 and 8.186.

World Trade Organization

**Thailand – Customs and Fiscal Measures on Cigarettes from
the Philippines**

Report of the Appellate Body, 17 June 2011

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**THAILAND – CUSTOMS AND FISCAL MEASURES ON CIGARETTES
FROM THE PHILIPPINES**

AB-2011-1

Report of the Appellate Body

CASES CITED IN THIS REPORT I

Short Title	Full Case Title and Citation
Argentina – Hides and Leather	Panel Report, <i>Argentina – Measures Affecting the Export of Bovine Hides and Import of Finished Leather</i> , WT/DS155/R and Corr.1, adopted 16 February 2001, DSR 2001:V, 1779
Argentina – Textiles and Apparel	Appellate Body Report, <i>Argentina – Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items</i> , WT/DSS6/AB/R and Corr.1, adopted 22 April 1998, DSR 1998:III, 1003
Australia – Salmon	Appellate Body Report, <i>Australia – Measures Affecting Importation of Salmon</i> , WT/DS18/AB/R, adopted 6 November 1998, DSR 1998:VIII, 3327
Brazil – Retreaded Tyres	Appellate Body Report, <i>Brazil – Measures Affecting Imports of Retreaded Tyres</i> , WT/DS332/AB/R, adopted 17 December 2007, DSR 2007:IV, 1527
Canada – Autos	Panel Report, <i>Canada – Certain Measures Affecting the Automotive Industry</i> , WT/DS139/R, WT/DS142/R, adopted 19 June 2000, as modified by Appellate Body Report WT/DS139/AB/R, WT/DS142/AB/R, DSR 2000:VII, 3043
Canada – Continued Suspension	Appellate Body Report, <i>Canada – Continued Suspension of Obligations in the EC – Hormones Dispute</i> , WT/DS321/AB/R, adopted 14 November 2008
Canada – Patent Term	Appellate Body Report, <i>Canada – Term of Patent Protection</i> , WT/DS170/AB/R, adopted 12 October 2000, DSR 2000:X, 5093
Canada – Periodicals	Appellate Body Report, <i>Canada – Certain Measures Concerning Periodicals</i> , WT/DS31/AB/R, adopted 30 July 1997, DSR 1997:1, 449
Canada – Wheat Exports and Grain Imports	Appellate Body Report, <i>Canada – Measures Relating to Exports of Wheat and Treatment of Imported Grain</i> , WT/DS276/AB/R, adopted 27 September 2004, DSR 2004:VI, 2739
Canada – Wheat Exports and Grain Imports	Panel Report, <i>Canada – Measures Relating to Exports of Wheat and Treatment of Imported Grain</i> , WT/DS276/R, adopted 27 September 2004, as upheld by Appellate Body Report WT/DS276/AB/R, DSR 2004:VI, 2817
Chile – Price Band System	Appellate Body Report, <i>Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products</i> , WT/DS207/AB/R, adopted 23 October 2002, DSR 2002:VIII, 3045 (Corr.1, DSR 2006:XII, 5473)
China – Auto Parts	Appellate Body Reports, <i>China – Measures Affecting Imports of Automobile Parts</i> , WT/DS339/AB/R, WT/DS340/AB/R, WT/DS342/AB/R, adopted 12 January 2009
China – Auto Parts	Panel Reports, <i>China – Measures Affecting Imports of Automobile Parts</i> , WT/DS339/R, WT/DS340/R, WT/DS342/R and Add.1 and Add.2, adopted 12 January 2009, as upheld (WT/DS339/R) and as modified (WT/DS340/R, WT/DS342/R) by Appellate Body Reports WT/DS339/AB/R, WT/DS340/AB/R, WT/DS342/AB/R
China – Intellectual Property Rights	Panel Report, <i>China – Measures Affecting the Protection and Enforcement of Intellectual Property Rights</i> , WT/DS362/R, adopted 20 March 2009
China – Publications and Audiovisual Products	Panel Report, <i>China – Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products</i> , WT/DS363/R and Corr.1, adopted 19 January 2010, as modified by Appellate Body Report WT/DS363/AB/R
Colombia – Ports of Entry	Panel Report, <i>Colombia – Indicative Prices and Restrictions on Ports of Entry</i> , WT/DS366/R and Corr.1, adopted 20 May 2009

Short Title	Full Case Title and Citation
EC – Asbestos	Appellate Body Report, <i>European Communities – Measures Affecting Asbestos and Asbestos-Containing Products</i> , WT/DS135/AB/R, adopted 5 April 2001, DSR 2001:VII, 3243
EC – Bananas III	Appellate Body Report, <i>European Communities – Regime for the Importation, Sale and Distribution of Bananas</i> , WT/DS27/AB/R, adopted 25 September 1997, DSR 1997:II, 591
EC – Chicken Cuts	Appellate Body Report, <i>European Communities – Customs Classification of Frozen Boneless Chicken Cuts</i> , WT/DS269/AB/R, WT/DS286/AB/R, adopted 27 September 2005, and Corr.1, DSR 2005:XIX, 9157
EC – Hormones	Appellate Body Report, <i>EC Measures Concerning Meat and Meat Products (Hormones)</i> , WT/DS26/AB/R, WT/DS48/AB/R, adopted 13 February 1998, DSR 1998:1, 135
EC – Sardines	Appellate Body Report, <i>European Communities – Trade Description of Sardines</i> , WT/DS231/AB/R, adopted 23 October 2002, DSR 2002:VIII, 3359
EC – Selected Customs Matters	Appellate Body Report, <i>European Communities – Selected Customs Matters</i> , WT/DS315/AB/R, adopted 11 December 2006, DSR 2006:IX, 3791
EC – Selected Customs Matters	Panel Report, <i>European Communities – Selected Customs Matters</i> , WT/DS315/R, adopted 11 December 2006, as modified by Appellate Body Report WT/DS315/AB/R, DSR 2006:IX-X, 3915
India – Autos	Panel Report, <i>India – Measures Affecting the Automotive Sector</i> , WT/DS146/R, WT/DS175/R and Corr.1, adopted 5 April 2002, DSR 2002:V, 1827
India – Patents (US)	Appellate Body Report, <i>India – Patent Protection for Pharmaceutical and Agricultural Chemical Products</i> , WT/DSS50/AB/R, adopted 16 January 1998, DSR 1998:1, 9
Japan – Alcoholic Beverages II	Appellate Body Report, <i>Japan – Taxes on Alcoholic Beverages</i> , WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, DSR 1996:1, 97
Korea – Alcoholic Beverages	Appellate Body Report, <i>Korea – Taxes on Alcoholic Beverages</i> , WT/DS75/AB/R, WT/DS84/AB/R, adopted 17 February 1999, DSR 1999:1, 3
Korea – Alcoholic Beverages	Panel Report, <i>Korea – Taxes on Alcoholic Beverages</i> , WT/DS75/R, WT/DS84/R, adopted 17 February 1999, as modified by Appellate Body Report WT/DS75/AB/R, WT/DS84/AB/R, DSR 1999:1, 44
Korea – Various Measures on Beef	Appellate Body Report, <i>Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef</i> , WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, DSR 2001:1, 5
Mexico – Corn Syrup (Article 21.5 – US)	Appellate Body Report, <i>Mexico – Anti-Dumping Investigation of High Fructose Corn Syrup (HFCs) from the United States – Recourse to Article 21.5 of the DSU by the United States</i> , WT/DS132/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6675
Thailand – Cigarettes (Philippines)	Panel Report, <i>Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines</i> , WT/DS371/R, circulated to WTO Members 15 November 2010
Thailand – H-Beams	Appellate Body Report, <i>Thailand – Anti-Dumping Duties on Angles, Shapes and Sections of Iron or Non-Alloy Steel and H-Beams from Poland</i> , WT/DS122/AB/R, adopted 5 April 2001, DSR 2001:VII, 2701

LIST OF ABBREVIATIONS USED IN THIS REPORT

Short Title	Full Case Title and Citation
US – Carbon Steel	Appellate Body Report, <i>United States – Countervailing Duties on Certain Corrosion-Resistant Carbon Steel Flat Products from Germany</i> , WT/DS213/AB/R and Corr.1, adopted 19 December 2002, DSR 2002:IX, 3779
US – Continued Suspension	Appellate Body Report, <i>United States – Continued Suspension of Obligations in the EC – Hormones Dispute</i> , WT/DS320/AB/R, adopted 14 November 2008, DSR 2008:X, 3507
US – Continued Zeroing	Appellate Body Report, <i>United States – Continued Existence and Application of Zeroing Methodology</i> , WT/DS350/AB/R, adopted 19 February 2009
US – FSC	Appellate Body Report, <i>United States – Tax Treatment for “Foreign Sales Corporations”</i> , WT/DS108/AB/R, adopted 20 March 2000, DSR 2000:III, 1619
US – FSC (Article 21.5 – EC)	Appellate Body Report, <i>United States – Tax Treatment for “Foreign Sales Corporations” – Recourse to Article 21.5 of the DSU by the European Communities</i> , WT/DS108/AB/RW, adopted 29 January 2002, DSR 2002:I, 55
US – Gambling	Appellate Body Report, <i>United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services</i> , WT/DS285/AB/R, adopted 20 April 2005, DSR 2005:XII, 5663 (Corr.1, DSR 2006:XII, 5475)
US – Gasoline	Appellate Body Report, <i>United States – Standards for Reformulated and Conventional Gasoline</i> , WT/DS2/AB/R, adopted 20 May 1996, DSR 1996:1, 3
US – Hot-Rolled Steel	Appellate Body Report, <i>United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan</i> , WT/DS184/AB/R, adopted 23 August 2001, DSR 2001:X, 4697
US – Malt Beverages	GATT Panel Report, <i>United States – Measures Affecting Alcoholic and Malt Beverages</i> , DS23/R, adopted 19 June 1992, BISD 39S/206
US – Section 211 Appropriations Act	Appellate Body Report, <i>United States – Section 211 Omnibus Appropriations Act of 1998</i> , WT/DS176/AB/R, adopted 1 February 2002, DSR 2002:II, 589
US – Section 301 Trade Act	Panel Report, <i>United States – Sections 301-310 of the Trade Act of 1974</i> , WT/DS152/R, adopted 27 January 2000, DSR 2000:II, 815
US – Section 337 Tariff Act	GATT Panel Report, <i>United States Section 337 of the Tariff Act of 1930</i> , L/6439, adopted 7 November 1989, BISD 36S/345
US – Shrimp	Appellate Body Report, <i>United States – Import Prohibition of Certain Shrimp and Shrimp Products</i> , WT/DSS8/AB/R, adopted 6 November 1998, DSR 1998:VII, 2755
US – Shrimp (Thailand) / US – Customs Bond Directive	Appellate Body Report, <i>United States – Measures Relating to Shrimp from Thailand / United States – Customs Bond Directive for Merchandise Subject to Anti-Dumping/Countervailing Duties</i> , WT/DS343/AB/R / WT/DS345/AB/R, adopted 1 August 2008, DSR 2008:VII, 2385 / DSR 2008:VIII, 2773
US – Tobacco	GATT Panel Report, <i>United States – Measures Affecting the Importation, Internal Sale and Use of Tobacco</i> , DS44/R, adopted 4 October 1994, BISD 41S/131

Abbreviation	Description
1995 DG Revenue ruling	Ruling by the Director-General of the Thai Revenue Department, Gor.Kor. 0802/Por.22836, dated 10 October 1995 (Panel Exhibit THA-96)
2000 DG Revenue ruling	Ruling by the Director-General of the Thai Revenue Department, Gor.Kor. 0811/Por.633, dated 27 January 2000 (Panel Exhibit PHL-253).
2006 textbook	Excerpt of page 4-266 of <i>Textbook on the Revenue Code</i> by Professor Paichit Rojanavanich, Chumporn Sensai, and Saroch Thongpracum, B.E. 2549 (2006) (Panel Exhibit THA-95)
Agreement on Customs Valuation	<i>Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994</i>
Anti-Dumping Agreement	<i>Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994</i>
BCI	business confidential information
BoA	Board of Appeals
DSB	Dispute Settlement Body
DSU	<i>Understanding on Rules and Procedures Governing the Settlement of Disputes</i>
GATT 1994	<i>General Agreement on Tariffs and Trade 1994</i>
MRSP	maximum retail selling price, a reference price fixed by the Thai Government for each brand of cigarettes
Order No. Por. 85/2542	Government of the Kingdom of Thailand, Order of Revenue Department No. Por. 85/2542, Re Computation of Tax Base for Importation and Sale of Tobacco According to Category and Type Prescribed by Director-General and Approved by Minister Under Section 79/5 of Revenue Code, and Preparation of Tax Invoice in Case of Sale of Tobacco Under Section 86/5(2) of Revenue Code (Panel Exhibit PHL-95)
Panel Report	Panel Report, <i>Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines</i> , WT/DS371/R, 15 November 2010
Revised Kyoto Convention	<i>International Convention on the Simplification and Harmonization of Customs Procedures</i> , done at Kyoto, 18 May 1973, 950 UNTS 269, as amended by the <i>Protocol of Amendment to the International Convention on the Simplification and Harmonization of Customs Procedures</i> , done at Brussels, 26 June 1999, 2370 UNTS 27
Royal Decree No. 239	Government of the Kingdom of Thailand, Royal Decree Issued Under the Revenue Code Governing Exemption from Value Added Tax (No. 239) B.E. 2534 (Panel Exhibit PHL-217)
Thai Customs	Thai Customs Department
Thai Customs Act	Government of the Kingdom of Thailand, The Customs Act, B.E. 2469 (Panel Exhibit PHL-20).

WORLD TRADE ORGANIZATION
APPELLATE BODY

Abbreviation	Description
Thai Revenue Code	Government of the Kingdom of Thailand, The Council of Regency, The Act Promulgating the Revenue Code, B.E. 2481 (Panel Exhibit PHL-94).
TRIPS Agreement	<i>Agreement on Trade-Related Aspects of Intellectual Property Rights</i>
TTM	Thailand Tobacco Monopoly
VAT	value added tax
<i>Working Procedures</i>	<i>Working Procedures for Appellate Review</i> , WT/AB/WP/6, 16 August 2010
WTO	World Trade Organization
<i>WTO Agreement</i>	<i>Marrakesh Agreement Establishing the World Trade Organization</i>

Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines

AB-2011-1

Present:

Thailand, *Appellant*

Philippines, *Appellee*

Australia, *Third Participant*

China, *Third Participant*

European Union¹, *Third Participant*

India, *Third Participant*

Separate Customs Territory of Taiwan, Penghu,

Kinmen and Matsu, *Third Participant*

United States, *Third Participant*

Van den Bossche, Presiding Member

Ramírez-Hernández, Member

Zhang, Member

I. Introduction

1. Thailand appeals certain issues of law and legal interpretations developed in the Panel Report, *Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines* (the "Panel Report").² The Panel was established on 17 November 2008 to consider a complaint by the Philippines with respect to certain customs and fiscal measures imposed by Thailand on cigarettes imported from the Philippines.³

¹This dispute began before the entry into force of the *Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community* (done at Lisbon, 13 December 2007) on 1 December 2009. On 29 November 2009, the World Trade Organization received a Verbal Note (WT/L/779) from the Council of the European Union and the Commission of the European Communities stating that, by virtue of the *Treaty of Lisbon*, as of 1 December 2009, the "European Union" replaces and succeeds the "European Community". On 13 July 2010, the World Trade Organization received a second Verbal Note (WT/Let/679) from the Council of the European Union confirming that, with effect from 1 December 2009, the European Union replaced the European Community and assumed all the rights and obligations of the European Community in respect of all Agreements for which the Director-General of the World Trade Organization is the depositary and to which the European Community is a signatory or a contracting party. We understand the reference in the Verbal Notes to the "European Community" to be a reference to the "European Communities". In the proceedings before the Panel, the third party submission dated 18 May 2009 and the statement at the third party session on 11 June 2009 were made by the delegation of the European Communities. On 8 January 2010, the European Union requested the Panel to refer to "European Union" and "EU", rather than "European Communities" and "EC", in the Panel Report. (Panel Report, footnote 3 to para. 1.6) We refer to the European Union in this Report.

²WT/DS371/R, 15 November 2010.

³Panel Report, para. 1.3.

2. Before the Panel, the Philippines made a number of claims in respect of several Thai customs and fiscal measures affecting cigarettes imported from the Philippines.⁴ The Philippines raised three sets of claims: (i) with respect to measures pertaining to customs valuation, under Articles 1, 4, 5, 7, 10, and 16 of the *Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994* (the "*Agreement on Customs Valuation*")⁵; (ii) with respect to measures forming part of Thailand's value added tax ("VAT") regime under Article III:2 and Article III:4 of the *General Agreement on Tariffs and Trade 1994* (the "*GATT 1994*")⁶; and (iii) with respect to Thailand's administration of certain customs and fiscal measures, including with respect to guarantees, under Article X of the *GATT 1994*.⁷

3. The Panel Report was circulated to Members of the World Trade Organization (the "WTO") on 15 November 2010.

⁴Panel Report, para. 7.1.

⁵With respect to Thai Customs' valuation of cigarettes imported from the Philippines and cleared between 11 August 2006 and 13 September 2007, the Philippines claimed that: (i) Thailand acted inconsistently with Article 1.1 and Article 1.2(a) of the *Agreement on Customs Valuation* because Thai Customs improperly rejected the transaction values of those entries; (ii) Thai Customs applied the deductive valuation method inconsistently with Thailand's obligations under Articles 5 and 7 in determining the customs value of those cigarette entries; (iii) Thailand acted inconsistently with its obligation under Article 10 not to disclose confidential information; and (iv) Thailand acted inconsistently with its obligation under Article 16 to provide an explanation for the determination of the final customs value. The Philippines also claimed that Thailand acted inconsistently with Article 1.1 and Article 1.2(a) of the *Agreement on Customs Valuation* by maintaining an unpublished general rule requiring the rejection of transaction value and the use of the deductive valuation method. (Panel Report, paras. 7.2 and 7.79-7.81)

⁶The Philippines claimed that Thailand acted inconsistently with Article III:2, first sentence, of the *GATT 1994* by subjecting imported cigarettes to tax in excess of that applied to like domestic cigarettes through: (i) a discriminatory tax base for VAT imposed on imported cigarettes; and (ii) the exemption of domestic cigarettes from VAT obligations. The Philippines also claimed that Thailand acted inconsistently with Article III:4 of the *GATT 1994* by imposing more onerous administrative requirements on resellers of imported cigarettes than on resellers of domestic cigarettes. (Panel Report, paras. 7.412, 7.568, and 7.645)

⁷The Philippines claimed that Thailand acted inconsistently with Article X:1 of the *GATT 1994* by failing to publish: (i) the methodology for determining the maximum retail selling price ("MRSP"), a reference price fixed by the Thai Government for each brand of cigarettes; (ii) the methodology for determining ex factory prices for Thailand Tobacco Monopoly ("TTM") cigarettes; and (iii) laws and regulations governing the release of guarantees for potential liability arising from health, excise, and television taxes. The Philippines also raised the following claims under Article X:3(a) of the *GATT 1994*: (i) Thailand did not administer its customs and internal tax rules in a "reasonable" and "impartial" manner by appointing certain senior Thai Government officials to serve on the Board of Directors of TTM; (ii) undue delays in the decision-making process of the Board of Appeals (the "BoA") constitute an "unreasonable" administration of customs laws; (iii) the determination of the tax base for VAT for imported cigarettes is administered in a "non-uniform", "unreasonable", and "partial" manner; and (iv) the establishment of the health, excise, and television taxes in relation to imported cigarettes is administered in a "non-uniform", "unreasonable", and "partial" manner. The Philippines further claimed that Thailand acted inconsistently with Article X:3(b) of the *GATT 1994*: by (i) failing to maintain tribunals or procedures for the prompt review of appeals against certain customs valuation decisions; and (ii) failing to maintain or institute tribunals or procedures for the purpose of prompt review of guarantees imposed by Thai Customs on imported cigarettes. (Panel Report, paras. 7.759, 7.862, 7.989, and 7.1016)

4. In its Report, the Panel made a number of findings with respect to the scope of the matters before it⁸, and a number of findings that Thailand had acted inconsistently with its obligations under the *Agreement on Customs Valuation*.⁹ None of these findings is at issue in this appeal.

5. The Panel further made several findings that Thailand had acted inconsistently with its obligations under Article III of the *GATT 1994*, including that:

- (b) regarding the VAT exemption for domestic cigarette resellers, Thailand acted inconsistently with Article III:2, first sentence by subjecting imported cigarettes to a VAT liability in excess of that applied to like domestic cigarettes by granting the exemption from the VAT liability only to domestic cigarette resellers; and
- (c) regarding the VAT exemption for domestic cigarette resellers, Thailand acted inconsistently with Article III:4 by subjecting imported cigarettes to less favourable treatment compared to like domestic cigarettes by imposing additional administrative requirements, connected to VAT liabilities, on imported cigarette resellers.¹⁰

⁸With respect to the *claims* advanced by the Philippines, the Panel found that: (i) the Philippines' claim under Article X:3(a) of the *GATT 1994* with respect to the Thai VAT system was outside its terms of reference because the Philippines failed to plainly connect the challenged measure with Article X:3(a) in its panel request; and (ii) the Philippines' claim under Article X:3(a) with respect to the health, excise, and television taxes was within the Panel's terms of reference. (Panel Report, para. 8.1(a) and (b)); see also paras. 7.26 and 7.31) The Panel also found that, although the two provisions were listed in the panel request, the Philippines' claims under Article 4 and Article 7.1 of the *Agreement on Customs Valuation* were not supported by specific arguments and evidence presented in a timely manner, and further that Article 7.1 of the *Agreement on Customs Valuation* does not constitute a basis for an independent sequencing claim under that Agreement. (*Ibid.*, paras. 8.5 and 8.6; see also para. 7.280) With respect to the *measures* at issue, the Panel found the following to be within its terms of reference: (i) Thai Customs' valuation determinations for the imported cigarettes at issue that were cleared between 11 August 2006 and 13 September 2007; and (ii) the December 2005 MRSP Notice, the September 2006 MRSP Notice, the March 2007 MRSP Notice, and the August 2007 MRSP Notice. (*Ibid.*, para. 8.1(c) and (d); see also paras. 7.51 and 7.67)

⁹Panel Report, para. 8.2; see also paras. 7.195, 7.223, 7.266, 7.332, 7.398, and 7.411. With respect to the Philippines' claims under the *Agreement on Customs Valuation*, the Panel found that the rejection by Thai Customs of the declared transaction values for certain cigarette entries in 2006 and 2007 was inconsistent with Article 1.1 and Article 1.2, and that Thailand acted inconsistently with Article 1.2(a) by failing to communicate Thai Customs' grounds for such rejection. The Panel also found that the application by Thai Customs of its valuation methodology was inconsistent with Thailand's obligations under Article 7.1 and Article 7.3, and that Thailand acted inconsistently with Article 10 and Article 16, respectively, by disclosing confidential information, and by failing to provide an adequate explanation as to how Thai Customs determined customs values for imported cigarettes. The Panel found, however, that Thailand does not, as the Philippines claimed, maintain or apply a general rule requiring the rejection of the transaction value and the use of the deductive valuation method.

¹⁰Panel Report, para. 8.3(b) and (c); see also paras. 7.644 and 7.738. The Panel also found that Thailand acted inconsistently with Article III:2, first sentence, by subjecting imported cigarettes to VAT liability in excess of that applied to like domestic cigarettes with respect to the MRSPs for the December 2005 MRSP Notice, the September 2006 MRSP Notice, the March 2007 MRSP Notice, and the August 2007 MRSP Notice. (*Ibid.*, para. 8.3(a); see also para. 7.567) This finding has not been appealed.

6. The Panel also made certain findings that Thailand had acted inconsistently with its obligations under Article X of the GATT 1994, including that:

- (g) Thailand acted inconsistently with Article X:3(b) by failing to maintain or institute independent review tribunals or process for the prompt review of guarantee decisions.¹¹

7. The Panel recommended that the Dispute Settlement Body (the "DSB") request Thailand to bring those measures found to be inconsistent into conformity with its obligations under the GATT 1994 and the *Marrakesh Agreement Establishing the World Trade Organization* (the "*WTO Agreement*"). The Panel made no recommendation with respect to one measure that had expired. With respect to certain other measures found to be inconsistent with Thailand's obligations under the *Agreement on Customs Valuation*, the Panel indicated that it was "not entirely clear ... whether and, if so, to what extent"¹² those measures have effects on subsequent measures. Accordingly, for those measures, the Panel stated that its recommendations "apply only to the extent [that those measures] continue to have effects".¹³

8. On 22 February 2011, Thailand notified the DSB of its intention to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, pursuant to Article 16.4 and Article 17 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), and filed a Notice of Appeal¹⁴ and an appellant's submission pursuant to Rule 20 and Rule 21, respectively, of the *Working Procedures for Appellate Review* (the "*Working Procedures*").¹⁵ On 14 March 2011, the Philippines filed an appellee's submission.¹⁶ On 15 March 2011, Australia, the European Union, and the United States each filed a third participant's submission¹⁷, and the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu notified its

¹¹Panel Report, para. 8.4(g); see also para. 7.1087. The Panel also found that: (i) Thailand acted inconsistently with Article X:1 of the GATT 1994 by failing to publish the methodology used to determine the MRSP (the tax base for VAT); (ii) Thailand did not act inconsistently with Article X:1 by failing to publish the methodology and data necessary to determine ex factory prices for domestic cigarettes; (iii) Thailand acted inconsistently with Article X:1 of the GATT 1994 by failing to properly publish the general rule pertaining to the release of guarantees; (iv) Thailand did not act inconsistently with Article X:3(a) by appointing certain government officials to the Board of Directors for TTM; (v) Thailand acted inconsistently with Article X:3(a) because of the delays caused in the BoA decision-making process; (vi) the Philippines' claim relating to the administration of That health, excise, and television taxes was improperly brought under Article X:3(a); and (vii) Thailand acted inconsistently with Article X:3(b) by failing to maintain or institute independent review tribunals or processes for the prompt review of customs valuation determinations. (*Ibid.*, para. 8.4(a)-(f); see also paras. 7.791, 7.829, 7.861, 7.929, 7.969, 7.988, and 7.1015) With the exception of the Panel's finding in paragraph 8.4(g)—reproduced above—none of these findings are at issue in this appeal.

¹²Panel Report, para. 8.8.

¹³Panel Report, para. 8.8.

¹⁴WT/DS371/8 (attached as Annex I to this Report).

¹⁵WT/AB/WP/6, 16 August 2010.

¹⁶Pursuant to Rule 22 of the *Working Procedures*.

¹⁷Pursuant to Rule 24(1) of the *Working Procedures*.

intention to appear at the oral hearing as a third participant.¹⁸ On 16 March 2011, China and India each notified its intention to appear at the oral hearing and requested to make an oral statement at the hearing. In accordance with Rule 24(4) of the *Working Procedures*, the Division authorized China, India, and the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu, each to make an oral statement at the hearing.

9. By letter dated 15 March 2011, the Philippines requested, pursuant to Rule 18(5) of the *Working Procedures*, authorization from the Appellate Body Division hearing this appeal to correct a clerical error in its appellee's submission. On 16 March 2011, the Division invited Thailand and the third participants to comment on this request. No comments were received. On 18 March 2011, the Division authorized the Philippines to correct the clerical error in its appellee's submission.

10. The Panel adopted additional working procedures for the protection of business confidential information ("BCI")¹⁹, but we have not done so in this appeal. Neither participant requested that we adopt additional procedures for the protection of BCI in these appellate proceedings, although the Philippines made a conditional request that we consult the participants in the event that we considered it necessary to refer to information that was considered to be BCI in the proceedings before the Panel. We have not found it necessary to refer to any such information in this Report.

11. The oral hearing in this appeal was held on 18 and 19 April 2011. The participants and three of the third participants (Australia, the European Union, and the United States) made oral statements. The participants and third participants responded to questions posed by the Members of the Division hearing the appeal.

II. Arguments of the Participants and the Third Participants

A. Claims of Error by Thailand – Appellant

1. Article III.2 of the GATT 1994

12. Thailand requests the Appellate Body to reverse the Panel's finding that Thailand acted inconsistently with Article III.2, first sentence, of the GATT 1994. Thailand contends that the measures at issue consist of administrative requirements that are not subject to the scope of Article III.2, and that, even if these administrative requirements could be examined under

¹⁸Although the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu indicated that its notification was made pursuant to Rule 24(2) of the *Working Procedures*, the notification was not received before the 17:00 deadline specified in Rule 18(1) of the *Working Procedures*. Accordingly, the Division treated it as a notification and request to make an oral statement at the hearing made pursuant to Rule 24(4) of the *Working Procedures*.

¹⁹See Panel Report, paras. 2.3 and 2.4, and Annex A-1 at pp. 399 and 400.

Article III:2, the Panel erred in finding an inconsistency arising in situations where resellers of imported cigarettes do not satisfy those requirements.

13. Thailand argues that the Panel improperly found a violation of Article III:2 because the Panel's analysis was not based on any difference in the tax burdens imposed on imported and domestic cigarettes, but rather on the regulatory requirements affecting the resale of imported cigarettes and the consequences of non-compliance with those requirements. In Thailand's view, such a difference in regulatory requirements cannot give rise to a violation of Article III:2 and should therefore have been addressed solely under Article III:4.

14. According to Thailand, Article III:2 "imposes a strict standard"²⁰ that internal taxes or internal charges on imported products may not be in excess of those applied to like domestic products. Thus, Article III:2 concerns the actual tax burden, and is essentially a mathematical exercise in which the tax burden on imported and domestic products under the measure at issue is first identified and then compared. In contrast, Article III:4 addresses the non-charge elements of internal legislation, which, in this dispute, consist of administrative requirements.

15. Thailand submits that the difference in how measures are analyzed under Article III:2 and under Article III:4 explains why it is important to maintain the distinction between their scopes. Article III:2 is intended to discipline the tax burdens imposed on imported and domestic products by Members, not how Members regulate their internal markets. Subjecting administrative requirements, or the financial consequences of failing to comply with those requirements, to the scope of Article III:2 will deprive Members of their right under Article III:4 to regulate sales of imported and domestic products differently, so long as the differences do not amount to less favourable treatment of imported products. Thailand further argues that it is well established that a measure that consists of administrative requirements should be analyzed under Article III:4, even if the failure to comply with those administrative requirements may have financial consequences for an imported product. Accordingly, the financial consequences of non-compliance with the administrative requirements of Thailand's VAT regime cannot be treated as separate measures to be analyzed under Article III:2 independently of those administrative requirements.

16. Thailand contends that, in the circumstances of this case, there is "no question of any difference between the actual tax burden"²¹ on imported cigarettes and that on domestic cigarettes. The Panel found that Thailand's VAT rate is seven per cent for both imported and domestic cigarettes, and that the full amount of VAT is collected from both the domestic producer and the importer at the

²⁰Thailand's appellant's submission, para. 55.

²¹Thailand's appellant's submission, para. 73.

time of the initial sale by the domestic producer or importer to the wholesaler. Thus, the Panel's finding was not based on the tax burden under Thai VAT law, but instead solely on the difference in the regulatory requirements for resales of imported and domestic cigarettes and the consequences of failure to comply with those requirements. Such requirements, Thailand contends, "are fundamentally administrative rather than fiscal in nature".²²

17. Thailand objects to the Panel's reliance on the GATT panel report in *US – Tobacco* and to its application of the proposition that a challenged measure is inconsistent with Article III:2 where it carries with it "the risk of discriminatory treatment of imports in respect of internal taxes".²³ Thailand states that it does not disagree that a risk of excess taxation may give rise to a violation of Article III:2, and that a measure that contains an inherent risk of applying a higher tax rate for imported products will be inconsistent with Article III:2. Such risk, however, must relate to the calculation of the tax burden imposed under the measures at issue. The scope of Article III:2 cannot be expanded to include consequences arising out of non-compliance with administrative requirements. In this dispute, the measures at issue do not prescribe a mandatory formula that "mathematically, invariably leads to a specific result concerning the tax rate".²⁴ Moreover, any risk associated with a failure to comply with reporting requirements cannot be equated with an inherent risk of being subject to higher taxation. Thailand maintains that the measures in this dispute *a priori* provide for equal taxation for imported and domestic products.

18. Even if the Panel were correct in examining the consequences of failure to comply with administrative requirements under Article III:2, first sentence, Thailand argues that the Panel's finding of inconsistency was incorrect for two reasons. First, a system of offsetting tax paid against tax collected cannot be said to be inconsistent with Article III:2 simply because private parties are required to comply with certain administrative requirements in order to obtain offsetting credits. Entitlement to a right is not any less "automatic" where parties do not avail themselves of that right. Moreover, the Panel improperly relied on the Appellate Body report in *Korea – Various Measures on Beef* in concluding that "what is relevant in assessing the consistency of a measure with the WTO obligations is whether the concerned measure itself imposes 'the legal necessity' of certain action on private parties".²⁵ In Thailand's view, the Appellate Body did not, in that dispute, suggest that WTO law does not permit Members to require private parties to comply with administrative procedures in order to protect their rights and fulfil their obligations under domestic law.

²²Thailand's appellant's submission, para. 78.

²³Thailand's appellant's submission, para. 80 (quoting Panel Report, para. 7.625, in turn quoting GATT Panel Report, *US – Tobacco*, para. 97 (emphasis added by the Panel)).

²⁴Thailand's appellant's submission, para. 83.

²⁵Thailand's appellant's submission, para. 93 (quoting Panel Report, para. 7.637, in turn quoting Appellate Body Report, *Korea – Various Measures on Beef*, para. 146).

19. Second, Thailand considers that the situations in which a tax credit may be denied involve either instances in which resellers cannot establish that the claimed credit relates to an actual and legitimate purchase of cigarettes, or where the rules do not relate to the purchase and resale of imported products. It cannot be inconsistent with WTO law not to give tax credits on purchases that may not have taken place, to require proof of purchase in order to obtain an input tax credit, or to deny claims based on inaccurate invoices. An analysis of excess taxation for purposes of Article III:2 must involve a comparison of the taxes applied on actual, legitimate, documented sales of imported and domestic products, and WTO Members must be entitled to establish reporting and record-keeping requirements to satisfy themselves that taxes are imposed and collected only with respect to legitimate sales. Yet, Thailand claims, the Panel's finding under Article III:2 implies that it would be required under WTO law to grant input tax credits claimed by resellers even if the resellers cannot prove that the purchases for which the credit was claimed actually took place.

2. Article III:4 of the GATT 1994

20. Thailand requests the Appellate Body to reverse the Panel's finding that Thailand acted inconsistently with Article III:4 of the GATT 1994 by subjecting imported cigarettes to less favourable treatment than that accorded to like domestic cigarettes, through the imposition of additional VAT-related administrative requirements only on resellers of imported cigarettes. Thailand advances three independent grounds for reversal of this finding: (i) that the Panel erred in its application of Article III:4 to the facts of this dispute and in finding that the Thai measures at issue accord less favourable treatment to imported cigarettes; (ii) that the Panel violated Thailand's due process rights, and acted inconsistently with Article 11 of the DSU and paragraph 15 of its Working Procedures, in accepting and relying upon a piece of evidence submitted late in the proceedings by the Philippines; and (iii) that the Panel erred in rejecting Thailand's defence under Article XX(d) of the GATT 1994.

(a) Article III:4: "treatment no less favourable"

21. Thailand submits that the Panel's analysis and findings do not support a finding of less favourable treatment under Article III:4. Under Article III:4, the fact that different regulatory regimes apply to imported and to like domestic products is not determinative of whether imported products are treated less favourably. Members have the right to treat imported products differently and, therefore, to impose additional or more complicated requirements so long as they do not amount to less favourable treatment. The Panel reached its finding without making any factual findings other than to establish the existence of the different requirements themselves. According to Thailand, in this case the Panel simply referred to price elasticity and switching patterns as an indication that the additional

administrative requirements can potentially have a negative impact, and asserted that "an additional administrative burden *can* be linked to the operating costs of [] businesses", which "*could* in turn result in modifying the competitive conditions".²⁶ The Panel's finding was thus based entirely on the theoretical possibility that the differences "*could potentially affect* the competitive position of imported cigarettes in a negative manner".²⁷ Thailand argues that the Panel, therefore, simply identified differences in the regulatory treatment of resales of imported cigarettes and assumed that those differences had the potential to affect negatively the competitive position of such imported products.

22. Thailand points out that the Appellate Body has found that a measure that accords imported products treatment different from that accorded to domestic products "is not necessarily inconsistent with Article III:4, as long as the treatment provided by the measure is 'no less favourable'".²⁸ The Panel's reliance on a "could potentially affect" standard appears to be founded on the Appellate Body's statement in *US – FSC (Article 21.5 – EC)* that an examination of less favourable treatment "need not be based on the *actual effects* of the contested measure in the marketplace".²⁹ The Appellate Body also stated in that case, however, that a determination of less favourable treatment "*cannot rest on simple assertion*, but must be found on a careful analysis of the contested measure and of its implications in the marketplace".³⁰ The Panel appears to have considered it sufficient to identify any conceivable potential negative effect on the competitive position of imports and to find a violation of Article III:4 on that basis. As a result, the Panel made no attempt to identify how or to what extent the minor differences in treatment might in practice increase costs, or how any increase in costs would affect negatively the competitive position of imported cigarettes. Moreover, the Panel failed to account for the gains that resellers of imported cigarettes obtain by virtue of the administrative requirements, such as the possibility to claim additional input tax credits from VAT paid on utilities, administrative expenses, and other services. Thus, in Thailand's view, the Panel "failed to conduct any meaningful analysis of how these differences affect the competitive position of imports".³¹

23. Thailand also rejects the Panel's reliance on several other WTO cases. For instance, Thailand does not understand the Appellate Body to have suggested, in *US – Section 211 Appropriations Act*,

²⁶Thailand's appellant's submission, para. 119 (quoting Panel Report, para. 7.736). (emphasis added by Thailand)

²⁷Thailand's appellant's submission, para. 120. (original emphasis)

²⁸Thailand's appellant's submission, para. 122 (quoting Appellate Body Report, *Korea – Various Measures on Beef*, para. 135; and referring to Appellate Body Report, *EC – Asbestos*, para. 100, and Appellate Body Report, *US – Section 211 Appropriations Act*, para. 261).

²⁹Thailand's appellant's submission, para. 124 (quoting Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 215 (original emphasis)).

³⁰Thailand's appellant's submission, para. 125 (quoting Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 215). (emphasis added by Thailand)

³¹Thailand's appellant's submission, para. 135. (original emphasis)

that all "additional" requirements are "inherently" less favourable. To the contrary, the Appellate Body emphasized that it is permissible to subject imported products to different legal provisions.³² Moreover, the differential treatment in that case involved two entirely separate administrative proceedings, a comparison qualitatively different from the "benign"³³ or "very minor"³⁴ differences in reporting requirements under Thailand's VAT regime. In addition, although the panel in *Canada – Wheat Exports and Grain Imports* stated that practices not very onerous in commercial terms may still be banned when they are likely to put imported products at a competitive disadvantage, Thailand argues that the Panel in this dispute never examined whether such a likelihood in fact exists for imported cigarettes.

(b) Article 11 of the DSU: the Panel's Treatment of Exhibit PHL-289

24. Thailand also contends that the Panel violated Thailand's due process rights and acted inconsistently with Article 11 of the DSU and paragraph 15 of its Working Procedures by accepting and relying on Exhibit PHL-289, which was submitted by the Philippines at the last stage of the proceedings, without affording Thailand the right to comment on such evidence. Because the Panel relied on Exhibit PHL-289 in reaching its findings under Article III:4, Thailand also requests the Appellate Body to reverse the Panel's finding that Thailand acted inconsistently with that provision.

25. Thailand submits that Article 11 of the DSU requires panels to protect the due process rights of each party to a dispute, including the provision of an adequate opportunity to respond to evidence adduced by the other party. However, Thailand was not afforded the opportunity to comment on Exhibit PHL-289, which was submitted by the Philippines in its comments on Thailand's responses to the Panel's questions after the second substantive meeting. The Panel's due process violation is particularly serious because the Panel stated in its Interim Report that it was basing its finding that sales of domestic cigarettes need not be reported in form Por.Por.30 solely on the expert opinion contained in Exhibit PHL-289. Although the Panel deleted this reference from its Report, "Exhibit PHL-289 was still the only evidence referred to in the final report".³⁵ As the panel found in *Korea – Alcoholic Beverages*, the rights of the parties under the DSU may be affected by the importance of the evidence at issue.³⁶ Therefore, since Exhibit PHL-289 was the only evidence upon which the Philippines based its *prima facie* case, Thailand considers that its due process rights with respect to

³²Thailand's appellant's submission, paras. 122 and 137 (referring to Appellate Body Report, *US – Section 211 Appropriations Act*, para. 261).

³³Thailand's appellant's submission, para. 135.

³⁴Thailand's appellant's submission, para. 137.

³⁵Thailand's appellant's submission, para. 169.

³⁶Thailand's appellant's submission, para. 170 (quoting Panel Report, *Korea – Alcoholic Beverages*, para. 10.25).

Exhibit PHL-289 should have been "accorded the highest importance"³⁷, and that Thailand could not have been required to request special leave to respond to Exhibit PHL-289 in order to have its due process rights respected.

26. Thailand also alleges that the Panel's due process violation was "exacerbated"³⁸ by the fact that the Panel did not accord considerable deference to Thailand's interpretation of its own law. This is because, in Thailand's view, where the only evidence suggesting that sales of domestic cigarettes need not be reported in form Por.Por.30 was expert testimony, and Thailand had informed the Panel that these sales had to be reported in that form, the Panel "could have and should have"³⁹ given deference to Thailand's interpretation of its own law.

27. Thailand contends that the Panel's reliance on the Appellate Body's statement in *Argentina – Textiles and Apparel*, that working procedures do not constrain panels with "hard and fast rules on deadlines for submitting evidence", is misplaced for three reasons.⁴⁰ First, a panel's working procedures cannot supersede a panel's due process obligations. Second, the Appellate Body made this finding in respect of the working procedures of the panel in that dispute, which contained deadlines for submitting evidence that were less detailed and clear than those specified in the Working Procedures adopted by the Panel in this dispute. Third, the Panel failed to take into account the Appellate Body's observation that *prima facie* evidence must be submitted during the first procedural stage of the panel proceedings.

28. Thailand also argues that the Panel failed to comply with paragraph 15 of its Working Procedures by accepting and relying upon Exhibit PHL-289. According to Thailand, under Article 12.1 of the DSU, panels are required to comply with working procedures that are adopted in agreement with the parties. Paragraph 15 of the Panel's Working Procedures establishes, as a general rule, that evidence cannot be submitted after the first substantive meeting, and that evidence may be submitted after this deadline only in exceptional circumstances, provided that good cause is shown and the other party is afforded an opportunity to comment.⁴¹ However, the Panel neither rejected

³⁷Thailand's appellant's submission, para. 171.

³⁸Thailand's appellant's submission, para. 173 (referring to Panel Report, *US – Section 301 Trade Act*, para. 7.19).

³⁹Thailand's appellant's submission, para. 173.

⁴⁰Thailand's appellant's submission, para. 176 (quoting Panel Report, para. 6.125, in turn quoting Appellate Body Report, *Argentina – Textiles and Apparel*, paras. 79 and 80).

⁴¹Paragraph 15 of the Panel's Working Procedures provides:

The parties shall submit all factual evidence to the Panel no later than the first substantive meeting, except with respect to factual evidence necessary for purposes of rebuttals, answers to questions or comments on answers provided by each other. Exceptions to this procedure will be granted where good cause is shown. In such cases, the other party shall be accorded a period of time for comment, as appropriate.

Exhibit PHL-289 as untimely, nor accepted it subject to a showing of good cause and the provision to Thailand of an opportunity to comment. Moreover, Exhibit PHL-289 cannot be classified as rebuttal evidence because it was crucial to the Philippines' *prima facie* case, and a piece of evidence cannot be rebuttal evidence and *prima facie* evidence at the same time. Nor could Exhibit PHL-289 be deemed to have been necessary for the Philippines' comments on Thailand's responses to the Panel's questions, since the opportunity to comment on answers provided by the other party is not intended to provide a fresh opportunity to rectify or expand *prima facie* evidence. Thailand adds that there is no reason why the Philippines could not have submitted the expert testimony contained in Exhibit PHL-289 earlier in the proceedings so as to permit Thailand to respond to it.

(c) Thailand's Defence Under Article XX(d) of the GATT 1994

29. Thailand requests the Appellate Body to reverse the Panel's finding that Thailand did not discharge its burden of establishing its defence under Article XX(d) of the GATT 1994 on the grounds that the Panel committed legal error in so finding. Furthermore, because the Panel's failure to conduct the correct legal analysis "effectively deprived Thailand of its right to assert its Article XX(d) defence"⁴², Thailand requests the Appellate Body to reverse the Panel's finding of inconsistency under Article III:4 on the grounds that it is also legally flawed.

30. Thailand contends that the Panel's reasoning in respect of Thailand's defence under Article XX(d) was circular. Before the Panel, Thailand had argued that, even if the additional administrative requirements were found to be inconsistent with Article III:4, those requirements are justified under Article XX(d) because they are necessary to secure compliance with "the obligation to pay VAT" and to "combat smuggling, including tax avoidance by contraband and counterfeit cigarettes".⁴³ Although an essential step in the analysis of an Article XX(d) defence is to identify the laws or regulations with which the measure at issue is asserted to secure compliance, the Panel in this case failed to identify the Thai laws or regulations with which the additional administrative requirements secure compliance. Instead, in paragraph 7.758, the Panel simply referred back to Section VII.F.6(b)(ii) of its Report, where it had found the additional administrative requirements to be inconsistent with Article III:4. Therefore, the Panel erroneously concluded that the additional administrative requirements cannot be justified under Article XX(d) because the same additional administrative requirements had been found to be inconsistent with Article III:4 of the GATT 1994. This circular reasoning led the Panel to commit a fundamental error of legal analysis in its rejection of Thailand's defence under Article XX(d). Thailand adds that, even if the Panel's cross-reference could be rewritten as having intended to be a reference to the Panel's finding under Article III:2, the Panel's

⁴²Thailand's appellant's submission, para. 156.

⁴³Thailand's appellant's submission, para. 151.

analysis under Article XX(d) would remain circular, because that finding was based on the same additional administrative requirements with respect to which Thailand asserted its Article XX(d) defence.

3. Article X:3(b) of the GATT 1994

31. Thailand requests the Appellate Body to reverse the Panel's finding that Thailand acted inconsistently with Article X:3(b) of the GATT 1994 by failing to maintain or institute independent review tribunals or procedures for the prompt review of guarantee decisions. Thailand contends that the Panel erred in concluding that requiring a guarantee in order to obtain the release of goods pending a final determination of customs value is "administrative action relating to customs matters" within the meaning of Article X:3(b). In the event that the Appellate Body rejects this allegation of error, Thailand asserts that providing for a right of appeal of guarantee decisions upon the final assessment of customs duties satisfies Thailand's obligations under Article X:3(b).

32. With respect to the allegation that the Panel erred in finding that guarantee decisions are covered by Article X:3(b), Thailand argues that: (i) the ordinary meaning of the phrase "administrative action relating to customs matters" in Article X:3(b) does not include provisional measures such as customs guarantees; (ii) the context of Article X:3(b) supports the conclusion that the acceptance of guarantees in the sense of Article 13 of the *Agreement on Customs Valuation* does not fall within the scope of "administrative action relating to customs matters"; and (iii) the "object and purpose of the treaty" supports the conclusion that the acceptance of guarantees is not within the scope of Article X:3(b).

33. Thailand submits that the ordinary meaning of the phrase "administrative action relating to customs matters" in Article X:3(b) does not include provisional measures such as customs guarantees for three reasons. First, dictionary definitions of the words making up the phrase "administrative action relating to customs matters" are not dispositive in this case. Because it is inconceivable that all government acts relating to customs matters fall within the scope of Article X:3(b), Thailand maintains that it is necessary to assess the "surrounding circumstances"⁴⁴ in order properly to assess the common intention of the parties.

34. Second, referring to the Panel's statement that "the provisional characteristic of an administrative action or determination [may] render such an action or determination to fall outside the

⁴⁴Thailand's appellant's submission, para. 238 (quoting Appellate Body Report, *EC – Chicken Cuts*, para. 175).

scope of Article X:3(b)⁴⁵, Thailand alleges that the Panel failed properly to analyze whether requiring a guarantee was of such a provisional character. Thailand also refers to the Appellate Body report in *US – Shrimp (Thailand) / US – Customs Bond Directive* in support of the proposition that a security required under the *Ad Note* to paragraphs 2 and 3 of Article VI of the GATT 1994 is an accessory or ancillary obligation. Because the guarantees in the present case are also "provisional" and "accessory or ancillary" to the final duty liability⁴⁶, Thailand submits that they should be regarded as a component of the final determination of customs duties, rather than as distinct decisions.

35. Third, Thailand argues that acceptance of the Panel's view that guarantees fall within the ambit of Article X:3(b) would "result in unduly interfering with"⁴⁷ the customs administration's decision-making process. Because a guarantee is intrinsically linked to the determination of the final customs value, decisions relating to a guarantee are within both the technical expertise and prerogative of the customs administration. Therefore, contends Thailand, allowing a guarantee decision to be challenged before the final duty assessment would curtail the power of the competent official to assess such duty.

36. Thailand further submits that the context of Article X:3(b) supports the conclusion that guarantee decisions do not fall within the scope of Article X:3(b). Specifically, Thailand refers to Article X:1 and Article X:3(a) of the GATT 1994, Articles 11, 12, and 13 of the *Agreement on Customs Valuation*, as well as to Articles 7, 13, and 9.5 of the *Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994* (the "*Anti-Dumping Agreement*") and Articles 2(j) and 3(h) of the *Agreement on Rules of Origin*. For Thailand, these provisions support the conclusion that the guarantee decisions at issue do not fall within the scope of the phrase "administrative action relating to customs matters" in Article X:3(b) of the GATT 1994.

37. With respect to Article X:1 of the GATT 1994, Thailand argues that, while this provision lists several different types of measures, namely, "[l]aws, regulations, judicial decisions and administrative rulings of general application", it contains no reference to guarantees or other securities. This suggests that the drafters did not intend Article X:3(b) to apply to provisional steps such as guarantee decisions. Thailand also refers to Article 13 of the *Agreement on Customs Valuation*, which relates to the possibility for customs to release goods in exchange for a guarantee. Because Article 13 itself does not contain a reference to a right of appeal against the imposition of a guarantee, there is no such right. If the drafters had intended to provide for a right to appeal, "they could and would have said

⁴⁵Thailand's appellant's submission, para. 239 (quoting Panel Report, para. 7.1035).

⁴⁶Thailand's appellant's submission, para. 242.

⁴⁷Thailand's appellant's submission, paras. 245 and 248 (quoting Panel Report, para. 7.1035).

so".⁴⁸ Thailand also refers to Article 11 of the *Agreement on Customs Valuation*, arguing that this Article provides for a right to appeal only with respect to a determination of customs value and that the lack of express provision for an appeal against the taking of a guarantee indicates that the negotiators did not intend to provide for the possibility of such appeal.

38. Thailand also refers to Articles 7, 9.5, and 13 of the *Anti-Dumping Agreement*. For Thailand, the absence of a right to appeal against either provisional measures or "new shipper" guarantees under the *Anti-Dumping Agreement* suggests that guarantees taken to secure payment of customs duties do not fall within the scope of "administrative action relating to customs matters" in Article X:3(b) of the GATT 1994. Thailand also refers to Articles 2(j) and 3(h) of the *Agreement on Rules of Origin*. These provisions stipulate that WTO Members must ensure that "any administrative action which they take in relation to the determination of origin is reviewable promptly by judicial, arbitral, or administrative tribunals or procedures".⁴⁹ Thailand argues that, because the word "any" is used in these provisions of the *Agreement on Rules of Origin* but not in Article X:3(b) of the GATT 1994, certain "administrative action[s]", such as the taking of a guarantee, are not within the scope of Article X:3(b).

39. In addition, Thailand argues that considerations of object and purpose also support the conclusion that the acceptance of guarantees is not within the scope of Article X:3(b). For Thailand, the principle of due process, which the Panel considered to be expressed in Article X:3, does not compel the conclusion that there must be a right of appeal against provisional steps. Procedural due process is not a technical concept with fixed content unrelated to time, place, and circumstance, but must be defined in the light of the particular circumstances of the case.⁵⁰ The doctrine of "ripeness" and deference to the expertise of an administrative agency must also be taken into account.⁵¹ Thailand argues that "it does not make practical sense to require courts to intervene in a decision-making process within the technical expertise of an administrative agency before that agency has had an opportunity to consider the issue fully and issue a final decision."⁵²

40. In the event that the Appellate Body upholds the Panel's finding that requiring a guarantee in order to obtain the release of goods pending a final determination of customs value constitutes "administrative action relating to customs matters", Thailand argues that providing for a right of appeal upon final assessment of duties nonetheless satisfies Thailand's obligations under

⁴⁸Thailand's appellant's submission, para. 256.

⁴⁹Thailand's appellant's submission, para. 272. (emphasis added by Thailand)

⁵⁰Thailand's appellant's submission, para. 277 (quoting United States Supreme Court, *Cafeteria Workers v. McElroy*, 367 U.S. 886, 895 (1961)).

⁵¹Thailand's appellant's submission, para. 278 (referring to United States Supreme Court, *Abbott Laboratories v. Gardner*, 387 U.S. 136 (1967)).

⁵²Thailand's appellant's submission, para. 278.

Article X:3(b). Allowing the challenge of a guarantee before the issuance of the final notice of customs value would unduly interfere with the customs administration's decision-making process in an area within its technical expertise. Thailand submits that this concern can be reconciled with the right of appeal under Article X:3(b) if it were considered to be consistent with that provision to require importers to await the final determination of customs value before exercising their right of appeal in respect of the guarantee. Thailand asserts that this point was acknowledged by the Panel when it stated that it does "not ... consider that the existence of interposing steps prior to an independent review in itself constitutes a systemic flaw that prevents Thailand from maintaining procedures for prompt review of administrative actions under Article X:3(b)".⁵³ Thailand however alleges that the Panel did not explain "why *other* interposing steps might not result in a violation of Article X:3(b) but an interposing step in the form of a requirement to await the final assessment before appealing a guarantee would *always* do so".⁵⁴

B. *Arguments of the Philippines – Appellee*

1. Article III:2 of the GATT 1994

41. The Philippines requests the Appellate Body to uphold the Panel's finding that Thailand acted inconsistently with Article III:2, first sentence, of the GATT 1994. The Philippines contends that the Panel properly based its finding on differences in the levels of taxation that apply to resales of domestic and imported cigarettes resulting from Thailand's *de jure* exemption from VAT liability for resellers of domestic cigarettes. The Philippines also maintains that discriminatory taxation cannot be cured by a right to claim an offsetting tax credit, and that, even if it could, the Panel properly found that resellers of imported cigarettes may be denied a tax credit in defined circumstances under Thai law.

42. The Philippines argues that *de jure* discriminatory taxation between imported and domestic cigarettes constitutes a sufficient basis for a finding of inconsistency under Article III:2. Article III:2 requires that goods shall not be subject to internal taxes in excess of those applied to domestic goods and, as Thailand acknowledges, the first sentence of Article III:2 is violated if imported goods are subject to "even the slightest difference"⁵⁵ in taxation. Moreover, the Philippines argues, *de jure* discrimination arises if it can be demonstrated on the basis of the words of the relevant legislation, regulation, or other legal instrument constituting the measure.

⁵³Thailand's appellant's submission, para. 297 (quoting Panel Report, para. 7.1014).

⁵⁴Thailand's appellant's submission, para. 297. (original emphasis)

⁵⁵Philippines' appellee's submission, para. 58 (referring to Thailand's appellant's submission, footnote 30 to para. 62).

43. The Philippines considers that the Panel correctly found that resales of imported cigarettes are subject to internal taxes in excess of those applicable to resales of domestic cigarettes. Resellers of imported cigarettes are obliged to account fully to Thai fiscal authorities for the VAT liability on taxable resales. The process of securing a tax credit does not mean that resales of imported cigarettes are not subject to tax, but is rather a mechanism for accounting for that tax liability. The Panel also correctly found that, in contrast, resellers of domestic cigarettes are exempt from VAT on resales of cigarettes, and therefore are not subject to any VAT liability. Because resales of imported cigarettes are subject to a tax rate of seven per cent, whereas resales of domestic cigarettes are subject to zero tax, a comparison of the relative tax burdens shows excess taxation based on the origin of the cigarettes. For these reasons, the Philippines maintains that Thailand errs in arguing that the Panel's finding under Article III:2 was based on different administrative requirements, and not on different tax burdens.

44. With respect to Thailand's argument that VAT liability is offset by an input tax credit, the Philippines maintains that, having established that imported cigarettes are subject to VAT in excess of that applicable to like domestic cigarettes, the Panel was not required to examine the legal conditions under which Thailand grants offsetting tax credits. In *Canada – Patent Term*, the Appellate Body rejected the argument that Canada had met its obligation to provide patent protection for 20 years, under Article 33 of the *Agreement on Trade-Related Aspects of Intellectual Property Rights* (the "*TRIPS Agreement*"). In that case, Canada granted a 17-year patent term, which patent holders could extend to 20 years by taking specific procedural action.⁵⁶ Similarly, Article III:2 of the GATT 1994 prevents a Member from making its compliance with the national treatment obligations depend on private party action. *De jure* discrimination cannot be cured by the fact that a private party may take action in an attempt to counteract that discrimination. In the Philippines' view, if a private party fails to take all possible action available to it under a Member's law, the adverse consequences of the private party's lack of action are the responsibility of the Member.

45. The Philippines further submits that the Panel correctly found that resellers of imported cigarettes are not automatically entitled to a tax credit to offset the discriminatory obligation to pay VAT. Thailand admitted before the Panel, and accepts on appeal, that a tax credit is available only if a reseller of imported cigarettes complies with the relevant administrative requirements. In particular, Thailand accepts that a tax credit is not granted if the reseller of imported cigarettes: (i) fails to file form Por.Por.30; (ii) fails to claim a tax credit in form Por.Por.30; (iii) fails to produce an invoice as proof of purchase; and (iv) fails to produce a complete and accurate invoice. Section 82/5 of the Thai

⁵⁶Philippines' appellee's submission, para. 73 (referring to Appellate Body Report, *Canada – Patent Term*, paras. 91 and 92).

Revenue Code⁵⁷ sets forth other circumstances in which a reseller of imported cigarettes can be denied an input tax credit. Accordingly, the Philippines considers that the Panel properly rejected Thailand's argument that a reseller of imported cigarettes can never incur a net liability on the resale of cigarettes, and correctly found that there are circumstances, defined under Thai law, in which a reseller of imported cigarettes would not receive a tax credit.

46. The Philippines also maintains that the Panel properly dismissed Thailand's argument that an inconsistency does not arise under Article III:2 if a reseller of imported cigarettes does not obtain a tax credit due to the reseller's own failure to exercise its right to claim a tax credit. It is the Thai Government, and not a private reseller, that establishes the legal conditions that determine whether a reseller of imported cigarettes is entitled to offset the discriminatory obligation to pay VAT. In contrast, resellers of domestic cigarettes are never required to comply with the tax credit requirements in connection with resales of domestic cigarettes, because they are automatically exempt from VAT on these sales. The Philippines argues that, under Article III of the GATT 1994, it is Thailand, and not a private reseller, that is obliged to ensure that imported cigarettes benefit, in all circumstances, from equality of competitive conditions.

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47. The Philippines takes note of Thailand's argument that it should not be obliged to grant a tax credit to resellers of imported cigarettes if they cannot demonstrate that the claimed credit results from actual and legitimate purchases of cigarettes. This, the Philippines asserts, "is the same argument in another guise".⁵⁸ It is Thailand, and not a private reseller, that is responsible under Article III:2 for establishing a regulatory framework in which imported goods are not subject to taxation in excess of that applied to like domestic cigarettes. This does not imply that Members cannot, as a general matter, insist that taxpayers comply with legal conditions to obtain a tax credit. The reason Thailand's VAT system discriminates, the Philippines submits, is because resales of domestic cigarettes are *de jure* exempt from VAT liability, and are therefore exempt from all requirements relating to tax credits.

2. Article III:4 of the GATT 1994

48. The Philippines requests the Appellate Body to uphold the Panel's finding that Thailand acted inconsistently with Article III:4 of the GATT 1994. The Philippines further requests the Appellate Body to reject Thailand's arguments that the Panel acted inconsistently with Article 11 of the DSU and paragraph 15 of its Working Procedures in accepting the expert opinion contained in Exhibit

⁵⁷Government of the Kingdom of Thailand, The Council of Regency, The Act Promulgating the Revenue Code, B.E. 2481 (Panel Exhibit PHL-94).

⁵⁸Philippines' appellee's submission, para. 86.

PHL-289, as well as Thailand's appeal of the Panel's finding on Thailand's defence under Article XX(d) of the GATT 1994.

(a) Article III:4: "treatment no less favourable"

49. The Philippines contends that the Panel correctly found that Thailand subjects imported cigarettes to less favourable treatment than domestic cigarettes by imposing additional VAT-related administrative requirements only on resellers of imported cigarettes. "Less favourable treatment" within the meaning of Article III:4 is accorded where treatment does not ensure effective equality of opportunities, and does not protect expectations on the competitive relationship between imported and domestic products. Article III:4 requires that government regulation on imported and like domestic products be "perfectly neutral".⁵⁹ The Philippines adds that, when government regulation subjects imported goods to administrative burdens that are not imposed on like domestic goods, this is not neutral, and upsets the equality of competitive conditions.

50. The Philippines considers that the Panel correctly relied on WTO jurisprudence in support of its finding. For instance, the Appellate Body stated in *US – Section 211 Appropriations Act* that "even the possibility that [foreign nationals] face two hurdles is *inherently less favourable* than the undisputed fact that United States [nationals] face only one".⁶⁰ Moreover, the panel in *Canada – Wheat Exports and Grain Imports* found that "less favourable treatment in this case results from the imposition of an *additional requirement on imported grain that does not apply to domestic grain*".⁶¹ Accordingly, to the extent that a Member subjects imported products to administrative requirements to which domestic products are not subject, this gives rise to unequal treatment, which is inherently less favourable for imported products. This is because the additional requirements prevent traders from making a "free choice between like domestic and imported [products] on the basis of purely commercial considerations".⁶² This situation is to be distinguished from one in which different sets of requirements are imposed on imported and domestic products. In such circumstances, the Philippines maintains, a panel may be required to conduct a closer examination of the measures to determine whether the different administrative requirements disturb the effective equality of competitive conditions to the detriment of imported goods and thus constitute less favourable treatment.

⁵⁹Philippines' appellee's submission, para. 123.

⁶⁰Philippines' appellee's submission, para. 125 (quoting Appellate Body Report, *US – Section 211 Appropriations Act*, para. 265 (original emphasis)).

⁶¹Philippines' appellee's submission, para. 126 (quoting Panel Report, *Canada – Wheat Exports and Grain Imports*, para. 6.190). (emphasis added by the Philippines)

⁶²Philippines' appellee's submission, para. 130 (quoting Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 219).

51. The Philippines recalls that the Panel found that Thailand subjects resales of imported cigarettes to a number of VAT administrative requirements and that such requirements do not apply in connection with resales of domestic cigarettes. It follows from this alone that the treatment accorded to imported cigarettes is less favourable, and there is no need to inquire into the "impact of the discriminatory treatment" or the "trade effects" of such treatment.⁶³ Thus, Thailand's appeal, which focuses on, and finds fault with, the Panel's assessment of "the degree of likelihood that any differences in treatment will have any negative impact on the competitive position of imports"⁶⁴, is misplaced. In addition, although it was not required to do so, the Panel sought further confirmation for its finding by examining the ways in which Thailand's discriminatory administrative requirements upset the equality of competitive conditions in the Thai market. The Panel correctly concluded, on the basis of evidence of price elasticity and switching patterns, that the close competitive relationship between imported and domestic cigarettes means that any unequal fiscal treatment is sufficient to disturb the equality of competitive conditions. Moreover, the Panel correctly linked the effects of the additional administrative requirements with the operating costs of businesses, and stated that the costs of compliance with such administrative requirements could affect business decisions and limit opportunities for imported cigarettes. The Philippines considers it noteworthy that more than 20 per cent of cigarette retailers have opted not to sell imported cigarettes. Although there is no evidence as to why they do not resell imported cigarettes, these retailers avoid the administrative requirements by reselling only domestic cigarettes. Regarding Thailand's assertion that, by complying with the additional requirements, resellers of imported cigarettes may obtain certain gains in the form of additional tax credits, the Philippines argues that the fact that the obligation to pay VAT may be offset in some instances "does not cure the *de jure* discrimination".⁶⁵ The Philippines emphasizes that WTO jurisprudence clearly establishes that more favourable treatment of imported products in some instances does not justify less favourable treatment in other instances.

(b) Article 11 of the DSU: the Panel's Treatment of Exhibit PHL-289

52. With respect to the Panel's acceptance of and reliance on Exhibit PHL-289, the Philippines argues that Thailand's due process rights were properly respected by the Panel because Thailand had opportunities to comment on Exhibit PHL-289 and took advantage of one of them. The exercise of due process rights involves responsibilities for the party invoking such rights, and parties should bring

⁶³Philippines' appellee's submission, para. 138.

⁶⁴Philippines' appellee's submission, para. 136 (quoting Thailand's appellant's submission, footnote 115 to para. 124).

⁶⁵Philippines' appellee's submission, para. 150.

alleged procedural deficiencies to a panel's attention at the "earliest possible opportunity".⁶⁶ Although the Philippines submitted the 2000 DG Revenue ruling⁶⁷ at the second substantive meeting, Thailand chose to submit the 1995 DG Revenue ruling⁶⁸ only in its responses to Panel questions after the second substantive meeting. Conversely, the Philippines submitted Exhibit PHL-289 in its comments on those responses, which was the first opportunity after Thailand filed the 1995 DG Revenue ruling. In any event, the Philippines maintains, Thailand was responsible for seeking an opportunity to comment on Exhibit PHL-289, but instead opted to object to this evidence only in its comments on the Panel's Interim Report, where Thailand made largely the same arguments it now raises on appeal.

53. The Philippines also contends that Exhibit PHL-289 was properly submitted before the Panel, in accordance with paragraph 15 of its Working Procedures, because it is rebuttal evidence provided in comments on Thailand's answers to Panel questions. The Philippines asserts that Exhibit PHL-289 was submitted to support the Philippines' comments on the 1995 DG Revenue ruling that had been attached to Thailand's responses to Panel questions. The first sentence of paragraph 15 of the Panel's Working Procedures expressly allows the submission of evidence with comments on the other party's responses to questions. The expert testimony submitted in Exhibit PHL-289 stated that its purpose was to "provide an opinion on [the 1995 DG Revenue ruling]".⁶⁹ Had Thailand not submitted the 1995 DG Revenue ruling, the Philippines would have had no cause to submit this expert testimony. Thus, Exhibit PHL-289 falls within the category of evidence set out in the first sentence of paragraph 15 of the Panel's Working Procedures, as opposed to that set out in the second sentence, for which a showing of good cause and an opportunity to respond is required. At any rate, the Philippines asserts, if Thailand considered that the evidence was not submitted consistently with paragraph 15, the proper course of action for Thailand would have been to object immediately to Exhibit PHL-289, rather than to wait until its comments on the Interim Report.

54. The Philippines argues that the Panel did not give decisive weight to Exhibit PHL-289 and did not act inconsistently with Article 11 of the DSU. Rather, the Panel reached its finding that sales of domestic cigarettes need not be reported in form Por.Por.30 based on the totality of the evidence. Article 11 of the DSU affords panels a "certain margin of discretion" in assessing the credibility and

⁶⁶Philippines' appellee's submission, para. 186 (quoting Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 205, in turn quoting Appellate Body Report, *US – Carbon Steel*, para. 123).

⁶⁷Ruling by the Director-General of the Thai Revenue Department, Gor.Kor. 0811/Por.633, 27 January 2000 (Panel Exhibit PHL-253).

⁶⁸Ruling by the Director-General of the Thai Revenue Department, Gor.Kor. 0802/Por.22836, 10 October 1995 (Panel Exhibit THA-96).

⁶⁹Philippines' appellee's submission, para. 200 (quoting Panel Report, para. 6.127).

weight to be ascribed to a given piece of evidence.⁷⁰ Even in its Interim Report, the Panel did not give decisive weight to Exhibit PHL-289, but simply explained that the expert testimony in Exhibit PHL-289 confirmed the change in the requirement to report sales of domestic cigarettes in form Por.Por.30. The Panel's use of the word "only" to describe the evidence relating to the change in reporting practice was incorrect, and, following a suggestion by the Philippines, the Panel corrected this mistake in the Panel Report. In any case, the Philippines considers that, under Article 17 of the DSU, the Interim Report is not subject to appellate review, and that it is improper for Thailand to base its appeal on the Panel's findings in the Interim Report.

(c) Thailand's Defence Under Article XX(d) of the GATT 1994

55. The Philippines requests the Appellate Body to reject Thailand's appeal of the Panel's finding on Thailand's defence under Article XX(d) of the GATT 1994. The Panel properly concluded that Article XX(d) does not justify one WTO-inconsistent measure (discriminatory administrative requirements on imported cigarettes) on the grounds that it secures compliance with another WTO-inconsistent measure (discriminatory taxation on imported cigarettes). The Philippines also points out that Thailand's arguments with respect to its Article XX(d) defence were not well developed, consisting of a total of six paragraphs in all of its submissions to the Panel.

56. In the view of the Philippines, the cross-reference made by the Panel, in paragraph 7.758 of its Report, is a clerical error rather than, as Thailand claims, a "fundamental"⁷¹ error. There is no basis in the Panel's reasoning to suggest that its substantive examination of Thailand's defence consisted of a circular analysis of whether the administrative requirements are necessary to secure compliance with those same administrative requirements. To the contrary, the Panel properly articulated the legal standard under Article XX(d) as involving two different measures, one to be justified and the other that must be WTO-consistent. The Panel also identified Thailand's argument as being that the "administrative requirements" are necessary to secure compliance "with the Thai VAT laws". The Panel therefore correctly assessed whether the inconsistent measures were necessary to secure compliance with different measures. Thus, the Philippines believes that the Panel's reasoning reveals that the cross-reference in paragraph 7.758 was simply a mistake: the Panel referred to Section VII.F.6(b)(ii) of its Report, which deals with discriminatory administrative requirements, instead of to Section VII.E.5(b)(ii), which deals with discriminatory taxation. Accordingly, the Philippines requests the Appellate Body to modify this clerical error, replacing the reference to

⁷⁰Philippines' appellee's submission, para. 212 (quoting Appellate Body Report, *US – Continued Zeroing*, para. 331, in turn referring to Appellate Body Report, *EC – Hormones*, para. 132, and Appellate Body Report, *EC – Sardines*, para. 299).

⁷¹Philippines' appellee's submission, para. 238 (referring to Thailand's appellant's submission, para. 153).

"Section VII.F.6(b)(ii)" with a reference to "Section VII.E.5(b)(ii)". The Philippines further rejects Thailand's contention that the Panel's analysis under Article XX(d) would remain circular even if the cross-reference were rewritten in this way, because the Panel's finding under Article III:2 of the GATT 1994 was based on the discriminatory obligation to pay VAT, rather than, as Thailand asserts, on the discriminatory administrative requirements with respect to which Thailand advanced its Article XX(d) defence.

57. The Philippines also disagrees with Thailand's contention that, should the Appellate Body reverse the Panel's finding under Article XX(d), it should also reverse the Panel's finding under Article III:4. The interpretation and/or application of a substantive obligation is distinct from an analysis of an exception set out in a separate legal provision, and reversal of a finding under the latter does not entail reversal of a finding under the former. The Philippines also observes that Thailand has not requested the Appellate Body to complete the analysis of its Article XX(d) defence.

3. Article X:3(b) of the GATT 1994

58. The Philippines requests the Appellate Body to uphold the Panel's finding that Thailand acted inconsistently with Article X:3(b) of the GATT 1994 by failing to maintain or institute independent review tribunals or procedures for the prompt review of guarantee decisions. The Philippines argues that the Panel correctly found that requiring a guarantee in order to obtain the release of goods pending a final determination of customs value is "administrative action relating to customs matters" within the meaning of Article X:3(b). The Philippines further submits that the Panel correctly found that providing for independent review of guarantees only following the final determination of customs value does not satisfy Article X:3(b) of the GATT 1994.

59. The Philippines contends that the legal character and purpose of a customs guarantee, the context of Article X:3(b), as well as the object and purpose of Article X:3(b), confirm that guarantee decisions constitute "administrative action relating to customs matters" within the meaning of Article X:3(b). Guarantees involve a process that is related to, but separate from, the customs valuation process. A guarantee decision establishes the legal conditions under which an importer may withdraw its goods from customs, pending the final assessment of the customs value. Thus, the Panel correctly found that a guarantee is a decision that is "intended to serve the distinct purpose of *securing* the payment of the ultimate actual amount of customs duty pending final determination by customs".⁷² For the Philippines, a guarantee is not an integral part of the determination of customs value and does not, as Thailand asserts, constitute a provisional decision regarding customs value.

⁷²Philippines' appellee's submission, para. 287 (quoting Panel Report, para. 7.1040 (original italics; underlining added by the Philippines)).

Instead, it is a final administrative action establishing the definite legal conditions under which the importer may withdraw its goods from customs, and has immediate consequences for importers and market access. As the panel in *Colombia – Ports of Entry* recognized, a guarantee is legally distinct from the payment obligation that it secures.⁷³ While acknowledging the Appellate Body's statement in *US – Shrimp (Thailand) / US – Customs Bond Directive* that a guarantee obligation is "ancillary" and "intrinsically linked to" the obligation it secures⁷⁴, the Philippines argues that this does not mean that the two obligations become an "indistinguishable whole".⁷⁵

60. With respect to the context of Article X:3(b), the Philippines notes that Article 11 of the *Agreement on Customs Valuation* limits independent review to final "determination[s] of customs value", and that Article 13 of the *Anti-Dumping Agreement* limits independent review to "final" anti-dumping determinations. The Panel was correct to conclude that the absence of the word "final" in Article X:3(b) suggests that independent review under Article X:3(b) "is not necessarily confined to final administrative actions".⁷⁶ The Philippines also endorses the Panel's reasoning that the use of the term "customs matters" in Article X:3(b), as opposed to "customs value" in Article 11.1 of the *Agreement on Customs Valuation*, suggests that the scope of Article X:3(b) is broader than that of Article 11.1.

61. The Philippines characterizes as misplaced Thailand's contextual arguments based on Article X:1 of the GATT 1994 and Article 12 of the *Agreement on Customs Valuation*. In response to Thailand's contention that the absence of a reference to guarantee decisions in Article X:1 suggests that Article X:3(b) of the GATT 1994 does not apply to guarantee decisions, the Philippines notes that Thailand has not appealed the Panel's finding that rules relating to guarantees are covered by Article X:1 as rules pertaining to customs valuation. Moreover, the Philippines argues that the absence of a reference to Article X of the GATT 1994 in Article 12 of the *Agreement on Customs Valuation* cannot be read to restrict the obligation to provide for independent review pursuant to Article X:3(b).

62. The Philippines also disagrees with Thailand's contextual arguments based on Article 7.2 and Article 9.5 of the *Anti-Dumping Agreement*. For the Philippines, there is a significant difference

⁷³Philippines' appellee's submission, para. 290 (quoting Panel Report, *Colombia – Ports of Entry*, para. 7.88).

⁷⁴Philippines' appellee's submission, para. 294 (referring to Thailand's appellant's submission, paras. 240-243, in turn quoting Appellate Body Report, *US – Shrimp (Thailand) / US – Customs Bond Directive*, para. 231).

⁷⁵Philippines' appellee's submission, para. 295.

⁷⁶Philippines' appellee's submission, para. 301 (quoting Panel Report, para. 7.1034). (emphasis added by the Philippines)

between provisional anti-dumping measures and guarantees provided pending completion of "new shipper" reviews under the *Anti-Dumping Agreement*, on the one hand, and a customs guarantee, on the other hand. Both a provisional anti-dumping measure and a "new shipper" guarantee can be imposed for only a short period. Once the authority completes the relevant proceeding, the provisional measure or security is automatically removed and replaced by a definitive anti-dumping measure. In contrast, the Philippines maintains, a customs guarantee may be imposed for an indefinite period of time, and thus has the potential of imposing long-term costs on the importer.

63. The Philippines submits that the object and purpose of Article X:3(b) confirms the Panel's conclusion that a customs guarantee is administrative action relating to customs matters falling within the scope of Article X:3(b). The Panel was correct in stating that the underlying objective of Article X:3(b) is the preservation of due process rights for affected parties, and in finding that a guarantee decision can cause an immediate commercially adverse impact on importers if the level of a guarantee is excessive. The Philippines disagrees with Thailand that, because customs guarantee decisions are only provisional measures, they are not "ripe" for independent review, and that courts should therefore not intervene in a decision-making process that falls within the technical expertise of an administrative agency. Thailand itself has illustrated, in another dispute, the importance of permitting a challenge to a guarantee decision for due process reasons, when it successfully challenged in WTO dispute settlement a guarantee imposed by the United States to cover potential liability for definitive anti-dumping duties.⁷⁷ There was no suggestion in that case that such review prejudiced or unduly interfered with the ability of the United States Department of Commerce to assess final anti-dumping duties. The Philippines adds that, irrespective of the level of a guarantee or the basis for its determination, customs authorities are required to determine the customs value consistently with the relevant provisions of the *Agreement on Customs Valuation*, and that customs law is not so complex and difficult that governmental actions must be immune from scrutiny by independent tribunals. By interpreting Article X:3(b) to encompass customs guarantees, the Panel ensured that importers are entitled to seek independent review to contest the amount of a guarantee, thereby preserving the competitive opportunities that Article X of the GATT 1994 protects.

64. Finally, the Philippines takes issue with Thailand's conditional appeal requesting that, if a guarantee decision is considered to be an "administrative action relating to customs matters", the Appellate Body find that the provision of a right of appeal upon final assessment of customs duties nonetheless satisfies Thailand's obligations under Article X:3(b). Under Thai law, no independent tribunal enjoys jurisdiction to hear a challenge to a guarantee decision separately from the appeal of a

⁷⁷Philippines' appellee's submission, para. 319 (referring to Appellate Body Report, *US – Shrimp (Thailand) / US – Customs Bond Directive*, paras. 258-260).

final assessment of customs value. The Panel was correct to find that permitting review of guarantee decisions only after the final determination of customs value has been issued does not comply with Article X:3(b). Such a system is not a system for the prompt review and correction of guarantee decisions, but only a system of review of customs valuation determinations. If an importer decides not to import goods because a guarantee imposes too great a financial burden, there would never be a final determination of customs value, and it would thus be impossible for an importer to obtain independent review of a guarantee decision. Even in situations in which importation occurs and a final customs valuation determination is made, the requirement to await that determination before pursuing independent review of a guarantee results in unnecessary delays.

65. The Philippines disagrees with Thailand's argument that, since the Panel found that it is, in principle, acceptable under Article X:3(b) to require that importers pursue internal review before seeking independent review of a customs valuation determination, it must also be permissible to compel importers to await a final customs value determination before seeking independent review of a guarantee decision. A requirement first to seek internal review of a customs valuation determination does not create a lacuna in the review system, thereby making independent review of a final determination impossible in certain situations. In contrast, requiring importers to await a final customs value determination before seeking independent review of a guarantee decision does give rise to such a lacuna. In addition, the Philippines contends that, while internal review of a customs valuation determination may contribute to the resolution of the valuation issue, waiting for the issuance of the final customs value determination does not contribute to the prompt review and correction of a guarantee decision.

C. *Arguments of the Third Participants*

1. Australia

66. Australia submits that, in examining Thailand's appeal under Article III:2 of the GATT 1994, the Appellate Body must first examine the threshold issue of whether the Panel correctly identified the measure at issue. Australia considers that the Panel was unclear as to whether this was the VAT scheme *per se*, or whether the measure comprises the mechanisms used to collect the VAT. Australia considers it difficult to separate each component of Thailand's VAT regime, and observes that whether a sale of a product is exempt from VAT, or whether a reseller may apply for input tax credits to relieve itself of the tax burden, is relevant and indistinguishable from the tax regime itself.

67. Referring to the reasoning of the panel in *Argentina – Hides and Leather*, and the GATT panel in *US – Malt Beverages*, Australia submits that the administrative nature of Thailand's tax

collection mechanism does not mean *a priori* that it falls outside the scope of the first sentence of Article III:2 of the GATT 1994. In the circumstances of this case, the administrative requirements are a collection mechanism that affects the calculation of the cumulative VAT burden. The non-fulfilment of the administrative requirements for resellers of imported cigarettes directly results in a higher tax burden, whereas resellers of domestic cigarettes are fully exempt from paying VAT. Accordingly, the collection mechanism itself constitutes a "tax" for the purposes of Article III:2 as it potentially results in a higher cumulative tax burden on the reseller of imported cigarettes. As for whether the tax burden on imported cigarettes is "in excess" of that on domestic cigarettes, Australia submits that the additional administrative requirements applicable to resellers of imported cigarettes, and the inherent risk of a higher tax burden if these requirements are not met, should be taken into account. Noting Thailand's acknowledgment that "a risk of excess taxation may give rise to a violation of Article III:2"⁷⁸, Australia points out that, when a claim for input tax credit by a reseller is rejected, the actual tax burden is higher, whereas this risk is not faced by resellers of domestic cigarettes, which are automatically exempt from VAT.

68. With respect to Thailand's arguments that the Panel erred in finding that the additional administrative requirements accord "less favourable treatment" within the meaning of Article III:4 of the GATT 1994, Australia disagrees with Thailand's contention that "the right to treat imported products differently may include the right to impose additional or more complicated requirements so long as they do not amount to 'less favourable' treatment".⁷⁹ Rather, panels and the Appellate Body have found merely that different treatment is not sufficient for a finding of inconsistency with Article III:4. While emphasizing that any determination of less favourable treatment must be made on a case-by-case basis, Australia requests the Appellate Body to take account of the broader systemic implications of the threshold for a finding of inconsistency under Article III:4. For Australia, the Panel's finding of less favourable treatment based on its view that the measures "could potentially affect", or "may potentially modify", the conditions of competition seems to imply a lower threshold than that used by the panels in *China – Publications and Audiovisual Products* ("may reasonably be expected")⁸⁰ and *India – Autos* ("is more than likely").⁸¹

69. Regarding Thailand's appeal under Article XX(d) of the GATT 1994, Australia expresses concern that the Panel failed to identify clearly both the GATT-inconsistent measure and the "laws or

⁷⁸ Australia's third participant's submission, para. 19 (quoting Thailand's appellant's submission, para. 81).

⁷⁹ Australia's third participant's submission, para. 24 (quoting Thailand's appellant's submission, para. 129) (underlining added by Australia)

⁸⁰ Australia's third participant's submission, para. 26 (quoting Panel Report, *China – Publications and Audiovisual Products*, para. 7.1471).

⁸¹ Australia's third participant's submission, para. 27 (quoting Panel Report, *India – Autos*, para. 7.201).

regulations" with which the GATT-inconsistent measure secures compliance. This apparent failure "compromised [the Panel's] ability to consider the [Article XX(d) defence]"⁸². The Panel should have considered whether the administrative mechanism for the implementation of VAT was designed to secure compliance with Thailand's VAT regime. In Australia's view, the design of that measure appears, at least in part, to secure such compliance. Moreover, in determining whether the measure is "necessary", consideration should have been given to the range of possible alternative measures that could secure compliance with Thailand's VAT regime. Australia notes, in this regard, the Philippines' argument before the Panel that Article XX(d) cannot justify "both the VAT-related administrative requirements imposed on resellers of imported cigarettes and the exemption accorded to resellers of domestic cigarettes"⁸³.

70. Australia supports Thailand's view that the acceptance of a guarantee is a provisional decision that does not fall within the scope of Article X:3(b) of the GATT 1994. Guarantees are interlocutory decisions made pending a final customs valuation determination, and are difficult to distinguish from that final determination. In the absence of an express reference to a right to appeal at an interlocutory stage, no such right should be read into Article X:3(b). Noting the Panel's statement that it could "think of a situation where the provisional characteristics of an administrative action or determination would render such an action or determination to fall outside the scope of Article X:3(b)", Australia argues that the Panel then failed to consider whether the acceptance of guarantees for the payment of customs duties may be such a situation.⁸⁴ Requiring external review of a provisional decision to accept a guarantee could effectively pre-empt and interfere with the final customs valuation determination to be taken by the relevant domestic agency. Australia submits that, so long as the right to appeal the final determination is capable of overturning any stage of the process, then there should be no right of appeal of individual, interlocutory stages in that process unless such a right is expressly provided for, which is not the case under Article X:3(b).

2. European Union

71. With respect to Thailand's appeal under Article III:2 of the GATT 1994, the European Union understands the measure at issue to consist of the VAT exemption on the resale of domestic cigarettes, as compared to the additional administrative requirements that are imposed on imported cigarettes in order to obtain the same level of tax burden. The European Union considers that there is a *de jure* violation of Article III:2 of the GATT 1994 when, for domestic products only, an automatic exemption from VAT is embedded in the design and structure of the measure, but the same automatic

⁸² Australia's third participant's submission, para. 32.

⁸³ Australia's third participant's submission, para. 35. (original underlining)

⁸⁴ Australia's third participant's submission, para. 39 (quoting Panel Report, para. 7.1035).

result is not granted with respect to imported products. The European Union disagrees with Thailand that, in order to be found inconsistent with Article III:2, first sentence, a measure needs to lead to a higher tax rate for imported products. Rather, as the panel stated in *Argentina – Hides and Leather*, the "tax burden" need not be the tax itself, but can also be derived from "aspects of broader tax systems" that are covered by the disciplines of Article III:2.⁸⁵ The European Union adds that the use of the term "indirectly" in Article III:2 supports the view that the scope of this provision includes situations, like the present case, where the measure at issue contains elements that adversely affect only imported products, by increasing their overall tax burden, as compared to domestic products.

72. The European Union also disagrees with Thailand's contention that the analysis of a measure under the first sentence of Article III:2 must consist of a mathematical exercise. Such a narrow interpretation would give WTO Members the possibility to circumvent the norm of Article III:2. Moreover, it is not appropriate to draw a distinction between "substantive" tax measures, such as the tax rate, and "measures of tax administration", such as the measures at issue in the present case. The European Union insists that a tax burden can also be of a non-mathematical nature.

73. The European Union observes that Thailand's appeal under Article III:4 of the GATT 1994 appears to raise the issue of whether, in an analysis under that provision, panels must engage in a detailed analysis in order to establish that the measure at issue *will* affect the competitive position of imported cigarettes in a negative manner, or whether an analysis based on the possibility that the measure at issue *could* affect the competitive position of imported cigarettes can suffice to find an inconsistency. The Appellate Body has stated that, in establishing inconsistency with Article III:4, the actual effects of a measure in the marketplace need not be shown. Instead, it is sufficient to show that "such a measure is likely to lead to that result".⁸⁶ Previous measures have also been found to be inconsistent with Article III:4 when they create a mere "incentive"⁸⁷ to favour domestic products, or "may be reasonably expected"⁸⁸ to modify the conditions of competition. Accordingly, it seems to be sufficient for a panel to determine on the basis of the available elements of fact that the measure will *probably* negatively affect the conditions of competition. Without expressing a view on the Panel's finding under Article III:4, the European Union encourages the Appellate Body to review that finding in accordance with this case law, and to consider the extent to which the facts before the Panel (that is, the accumulation of all the requirements imposed on the resellers of imported cigarettes) allow a

⁸⁵ European Union's third participant's submission, para. 18 (quoting Panel Report, *Argentina – Hides and Leather*, footnote 449 to para. 11.152).

⁸⁶ European Union's third participant's submission, para. 27 (referring to Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 215).

⁸⁷ European Union's third participant's submission, para. 28 (referring to Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 212; and Panel Report, *India – Autos*, paras. 7.195-7.198 and 7.201).

⁸⁸ European Union's third participant's submission, para. 29 (referring to Panel Report, *China – Publications and Audiovisual Products*, para. 7.1471).

reasonable expectation, or, in other words, lend credence to the conclusion, that the imported products will be treated less favourably.

74. Concerning Thailand's appeal in respect of the Panel's acceptance of Exhibit PHL-289, the European Union submits that the first issue that the Appellate Body needs to resolve is whether Exhibit PHL-289 is rebuttal evidence or not. If it is not, then the Panel infringed its Working Procedures by admitting this item of untimely evidence without requiring good cause and without affording Thailand the right to comment thereon. Article 11 of the DSU requires panels actively to respect parties' due process rights. Thus, if the Panel accepted and relied upon Exhibit PHL-289 contrary to its Working Procedures, it should, at a minimum, have afforded Thailand an opportunity to comment. If the Panel failed to do so, then this defect cannot be cured by arguing that such an opportunity was provided during interim review. The Appellate Body need not address the content of the Interim Report since the issue on appeal is whether the Panel's finding in its Report that VAT registrants need not report resales of domestic cigarettes in form Por.30 was based exclusively on Exhibit PHL-289. Finally, the European Union observes that, even if the Appellate Body agrees with Thailand regarding the Panel's treatment of Exhibit PHL-289, Thailand bears the burden of explaining why and how the ultimate finding made by the Panel under Article III:4 was fully dependent on the Panel's factual finding regarding the reporting of resales of domestic cigarettes in form Por.30.

75. Regarding Thailand's appeal under Article XX(d) of the GATT 1994, the European Union considers the relevant question to be whether the measure at issue secures compliance with other laws or regulations which are not WTO-inconsistent. The measure at issue in this dispute is the different treatment applied to imported cigarettes versus domestic cigarettes, that is, the additional administrative requirements imposed on imported cigarettes. The laws or regulations with which the measure at issue aims to secure compliance are Thailand's VAT laws. Since the GATT-inconsistent measure at issue is part of the VAT regime, the European Union considers that the Panel properly concluded that the laws or regulations with which the measure at issue secures compliance, namely, the laws comprising the Thai VAT regime, are also WTO-inconsistent.

76. The European Union submits that the Panel correctly found that decisions on the imposition of guarantees pursuant to Article 13 of the *Agreement on Customs Valuation* fall within the scope of "administrative action relating to customs matters" in Article X:3(b) of the GATT 1994. The characterization of an action as "provisional" or "final" is not crucial to bring that action within the scope of Article X:3(b). Rather, the key issue is whether the administrative action at issue has a direct and individual material effect on the importer. The European Union contends that neither the text of Article X:3(b), nor that of the other paragraphs of Article X, make a distinction between "provisional"

and "final" administrative actions. This contrasts with other provisions in the GATT 1994, such as Article XV:2, which explicitly refer to "final" measures. The European Union also agrees with the Panel's reasoning that the due process objective underlying Article X:3(b) supports an interpretation of the term "administrative action" that is not limited to final administrative determinations.

77. Furthermore, the European Union views the imposition of a guarantee as being separate and distinct from a customs value determination. Like a determination of the value of imported goods, the imposition of a guarantee is one component of the imposition and collection of customs duties. However, imposing a guarantee is not a component of determining the customs value. Instead, it is a separate and distinct action, constituting "administrative action" in the sense of Article X:3(b). The European Union also disputes Thailand's assertion that the imposition of a guarantee cannot be reviewed effectively without knowing the final duty liability, as well as Thailand's reliance upon the Appellate Body report in *US – Shrimp (Thailand) / US – Customs Bond Directive*. The Appellate Body did not, in that dispute, rule out that, under certain circumstances, a guarantee could constitute "specific action against dumping" pursuant to Article 17.4 of the *Anti-Dumping Agreement*.⁸⁹ In the view of the European Union, the same reasoning supports the view that a guarantee pursuant to Article 13 of the *Agreement on Customs Valuation* may constitute "administrative action relating to customs matters" within the meaning of Article X:3(b) of the GATT 1994.

78. Finally, in the event that the Appellate Body upholds the Panel's finding that the acceptance of a guarantee under Article 13 of the *Agreement on Customs Valuation* constitutes an "administrative action relating to customs matters" within the meaning of Article X:3(b) of the GATT 1994, the European Union considers that a system which requires a final customs value determination in order to appeal the imposition of a guarantee is contrary to Article X:3(b). Thailand's concerns about an appeal of a guarantee interfering with the customs administration's decision-making process are unfounded. Courts are in a position fully to review customs authorities' decisions. Furthermore, courts may not need to review the final customs value determination, but could limit their analysis to reviewing the basis for establishing the amount of the guarantee, thus not interfering with the customs administration's decision-making process. The European Union adds that, once the final customs value is established, an appeal against the imposition of a guarantee becomes irrelevant because the guarantee effectively ceases to exist.

⁸⁹European Union's third participant's submission, para. 64 (referring to Appellate Body Report, *US – Shrimp (Thailand) / US – Customs Bond Directive*, paras. 230 and 231).

3. United States

79. With respect to Thailand's appeal of the Panel's finding of less favourable treatment under Article III:4 of the GATT 1994, the United States argues that, while a complainant need not demonstrate the actual trade impact of a measure, it must establish that the measure modifies the conditions of competition for imported products. The United States questions whether mere risk that a change to the conditions of competition might occur would fulfil that requirement, given that a finding of less favourable treatment cannot be based on mere assertion or speculation.⁹⁰

80. As regards Thailand's appeal concerning the Panel's treatment of Exhibit PHL-289, the United States observes that the Panel's Working Procedures expressly allowed for the submission of factual evidence, even after the first substantive meeting, for the purposes of rebuttals, answers to questions, or comments on answers to questions. The United States takes no view on whether the evidence at issue can properly be considered to have been submitted for these purposes. In any event, while it could have done so, the Panel was not required as a matter of due process to offer Thailand an opportunity to comment on Exhibit PHL-289. Furthermore, Thailand did in fact respond to the evidence as part of the interim review, and the Panel took Thailand's response into account in its evaluation of the evidence. Accordingly, it is not clear to the United States what due process right of Thailand was not respected. The United States also recalls that Article 11 of the DSU affords panels a degree of discretion regarding the treatment of evidence, and that working procedures "do not constrain panels with hard and fast rules on deadlines for submitting evidence".⁹¹

81. The United States takes no position on whether Thailand has acted inconsistently with the obligations of Article X:3(b) of the GATT 1994. The United States observes, however, that the Panel did not accept Thailand's categorization of "provisional" versus "non-provisional" customs measures, and thus did not make a broad finding about such classes of measures, nor seek to define the precise types of measures falling within the scope of Article X:3(b). Instead, the United States maintains, the Panel properly examined whether the guarantees at issue constitute "administrative action relating to customs matters", and, if so, whether Thailand failed to provide for the prompt review and correction of such action. This is the same question that is presented on appeal. The United States further considers that, contrary to Thailand's arguments on appeal, neither the Appellate Body report in *US – Shrimp (Thailand) / US – Customs Bond Directive*, nor the provisions of the *Agreement on Customs Valuation* or the *Anti-Dumping Agreement*, are relevant in answering this question. With respect to the issue of whether a measure satisfies the obligation to provide for "prompt review and

⁹⁰United States' closing statement at the oral hearing.

⁹¹United States' opening statement at the oral hearing (quoting Appellate Body Report, *Argentina – Textiles and Apparel*, para. 80).

correction", the United States agrees with both Thailand and the Panel that such an evaluation requires a case-by-case analysis, and with the Panel that what it means for action to be taken "promptly" will depend on the factual context of the specific measure at issue in a dispute.

III. Issues Raised in This Appeal

82. The following issues are raised in this appeal:

- (a) With respect to the Panel's findings under Article III of the GATT 1994 concerning Thailand's treatment of resellers of imported cigarettes, as compared to its treatment of resellers of like domestic cigarettes:
- (i) whether the Panel erred in finding that Thailand acts inconsistently with Article III:2, first sentence, of the GATT 1994 by subjecting imported cigarettes to value added tax ("VAT") liability in excess of that applied to like domestic cigarettes;
 - (ii) whether the Panel erred in finding that Thailand acts inconsistently with Article III:4 of the GATT 1994, and, in particular:
 - whether the Panel erred in finding that Thailand accords less favourable treatment to imported cigarettes than to like domestic cigarettes;
 - whether the Panel failed to ensure due process and, thus, to comply with its duty under Article 11 of the DSU to make an objective assessment of the matter, by accepting and relying on Exhibit PHL-289 without affording Thailand an opportunity to comment on that evidence; and
 - whether the Panel erred in rejecting Thailand's defence under Article XX(d) of the GATT 1994 to the Panel's finding of inconsistency under Article III:4; and
- (b) Whether the Panel erred in its interpretation and application of Article X:3(b) of the GATT 1994 in finding that Thailand acts inconsistently with its obligation, under that provision, to maintain or institute independent tribunals or procedures for the prompt review of guarantee decisions.

IV. Article III of the GATT 1994

A. Introduction

83. The Philippines alleged before the Panel that Thai law discriminates between resellers of imported cigarettes and resellers of domestic cigarettes in a manner inconsistent with Article III:2 and Article III:4 of the GATT 1994. According to the Philippines, Thailand acts inconsistently with Article III:2, first sentence, because Thailand imposes VAT liability on imported cigarettes in excess of that applied to like domestic cigarettes through an exemption from VAT for resales of domestic cigarettes.⁹² The Philippines also claimed that Thailand acts inconsistently with Article III:4 because its VAT system accords less favourable treatment to imported cigarettes by imposing more onerous administrative requirements on resellers of imported cigarettes than on resellers of like domestic cigarettes.

84. In respect of both claims, the Panel found in favour of the Philippines⁹³, and Thailand appeals those findings. Before examining Thailand's appeal, we describe relevant aspects of Thailand's VAT regime, and identify the measures that the Panel found to be inconsistent with Article III:2 and Article III:4, respectively, of the GATT 1994.

B. Overview of the Measures at Issue

1. The Measure Challenged Under Article III:2 of the GATT 1994

85. For purposes of the Philippines' claim under Article III:2 of the GATT 1994, the Panel considered various provisions of Thailand's VAT regime.⁹⁴

86. Thailand administers VAT pursuant to Chapter IV of the Act Promulgating the Revenue Code⁹⁵ (the "Thai Revenue Code").⁹⁶ The Thai Revenue Code provides that, as a general rule, every

⁹²The Philippines also claimed that, in the determination of the tax base for imported cigarettes, Thailand acts inconsistently with Article III:2, first sentence, of the GATT 1994 by subjecting imported cigarettes to VAT liability in excess of that applied to like domestic cigarettes. The Panel found in favour of the Philippines in respect of this claim, and Thailand has not appealed this finding. (Panel Report, para. 8.3(a))

⁹³Panel Report, para. 8.3(b) and (c).

⁹⁴The Panel stated that the Thai measures specifically identified in the Philippines' panel request are "Sections 81 and 82/7 of the Thai Revenue Code, Section 3(1) of Royal Decree No. 239, and Order of Revenue Department No. Por. 85/2542". The Panel explained that in the course of the dispute the parties also referred to other provisions pertaining to the imposition of, and exemption from, VAT liability. (Panel Report, para. 7.572)

⁹⁵Government of the Kingdom of Thailand, The Council of Regency, The Act Promulgating the Revenue Code, B.E. 2481 (Panel Exhibit PHL-94).

⁹⁶Panel Report, para. 7.573 (referring to Chapter IV, "Value Added Tax", consisting of Sections 77-90 of the Thai Revenue Code).

VAT registrant⁹⁷ in the distribution chain for a product incurs liability in respect of VAT.⁹⁸ The VAT rate generally applicable to sales of products in Thailand is seven per cent *ad valorem*.⁹⁹ For most products, VAT is determined by applying this rate to the actual selling price of the product at each stage of the supply chain.¹⁰⁰ VAT must be reported on a monthly basis in tax form Por.30.¹⁰¹ Pursuant to Section 82/3 of the Thai Revenue Code, in each tax month sellers are entitled to deduct the "input tax", paid upon purchase of the goods from the previous seller, from the "output tax" collected from the next purchaser of the goods.¹⁰² VAT liability under Thai law in respect of a sales transaction thus consists of the amount to be paid after subtracting input tax from output tax.¹⁰³ When output tax exceeds input tax, the tax payable is equal to the difference between the two. When input tax exceeds output tax, the difference is treated as a tax credit, and the seller is entitled to receive a tax refund or to apply that credit in future VAT assessments.¹⁰⁴

87. With respect to sales of cigarettes, however, Thailand's VAT system operates differently in two main respects. First, instead of applying the tax rate against the actual sales price, VAT is determined for each stage of the supply chain for cigarettes, starting with the first sale of cigarettes in Thailand by Thailand Tobacco Monopoly ("TTM") or an importer, by applying the seven per cent rate to the maximum retail selling price ("MRSP"), a reference price fixed by the Thai Government for each brand of cigarettes.¹⁰⁵ This means that, because VAT is based on the same fixed price at each stage of the supply chain, the amount of VAT assessed is the same for each sales transaction along that chain. Moreover, because the VAT paid by a reseller of cigarettes to a prior seller in the form of input tax is the same as the amount that the reseller collects from a subsequent purchaser in the form of output tax, these amounts will, subject to compliance with certain administrative requirements, be offset, resulting in a VAT liability of zero.

88. Second, Thai law provides for an exemption from VAT for all sales of domestic cigarettes by resellers in the distribution chain for domestic cigarettes. Thus, resellers of domestic cigarettes incur

⁹⁷VAT obligations under the Thai Revenue Code apply to VAT registrants. Section 85 of the Thai Revenue Code requires that all sellers file an application for VAT registration before commencing a business of selling goods or providing services. Section 81 of the Thai Revenue Code exempts from VAT registration businesses engaged in sales only of VAT-exempt goods, and businesses with annual sales of less than 1.8 million baht. (Panel Report, paras. 7.687-7.689 and footnote 1243 thereto)

⁹⁸Panel Report, paras. 7.574 and 7.580 (referring to, *inter alia*, Thai Revenue Code, Section 82 and Section 82/3).

⁹⁹Panel Report, para. 7.457.

¹⁰⁰Panel Report, footnote 947 to para. 7.460.

¹⁰¹Panel Report, paras. 7.634 and 7.652.

¹⁰²Panel Report, para. 7.579.

¹⁰³Panel Report, paras. 7.580 and 7.628.

¹⁰⁴Panel Report, para. 7.581.

¹⁰⁵Panel Report, para. 7.460 and footnote 947 thereto, and paras. 7.577 and 7.578 (referring to Thai Revenue Code, Section 79/5 and Section 82/7). Although cigarettes cannot be sold at prices exceeding the MRSP, they may be sold at prices below the MRSP. (*Ibid.*, para. 7.463)

no VAT liability because of an exemption provided pursuant to Section 81(1)(v) of the Thai Revenue Code, Section 3(1) of Thailand's Royal Decree issued under the Thai Revenue Code¹⁰⁶ ("Royal Decree No. 239"), and Thailand's Order of Revenue Department No. Por. 85/2542¹⁰⁷ ("Order No. Por. 85/2542").¹⁰⁸

89. Section 81(1)(v) of the Thai Revenue Code provides:

Section 81. There shall be exempt from value added tax the following transactions:

(1) Sale of goods not for export or provision of services as follows:

...
(v) Sale of goods or provision of services designated by a Royal Decree.¹⁰⁹ (footnote omitted)

90. Section 3(1) of Royal Decree No. 239 provides:

Section 3. There shall be exempt from value added tax for the following businesses:

(1) Sale of cigarettes produced by a manufacturer which is an organization of a government where the seller is not such manufacturer who produces such cigarettes ...¹¹⁰

91. As the Panel explained, because TTM is the only manufacturer of cigarettes in Thailand, and an organization of the Thai Government, these provisions exempt resellers of TTM brand cigarettes from VAT.¹¹¹ The Panel thus concluded that, in respect of sales of domestic cigarettes, TTM is subject to VAT, whereas resellers of domestic cigarettes are not.¹¹²

¹⁰⁶Government of the Kingdom of Thailand, Royal Decree Issued Under the Revenue Code Governing Exemption from Value Added Tax (No. 239) B.E. 2534 (Panel Exhibit PHL-217).

¹⁰⁷Government of the Kingdom of Thailand, Order of Revenue Department No. Por. 85/2542, Re Computation of Tax Base for Importation and Sale of Tobacco According to Category and Type Prescribed by Director-General and Approved by Minister under Section 79/5 of Revenue Code, and Preparation of Tax Invoice in Case of Sale of Tobacco under Section 86/5(2) of Revenue Code (Panel Exhibit PHL-95).

¹⁰⁸Panel Report, para. 7.591.

¹⁰⁹See Panel Report, para. 7.584.

¹¹⁰Panel Report, para. 7.585.

¹¹¹Panel Report, para. 7.585. Order No. Por. 85/2542 also confirms that, with respect to the first purchaser of cigarettes from TTM, there is an exemption from VAT in accordance with Section 81(1)(v) of the Thai Revenue Code. (*Ibid.*, para. 7.586)

¹¹²Panel Report, paras. 7.590 and 7.591.

92. In respect of imported cigarettes, the Panel stated:

No such exemption is available for imported cigarettes. As such, when the wholesaler subsequently resells imported cigarettes to the retailer, for example, the wholesaler incurs a VAT liability of 7 per cent of the MRSP. This VAT liability arises at each subsequent transactional stage until consumers purchase imported cigarettes. Each agent subject to VAT in the imported cigarettes distribution chain can claim a refund of the VAT amounts paid in excess, based on the amount of VAT credits acquired upon the purchase of cigarettes from a previous seller, by filing form Por.Por.30 with the Thai authorities.¹¹³ (footnote omitted)

93. Finally, the Panel referred to certain "[o]ther relevant provisions" that it examined, including Section 82/5 of the Thai Revenue Code, which sets out instances in which VAT registrants are not allowed to deduct input tax in computing tax liability under Section 82/3.¹¹⁴ Section 82/5 provides for the denial of a tax credit in the following six instances:

(i) a tax invoice is absent or cannot be produced to prove that input tax has been collected, except where there is a reasonable excuse according to the rules and conditions prescribed by the Director-General;

(ii) a tax invoice contains information which is incorrect or inadequate in the matter of substance according to the rules and conditions prescribed by the Director-General;

(iii) the input tax is not directly connected with the business carried on by a supplier according to the rules and conditions prescribed by the Director-General;

(iv) the input tax originated from entertainment expenses or expenses of a similar nature according to the rules and conditions prescribed by the Director-General;

(v) input tax under a tax invoice issued by a person not authorized to do so under Division 10; or

(vi) input tax designated by the Director-General with the approval of the Minister.¹¹⁵

94. In sum, in evaluating the Philippines' Article III:2 claim in respect of resellers of cigarettes, the Panel considered several provisions under Thai law collectively. The Panel first identified that resellers of imported cigarettes are liable for VAT under Section 82/7 of the Thai Revenue Code, and that resellers of domestic cigarettes are exempt from VAT liability pursuant to Section 81(1)(v) of the

¹¹³Panel Report, para. 7.591.

¹¹⁴Panel Report, subheading VII.E.3(d) and para. 7.593.

¹¹⁵Panel Report, para. 7.593.

Thai Revenue Code, Section 3(1) of Royal Decree No. 239, and Order No. Por. 85/2542.¹¹⁶ Recognizing that VAT liability consists of output tax minus input tax¹¹⁷, the Panel then proceeded to evaluate whether an input tax credit is "automatically" available to resellers of imported cigarettes.¹¹⁸ The Panel found that such resellers would not obtain an input tax credit if they fail to satisfy certain conditions, namely: (i) to complete and file form Por.Por.30; (ii) to produce a complete and accurate tax invoice in respect of a transaction (or to satisfy other conditions under Section 82/5 of the Thai Revenue Code); or (iii) to meet other record-keeping requirements.¹¹⁹ On this basis, the Panel concluded that "resellers of domestic cigarettes are *de jure* exempt from the VAT liability, whereas the same exemption is not granted to resellers of imported cigarettes as tax credits do not automatically and irrevocably offset tax liabilities incurred by [resellers] of imported cigarettes in every case."¹²⁰

95. Accordingly, the measure that the Panel analyzed under Article III:2 of the GATT 1994 consists of an exemption from VAT liability for resellers of domestic cigarettes, together with the imposition of VAT on resellers of imported cigarettes when they do not satisfy prescribed conditions for obtaining input tax credits necessary to achieve zero VAT liability.

2. The Measure Challenged Under Article III:4 of the GATT 1994

96. For purposes of the Philippines' claim under Article III:4 of the GATT 1994, the Panel also considered a series of provisions of Thailand's VAT regime.¹²¹

97. Pursuant to Section 81/2 of the Thai Revenue Code, businesses exempt from VAT are also exempt from compliance with the provisions of Chapter IV of the Thai Revenue Code. Consequently, because resellers of domestic cigarettes are exempt from VAT, they are also relieved of the obligation to comply with VAT-related administrative requirements contained in Chapter IV.¹²² The Panel addressed various requirements that, according to the Philippines, apply only to resellers of imported cigarettes, and not to resellers of domestic cigarettes. The Panel concluded that three sets of

¹¹⁶Panel Report, paras. 7.621 and 7.622.

¹¹⁷Panel Report, para. 7.628.

¹¹⁸Panel Report, para. 7.632.

¹¹⁹Panel Report, para. 7.634.

¹²⁰Panel Report, para. 7.644.

¹²¹The Philippines identified the following relevant provisions in connection with Thailand's VAT-related administrative requirements: Sections 81 and 82/7 of the Thai Revenue Code; Royal Decree No. 239; and Order No. Por. 85/2542. (Panel Report, para. 7.649)

¹²²Panel Report, paras. 7.688-7.690.

VAT-related administrative requirements impose an additional administrative burden only on resellers of imported cigarettes.¹²³

98. First, Section 83/1 of the Thai Revenue Code imposes on every VAT registrant the obligation to file a tax return, namely, form Por.Por.30, on a monthly basis regardless of the type of goods sold and/or services provided.¹²⁴ Resellers of goods subject to VAT, such as imported cigarettes, are therefore required to file form Por.Por.30. Resellers of exclusively VAT-exempt goods, such as domestic cigarettes, are not required to be VAT registrants and are therefore exempt from this requirement.¹²⁵ When a reseller sells both domestic cigarettes and other goods subject to VAT, that reseller is, by virtue of its sales of the latter, under an obligation to file form Por.Por.30. The Panel found, however, that such a reseller is not required to report its sales of VAT-exempt domestic cigarettes in that form.¹²⁶ The Panel therefore concluded that resellers of imported cigarettes are subject to a heavier administrative burden in respect of the obligation to complete and submit form Por.Por.30 because: (i) a reseller of domestic cigarettes who carries exclusively VAT-exempt goods, and therefore is not required to register for VAT, is exempted from the obligation to file form Por.Por.30, whereas the same exemption is not provided to resellers of imported cigarettes; and (ii) a cigarette reseller who is a VAT registrant need not report sales of domestic cigarettes when completing form Por.Por.30.¹²⁷ In this Report, we refer collectively to this first set of requirements as the "requirements relating to form Por.Por.30".

99. Second, Section 87 of the Thai Revenue Code requires resellers of imported cigarettes to prepare and maintain input tax and output tax records, and goods and raw materials records.¹²⁸ Resellers of imported cigarettes are also subject to an obligation to file revenue and expense reports, from which resellers of exclusively domestic cigarettes are exempt.¹²⁹ Thus, the Panel concluded that resellers of imported cigarettes, but not resellers of domestic cigarettes, are subject to an obligation to fill out and file reports.¹³⁰ The Panel further found that Section 87/3 of the Thai Revenue Code

¹²³The Philippines also alleged before the Panel that resellers of imported cigarettes are subject to tax invoice-related requirements and auditing procedures to which resellers of domestic cigarettes are not subject. Regarding the requirement to prepare and keep tax invoices, the Panel found that the Philippines did not respond to Thailand's argument that sales receipts, which both VAT registrants and non-VAT registrants must maintain, may serve as tax invoices, and that the Philippines did not fully explain its argument that the use of the MRSP as the tax base would make the requirement to prepare a tax invoice more burdensome for resellers of imported cigarettes. (Panel Report, paras. 7.706 and 7.707) With respect to the auditing procedures, the Panel found that resellers of both imported and domestic cigarettes are subject to similar procedures. (*Ibid.*, para. 7.718)

¹²⁴Panel Report, para. 7.686.

¹²⁵Panel Report, para. 7.694.

¹²⁶Panel Report, para. 7.703.

¹²⁷Panel Report, para. 7.704.

¹²⁸Panel Report, para. 7.654.

¹²⁹Panel Report, para. 7.710.

¹³⁰Panel Report, para. 7.715.

requires resellers of imported cigarettes to maintain more information for accounting and auditing purposes than that required of resellers of domestic cigarettes.¹³¹ In this Report, we refer collectively to this second set of requirements as the "reporting and record-keeping requirements".

100. Third, Sections 89 and 90 of the Thai Revenue Code subject VAT registrants to various penalties and other sanctions associated with the failure to comply with VAT-related administrative requirements set out in Chapter IV of the Thai Revenue Code.¹³² Resellers of goods that are subject to VAT, such as imported cigarettes, are therefore subject to these penalties and other sanctions, whereas resellers of exclusively domestic cigarettes are not. In this Report, we refer collectively to this third set of requirements as the "penalties and other sanctions".

101. In sum, the Panel found that Thailand imposes these three sets of requirements only on resellers of imported cigarettes.¹³³ With the exception of the issue of whether sales of domestic cigarettes must be reported in form Por.Por.30, discussed below in section IV.D.2 of our Report, the participants do not contest on appeal the Panel's findings that the requirements relating to form Por.Por.30, the reporting and record-keeping requirements, and the penalties and other sanctions are imposed only on resellers of imported cigarettes, and not on resellers of domestic cigarettes.¹³⁴

102. Accordingly, the measure that the Panel analyzed under Article III:4 of the GATT 1994 consists of an exemption from three sets of VAT-related administrative requirements for resellers of domestic cigarettes, together with the imposition of these administrative requirements on resellers of imported cigarettes.

103. Based on the foregoing, we now turn to assess Thailand's claims of error on appeal under Article III:2 and Article III:4 of the GATT 1994.

¹³¹Panel Report, para. 7.717.

¹³²Panel Report, paras. 7.719, 7.720, and 7.722. The Panel analyzed these penalties and other sanctions as part of the additional administrative requirements at issue, and neither participant has challenged this approach. We observe that they are not administrative requirements as such, but rather the consequence of failing to comply with VAT-related administrative requirements. Nonetheless, like the Panel, we address the penalties and other sanctions as among the relevant additional administrative requirements for purposes of our Report.

¹³³Panel Report, para. 7.722.

¹³⁴The Panel did not make any finding regarding the extent to which cigarette resellers sell exclusively domestic, exclusively imported, or both domestic and imported cigarettes, nor regarding the extent to which the distribution channels for domestic and imported cigarettes in Thailand overlap. Although the Panel acknowledged evidence adduced by the Philippines that more than 20 per cent of cigarette resellers in Thailand do not sell imported cigarettes, the Panel considered that the Philippines had not demonstrated why the 68,000 businesses concerned decided not to sell imported cigarettes, and also took note of Thailand's argument that many of those businesses are exempt from VAT liability by virtue of their low annual turnover. (Panel Report, paras. 7.725 and 7.727, and footnote 1300 to para. 7.736) Pursuant to Section 81/1 and Section 81/2 of the Thai Revenue Code, small businesses (that is, businesses with annual sales of less than 1.8 million baht) are exempt from all obligations under Chapter IV of the Thai Revenue Code. (*Ibid.*, para. 7.689 and footnote 1243 thereto)

C. Article III:2 of the GATT 1994

104. Thailand appeals the Panel's finding that:

... regarding the VAT exemption for domestic cigarette resellers, Thailand acted inconsistently with Article III:2, first sentence by subjecting imported cigarettes to a VAT liability in excess of that applied to like domestic cigarettes by granting the exemption from the VAT liability only to domestic cigarette[] resellers.¹³⁵

105. Thailand raises two principal issues on appeal. First, Thailand claims that the Panel erred because the measures that it found to be inconsistent with Article III:2, first sentence, of the GATT 1994 are not fiscal measures subject to the scope of that provision. Rather, according to Thailand, the measures entail only administrative requirements that fall within the scope of Article III:4, rather than Article III:2. Second, Thailand claims that, even if the measures fall within the scope of Article III:2, they do not subject imported cigarettes to taxes in excess of those applied to domestic cigarettes. In Thailand's view, inconsistency with Article III:2 cannot arise due to an obligation to comply with the administrative formality of filing a tax form, or a limitation on the availability of tax credits only for transactions that are documented and legitimate.

106. The Philippines argues that the Panel correctly established under Article III:2 that imported cigarettes are subject to taxation in excess of that applied to like domestic cigarettes. The Philippines considers that the Panel could have limited its analysis and simply found that resellers of imported cigarettes are subject to VAT liability, whereas resellers of domestic cigarettes, through a complete exemption from VAT, are not. The Philippines adds that, although the Panel did not need to do so, the Panel undertook further analysis and correctly found the existence of a discriminatory tax because resellers of imported cigarettes, in defined circumstances under Thai law, may not satisfy the conditions necessary to offset VAT liability. The Philippines rejects Thailand's argument that the administrative formalities associated with VAT liability cannot give rise to excess taxation under Article III:2.

107. Before we turn to evaluate the substance of Thailand's claim of error on appeal, we consider it necessary to recall the measure that the Panel found to be inconsistent with Article III:2, first sentence, of the GATT 1994. Thailand asserts that it is beyond dispute that Thailand's VAT rate is seven per cent for both imported and domestic cigarettes, and that the Panel found that the full amount

¹³⁵Panel Report, para. 8.3(b); see also para. 7.644. In assessing the Philippines' claim under Article III:2, the Panel undertook a two-step analysis to determine: (i) whether the imported and domestic products at issue are "like"; and (ii) whether the challenged measure subjects the imported products to an internal tax or charge in excess of that applied to like domestic products. (*Ibid.*, para. 7.569) In respect of likeness, the Panel found that the imported cigarettes at issue are "like" domestic cigarettes within the same price segments. (*Ibid.*, paras. 7.451 and 7.597) Thailand has not appealed this finding.

of VAT is collected from both the domestic producer and importers at the time of the first sale.¹³⁶ Thus, Thailand argues, the Panel's finding was not based on the tax burden under Thai VAT law, but instead was based solely on the difference in the "administrative requirements" for resales of imported and domestic cigarettes, and the consequences of failure to comply with those requirements.¹³⁷

108. We consider that Thailand's description of the measure analyzed by the Panel under Article III:2 as "administrative requirements" in respect of VAT is both under-inclusive and over-inclusive. The description is under-inclusive because it does not account for the complete exemption from VAT for resales of domestic cigarettes, and therefore disregards that VAT liability will, when certain conditions prescribed under Thai law are not met, be incurred by resellers of imported cigarettes, but never by resellers of domestic cigarettes. For this reason, Thailand's observation that the domestic producer and importer pay the same VAT amount is incomplete because it disregards that, under Thai law, subsequent resellers of imported cigarettes, but not subsequent resellers of domestic cigarettes, may also incur VAT liability. At the same time, Thailand's description is over-inclusive because the relevant measure for purposes of the Panel's consideration of the Philippines' Article III:2 claim does not include all of the administrative requirements evaluated by the Panel in respect of the Philippines' Article III:4 claim.¹³⁸ As we have explained, the relevant measure analyzed by the Panel under Article III:2 consists of an exemption from VAT liability for resellers of domestic cigarettes, together with the imposition of VAT on resellers of imported cigarettes when they do not satisfy prescribed conditions for obtaining input tax credits necessary to achieve zero VAT liability.¹³⁹

109. On the basis of this understanding of Thailand's measure, we now turn to Thailand's appeal of the Panel's finding under Article III:2, first sentence, of the GATT 1994.

110. Article III of the GATT 1994, entitled "National Treatment on Internal Taxation and Regulation", sets out obligations that prohibit the application by Members of internal tax and regulatory measures in a manner affording protection to domestic production. The various provisions

¹³⁶Thailand's appellant's submission, para. 73 (referring to Panel Report, para. 7.590).

¹³⁷Thailand's appellant's submission, paras. 74 and 75.

¹³⁸In its Article III:2 analysis, the Panel identified provisions under Thai law that specify conditions for obtaining an input tax credit. The Panel considered that a reseller of imported cigarettes would be subject to VAT if it did not properly fill out and file form Por.30, or did not, as specified in Section 82/5(1) and (2) of the Thai Revenue Code, produce a complete and accurate tax invoice in respect of a transaction. The Panel also stated that an input tax credit would not be available if certain reporting and record-keeping requirements were not satisfied, or if the conditions specified in Section 82/5 of the Thai Revenue Code were not met. (Panel Report, para. 7.634) In contrast, we note that, in its consideration of the Philippines' claim under Article III:4, the Panel evaluated various administrative requirements in addition to the requirements relating to form Por.30, but did not examine the conditions specified in Section 82/5 of the Thai Revenue Code.

¹³⁹See *supra*, para. 95.

of Article III thus operate to ensure that Members provide equality of competitive conditions for imported products in relation to domestic products in their internal markets.¹⁴⁰

111. The first sentence of Article III:2 provides:

The products of the territory of any Member imported into the territory of any other Member shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products.

112. Article III:2, first sentence, thus serves to prohibit the imposition of discriminatory internal taxes or other internal charges on imported versus like domestic products. Thailand's appeal calls for us to address two issues: whether Thailand's measure falls within the scope of the first sentence of Article III:2; and, if so, whether the taxes or charges applied to imported products pursuant to Thailand's measure are "in excess of" those applied to like domestic products. Article III:2, first sentence, concerns circumstances where imported and like domestic products are subject "directly or indirectly" to internal taxes or other internal charges "of any kind". This language suggests that the provision applies to a broad range of measures.¹⁴¹ Regarding the requirement of "not ... in excess of", the Appellate Body has clarified that a finding of inconsistency under Article III:2, first sentence, is not conditional on a "trade effects test", and that even the smallest amount of "excess" is too much.¹⁴² For purposes of our consideration of Thailand's appeal, a measure that subjects products to internal taxes or other internal charges may be examined under Article III:2, first sentence, of the GATT 1994. When such a measure subjects imported products to taxes or charges in excess of those applied to like domestic products, it will be inconsistent with the first sentence of Article III:2.

113. Thailand argues that, because the relevant measure relates only to administrative requirements, and the financial consequences of non-compliance with those requirements, it should have been evaluated by the Panel under Article III:4, not Article III:2, of the GATT 1994. According to Thailand, administrative requirements related to the collection of taxes, or consequences arising out of failure to comply with those requirements, are not subject to the disciplines of Article III:2, "even if the failure to comply with those administrative requirements may have financial consequences for an

¹⁴⁰Appellate Body Report, *Japan – Alcoholic Beverages II*, pp. 16-18, DSR 1996:1, 97, at 109-111. See also Appellate Body Report, *Korea – Alcoholic Beverages*, paras. 119 and 127; and Appellate Body Reports, *China – Auto Parts*, para. 161.

¹⁴¹Appellate Body Report, *Canada – Periodicals*, p. 19, DSR 1997:1, 449, at 464-465.

¹⁴²Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 23, DSR 1996:1, 97, at 115.

imported product".¹⁴³ The Philippines argues that the Panel properly found that Thailand's measure falls within the scope of Article III:2.

1114. We have already explained that we do not accept Thailand's characterization of the measure that was challenged by the Philippines, and found by the Panel to be inconsistent with Article III:2, as administrative requirements. For the reasons set out above, we also do not accept Thailand's position that the measure at issue does not relate to the respective tax burdens imposed on imported and domestic cigarettes. Thailand's measure subjects resellers of imported cigarettes to VAT when they do not satisfy prescribed conditions for obtaining input tax credits necessary to achieve zero VAT liability. Whether such conditions are satisfied thus has a direct consequence for the amount of tax liability imposed on imported cigarettes. Conversely, a complete exemption from VAT ensures that there can never be any VAT liability for resellers in respect of their sales of domestic cigarettes. We therefore agree with the Panel that Thailand's measure affects the respective tax liability imposed on imported and like domestic cigarettes, and accordingly reject Thailand's claim that the measure consists solely of administrative requirements that are not subject to the disciplines of Article III:2, first sentence, of the GATT 1994.¹⁴⁴

1115. Thailand also argues that, even if the Panel were correct to examine Thailand's measure under Article III:2, the Panel erred in finding that Thailand acted inconsistently with that provision. Thailand contends that it cannot be WTO-inconsistent to require resellers to complete "administrative formalities"¹⁴⁵ in order to obtain input tax credits necessary to achieve zero VAT liability. Thailand adds that none of the six situations set out in Section 82/5 of the Thai Revenue Code¹⁴⁶ involves a situation in which a reseller could be denied an input tax credit on the basis of an actual, legitimate purchase of cigarettes for resale. In contrast, the Philippines argues that, if resellers of imported cigarettes cannot obtain an input tax credit, this is the legal consequence of the regulatory framework established by Thailand. The Philippines maintains that resellers of domestic cigarettes are never subject to that consequence because they are automatically exempt from VAT liability on such sales.

¹⁴³Thailand's appellant's submission, para. 71.

¹⁴⁴We note that even if a measure at issue consisted solely of administrative requirements, we do not exclude the possibility that such requirements may have a bearing on the respective tax burdens on imported and like domestic products, and may therefore be subject to Article III:2. Although Thailand may be correct in stating that prior WTO reports have examined measures consisting of "administrative requirements relating to the sale of imported products" under Article III:4 (Thailand's appellant's submission, para. 69), this does not in our view demonstrate that, if such requirements subject imported and like domestic products to internal taxes or other internal charges, the same measures, or certain aspects of the same measures, could not also be scrutinized under Article III:2. (See Panel Report, *Argentina – Hides and Leather*, para. 11.143 (finding that administrative measures concerning the pre-payment of tax "qualify as tax measures [that] fall to be assessed under Article III:2"))

¹⁴⁵Thailand's appellant's submission, para. 91.

¹⁴⁶See *supra*, para. 93.

1116. Thailand does not dispute that resellers of imported cigarettes incur VAT liability when they do not satisfy conditions to obtain an input tax credit¹⁴⁷, or that a measure that creates a risk of excess taxation may give rise to a violation of Article III:2, first sentence.¹⁴⁸ Rather, Thailand argues that requiring resellers to satisfy administrative requirements in respect of VAT does not present a risk related to the calculation of the tax burden, and therefore cannot give rise to a violation under Article III:2. We consider, however, that a proper conception of Thailand's measure clarifies that it is not the mere imposition of administrative requirements that creates a differential tax burden, but rather that only resellers of imported cigarettes will incur VAT liability as a consequence of failing to offset output tax. Resellers of imported cigarettes are subject to VAT liability in defined circumstances under Thai law, whereas resellers of domestic cigarettes, due to a complete exemption from VAT, are not. Based on this understanding of the measure, we therefore agree with the Panel that Thailand subjects imported cigarettes to internal taxes in excess of those applied to like domestic cigarettes, within the meaning of Article III:2, first sentence, of the GATT 1994.

1117. Thailand also argues that the conduct of private parties in relation to the challenged measure cannot form the basis for establishing a violation of Article III:2. As Thailand puts it, a system of offsetting input tax against output tax cannot be said to be WTO-inconsistent "simply because private parties are required to comply with certain administrative requirements", or because it compels resellers "to limit claims for input tax credits to actual, legitimate purchases" of cigarettes.¹⁴⁹ Thailand argued at the oral hearing that resellers of imported cigarettes will owe VAT only when they have not legitimately purchased cigarettes, or when they make mistakes in their filing for VAT.¹⁵⁰ It is not clear to us, based on the Panel's findings regarding the operation of Thailand's measure, that the situations in which resellers of imported cigarettes will incur VAT liability are limited to those identified by Thailand. In any event, we do not consider that Thailand's measure precludes a finding of inconsistency with Article III:2 due to the fact that resellers of imported cigarettes may take action to avoid the imposition of VAT liability. In our view, the availability of such a course of action does not alter the legal assessment of whether, under Thai law, imported cigarettes are subject to internal taxes or other internal charges in excess of those applied to domestic cigarettes. As we have explained, Thailand's measure provides for circumstances in which resellers of imported cigarettes will be subject to VAT liability, to which resellers of domestic cigarettes will never be subject. In this respect, we agree with the Panel's reliance on *Korea – Various Measures on Beef*, where the Appellate

¹⁴⁷Thailand's appellant's submission, para. 97. See also Thailand's responses to Panel Questions 137 and 138.

¹⁴⁸Thailand's appellant's submission, paras. 80-82 (referring to GATT Panel Report, *US – Tobacco*, para. 97).

¹⁴⁹Thailand's appellant's submission, para. 90.

¹⁵⁰Thailand's responses to questioning at the oral hearing.

Body stated, in the context of its Article III:4 analysis, that "the intervention of some element of private choice does not relieve Korea of responsibility under the GATT 1994 for the resulting establishment of competitive conditions less favourable for the imported product than for the domestic product".¹⁵¹

118. We also disagree with Thailand's suggestion that the Panel's finding would limit the ability of WTO Members to ensure the proper administration of their tax regimes.¹⁵² Again, the Panel considered that Thailand's measure was inconsistent with Article III:2, first sentence, not because it prescribed conditions for obtaining tax credits, but rather because those conditions applied only in respect of resellers of imported cigarettes, and did not "automatically and irrevocably offset tax liabilities incurred by [those resellers] in every case".¹⁵³ WTO Members remain free "to administer and collect internal taxes as they see fit", so long as they do so "in conformity with Article III:2".¹⁵⁴ Imposing legal requirements that result in tax liability on imported products when resellers do not satisfy prescribed conditions necessary to avoid that liability, but which never result in tax liability on like domestic products, is inconsistent with the requirements of Article III:2, first sentence.

119. For the foregoing reasons, we *uphold* the Panel's finding, in paragraph 8.3(b) of the Panel Report, that Thailand acts inconsistently with Article III:2, first sentence, of the GATT 1994 by subjecting imported cigarettes to VAT liability in excess of that applied to like domestic cigarettes.¹⁵⁵

D. *Article III:4 of the GATT 1994*

120. Thailand appeals the Panel's finding that:

... regarding the VAT exemption for domestic cigarette resellers, Thailand acted inconsistently with Article III:4 by subjecting imported cigarettes to less favourable treatment compared to like domestic cigarettes by imposing additional administrative requirements, connected to VAT liabilities, on imported cigarette resellers.¹⁵⁶

121. The Panel's finding under Article III:4 of the GATT 1994 concerned an exemption from three sets of VAT-related administrative requirements for resellers of domestic cigarettes, together with the

¹⁵¹Panel Report, para. 7.637 (quoting Appellate Body Report, *Korea – Various Measures on Beef*, para. 146).

¹⁵²Thailand's appellant's submission, paras. 96, 97, and 104.

¹⁵³Panel Report, para. 7.644.

¹⁵⁴Panel Report, *Argentina – Hides and Leather*, para. 11.144. The Panel stated that Thailand did not assert a defence under Article XX to the alleged violation of Article III:2 of the GATT 1994. (Panel Report, para. 7.642)

¹⁵⁵See also Panel Report, para. 7.644.

¹⁵⁶Panel Report, para. 8.3(c); see also para. 7.738.

imposition of these administrative requirements on resellers of imported cigarettes. These three sets of administrative requirements consist of: (i) requirements relating to form Por.Por.30; (ii) reporting and record-keeping requirements; and (iii) penalties and other sanctions.¹⁵⁷ We refer to these requirements collectively as the "additional administrative requirements".

122. Thailand advances three independent grounds for reversal of the Panel's finding under Article III:4. First, Thailand argues that the Panel's analysis of "treatment no less favourable" was insufficient as a matter of law to support a finding that Thailand acted inconsistently with Article III:4. Second, Thailand claims that the Panel erred in accepting and relying upon an exhibit submitted late in the proceedings by the Philippines—Exhibit PHL-289—and thus violated Article 11 of the DSU, Thailand's due process rights, and paragraph 15 of the Panel's Working Procedures. Third, Thailand alleges that, because the Panel failed to conduct a correct legal analysis in respect of Thailand's defence under Article XX(d) of the GATT 1994, the Panel "effectively deprived" Thailand of the opportunity to justify the additional administrative requirements as necessary to secure compliance with the Thai VAT laws. We address these issues in turn.

1. Article III:4: "treatment no less favourable"

123. In its appeal of the Panel's finding that imported cigarettes are treated less favourably than like domestic cigarettes, Thailand argues that differences in treatment are "not necessarily inconsistent with Article III:4, as long as the treatment provided by the measure is 'no less favourable'"¹⁵⁸, and that a determination of less favourable treatment "*cannot rest on simple assertion*", but must be founded on a careful analysis of the contested measure and of its implications in the marketplace.¹⁵⁹ According to Thailand, however, the Panel based its finding on a "mere assertion"¹⁶⁰ or a "theoretical possibility"¹⁶¹ that the differences in treatment found by the Panel "*could* affect costs and *could potentially affect* the competitive position" of imported cigarettes.¹⁶² Thailand adds that the Panel failed to conduct "*any* meaningful analysis"¹⁶³ of how the differences in treatment might, in practice, increase costs, or how the measures at issue "constrained" or "restricted" the choices available to traders in such a manner as to affect the competitive conditions for imported cigarette resellers.¹⁶⁴

¹⁵⁷See *supra*, Section IV.B.2.

¹⁵⁸Thailand's appellant's submission, para. 122 (quoting Appellate Body Report, *Korea – Various Measures on Beef*, para. 135).

¹⁵⁹Thailand's appellant's submission, para. 125 (quoting Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 215). (emphasis added by Thailand)

¹⁶⁰Thailand's appellant's submission, para. 142.

¹⁶¹Thailand's appellant's submission, para. 120.

¹⁶²Thailand's appellant's submission, para. 120. (original emphasis)

¹⁶³Thailand's appellant's submission, para. 135. (original emphasis)

¹⁶⁴Thailand's appellant's submission, para. 140.

124. In response, the Philippines submits that treatment is less favourable if it does not "ensure effective equality of opportunities"¹⁶⁵ between imported products and domestic products, and that this equality of opportunities is upset when government regulation is not "perfectly neutral".¹⁶⁶ The Philippines contends that, when government regulation subjects imported products to burdens that are not imposed on like domestic products, the treatment of imported and like domestic products is unequal and, accordingly, "inherently less favorable" for imported goods.¹⁶⁷ On this basis, the Panel correctly found that, because resellers of imported cigarettes must comply with three additional administrative requirements that are not imposed on resellers of domestic cigarettes, the treatment accorded to imported cigarettes was "inherently less favourable".¹⁶⁸ The Philippines adds that, even though it was not necessary for it to do so, the Panel sought further confirmation for its finding of less favourable treatment by examining the ways in which Thailand's additional administrative requirements upset the equality of competitive conditions in the Thai market. The Panel considered evidence of price elasticity and switching patterns and found that domestic and imported cigarettes operate in a close competitive relationship in the Thai market, such that the additional administrative requirements can potentially have a negative impact on the competitive position of imported cigarettes. The Philippines points out that the additional administrative requirements can be linked to the operating costs of businesses, thereby disturbing the equality of competitive conditions.

125. We begin our analysis with the text of Article III:4 of the GATT 1994, which provides in relevant part:

The products of the territory of any Member imported into the territory of any other Member shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use.

126. Article III:4 forms part of the broader framework set out in Article III, which ensures that Members provide equality of competitive conditions for imported products in relation to domestic products.¹⁶⁹ Like the other paragraphs of Article III, the obligation prescribed under Article III:4 is informed by the general principle set out in Article III:1 that internal measures should not be applied

¹⁶⁵Philippines' appellee's submission, para. 121 (quoting, *inter alia*, Panel Report, *Canada – Autos*, paras. 10, 78 and 10, 84).

¹⁶⁶Philippines' appellee's submission, para. 123.

¹⁶⁷Philippines' appellee's submission, para. 129 (referring to Appellate Body Report, *US – Section 211 Appropriations Act*, para. 265).

¹⁶⁸Philippines' appellee's submission, para. 137 (referring to Appellate Body Report, *US – Section 211 Appropriations Act*, para. 265).

¹⁶⁹See Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 16, DSR 1996:1, 97, at 109.

so as to afford protection to domestic production.¹⁷⁰ In the context of Article III:4, this means that, where there is less favourable treatment of imported products, there is protection to domestic production.¹⁷¹

127. Article III:4 consists of three elements that must be demonstrated in order to establish inconsistency with this provision, namely: (i) that the imported and domestic products are "like products"; (ii) that the measure at issue constitutes a law, regulation, or requirement affecting the internal sale, offering for sale, purchase, transportation, distribution, or use of the products at issue; and (iii) that the treatment accorded to imported products is less favourable than that accorded to like domestic products.¹⁷² Thailand's appeal concerns only the Panel's finding in respect of the third element, namely, the no less favourable treatment standard in Article III:4.¹⁷³

128. The phrase "treatment no less favourable" in Article III:4 has been interpreted by the Appellate Body in prior disputes. In *Korea – Various Measures on Beef*, the Appellate Body explained that the analysis of whether imported products are treated less favourably must ascertain whether the measure at issue "modifies the conditions of competition in the relevant market to the detriment of imported products".¹⁷⁴ The Appellate Body also stated that "[a] formal difference in treatment between imported and like domestic products is ... neither necessary, nor sufficient, to show a violation of Article III:4".¹⁷⁵ Accordingly, the mere fact that a Member draws regulatory distinctions between imported and like domestic products is, in itself, not determinative of whether imported products are treated less favourably within the meaning of Article III:4.¹⁷⁶ Rather, what is relevant is whether such regulatory differences distort the conditions of competition to the detriment of imported products. If so, then the differential treatment will amount to treatment that is "less favourable" within the meaning of Article III:4.

129. The analysis of whether imported products are accorded less favourable treatment requires a careful examination "grounded in close scrutiny of the fundamental thrust and effect of the measure itself"¹⁷⁷, including of the implications of the measure for the conditions of competition between

¹⁷⁰See Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 18, DSR 1996:1, 97, at 111.

¹⁷¹See Appellate Body Report, *EC – Asbestos*, para. 100.

¹⁷²Appellate Body Report, *Korea – Various Measures on Beef*, para. 133.

¹⁷³The Panel found that the imported cigarette brands Marlboro and L&M are "like" Thai domestic cigarettes within the meaning of Article III:4 of the GATT 1994. (Panel Report, para. 7.662) Likewise, the Panel found that the Thai regulations at issue, containing the additional administrative requirements, can be considered as affecting the internal sale of imported cigarettes within the meaning of Article III:4 of the GATT 1994. (*Ibid.*, para. 7.665) Neither of these findings is appealed.

¹⁷⁴Appellate Body Report, *Korea – Various Measures on Beef*, para. 137. (original emphasis)

¹⁷⁵Appellate Body Report, *Korea – Various Measures on Beef*, para. 137.

¹⁷⁶Appellate Body Report, *EC – Asbestos*, para. 100.

¹⁷⁷Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 215 (quoting Appellate Body Report, *Korea – Various Measures on Beef*, footnote 44 to para. 142).

imported and like domestic products. This analysis need not be based on empirical evidence as to the actual effects of the measure at issue in the internal market of the Member concerned. Of course, nothing precludes a panel from taking such evidence of actual effects into account.

130. The implications of the contested measure for the equality of competitive conditions are, first and foremost, those that are discernible from the design, structure, and expected operation of the measure. For instance, where a Member's legal system applies a single regulatory regime to both imported and like domestic products, with the sole difference being that an additional requirement is imposed only on imported products, the existence of this additional requirement may provide a significant indication that imported products are treated less favourably. Because, however, the examination of whether imported products are treated less favourably "cannot rest on simple assertion"¹⁷⁸, close scrutiny of the measure at issue will normally require further identification or elaboration of its implications for the conditions of competition in order properly to support a finding of less favourable treatment under Article III:4 of the GATT 1994.

131. The Panel found that the additional administrative requirements imposed only on resellers of imported cigarettes "could potentially affect" the conditions of competition for imported cigarettes in a negative manner.¹⁷⁹ In its analysis, the Panel began by observing that, in previous disputes, a simple administrative authorization scheme¹⁸⁰, a differentiated distribution scheme¹⁸¹, or the mere possibility that non-nationals have to defend their patent claims in two jurisdictions rather than only one¹⁸², were all situations found to constitute "additional administrative burdens" that accord less favourable treatment.¹⁸³ The Panel then observed that the relative market shares held by imported and domestic cigarettes in the Thai market and an econometric study submitted by the Philippines show a certain degree of price elasticity and switching patterns. The Panel considered that this would also indicate that the additional administrative requirements "can potentially have" a negative impact on the competitive position of imported cigarettes in the Thai market.¹⁸⁴ Furthermore, the Panel reasoned that, because the burden associated with the additional administrative requirements can be linked to the operating costs of suppliers of imported cigarettes, this could limit business opportunities

¹⁷⁸Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 215.

¹⁷⁹Panel Report, para. 7.734.

¹⁸⁰Panel Report, para. 7.732 (referring to Panel Report, *Canada – Wheat Exports and Grain Imports*, paras. 6.184 and 6.213).

¹⁸¹Panel Report, para. 7.732 (referring to Appellate Body Report, *Korea – Various Measures on Beef*, paras. 143-151; and GATT Panel Report, *US – Malt Beverages*, paras. 5.32 and 5.35).

¹⁸²Panel Report, paras. 7.730 and 7.732 (referring to Appellate Body Report, *US – Section 211 Appropriations Act*, para. 265).

¹⁸³Panel Report, para. 7.732.

¹⁸⁴Panel Report, para. 7.735.

for imported cigarettes to the extent that cigarette suppliers seek to reduce costs by avoiding resales of imported cigarettes.¹⁸⁵

132. On appeal, Thailand contends that the Panel erred and applied an incorrect standard of less favourable treatment because its finding was based on the "theoretical possibility" that the "differences could affect costs and could potentially affect the competitive position of imported cigarettes in a negative manner"¹⁸⁶, and that the Panel failed to engage in any meaningful analysis as to the implications of the measure in the marketplace, or how the differences affect the competitive position of imported cigarettes. Although Thailand does not contest the Panel's finding that the additional administrative requirements are imposed only on resellers of imported cigarettes¹⁸⁷, Thailand characterizes these requirements as "benign"¹⁸⁸ or "very minor"¹⁸⁹ differences in treatment, and argues that "the right to treat imported products differently may include the right to impose additional or more complicated requirements so long as they do not amount to 'less favourable' treatment".¹⁹⁰

133. We observe that the regulatory "differences" at issue stem from the fact that resellers of imported cigarettes must comply with the additional administrative requirements, whereas resellers of domestic cigarettes are exempt from such requirements. Thus, in this dispute, the sole difference in regulatory treatment consists of requirements applied *only* to imported cigarettes. The uncontested fact that resellers of imported cigarettes are subject to certain administrative requirements, whereas resellers of like domestic cigarettes are not, itself provides a significant indication that imported cigarettes are accorded less favourable treatment.

134. With respect to the standard of less favourable treatment under Article III:4, we observe that, in its third participant's submission, Australia expresses concern with the Panel's apparent use of a test of whether the measure at issue "may potentially modify" the conditions of competition to the detriment of imported products. Australia argues that previous panels have used a more rigorous legal standard of less favourable treatment, namely, whether a measure "may reasonably be expected"¹⁹¹ or "is more than likely"¹⁹² to modify adversely the conditions of competition. In our view, however, an

¹⁸⁵Panel Report, para. 7.736.

¹⁸⁶Thailand's appellant's submission, para. 120. (original emphasis)

¹⁸⁷Thailand confirmed at the oral hearing that, on appeal, it contests only the evidentiary basis for the Panel's finding that resellers of imported cigarettes are not required to report resales of domestic cigarettes in form Por.Por.30. That issue is addressed below in the context of Thailand's claim under Article 11 of the DSU.

¹⁸⁸Thailand's appellant's submission, para. 135.

¹⁸⁹Thailand's appellant's submission, para. 137.

¹⁹⁰Thailand's appellant's submission, para. 129.

¹⁹¹Australia's third participant's submission, para. 26 (quoting Panel Report, *China – Publications and Audiovisual Products*, para. 7.1471).

¹⁹²Australia's third participant's submission, para. 27 (quoting Panel Report, *India – Autos*, para. 7.201).

analysis of less favourable treatment should not be anchored in an assessment of the degree of likelihood that an adverse impact on competitive conditions will materialize. Rather, an analysis under Article III:4 must begin with careful scrutiny of the measure, including consideration of the design, structure, and expected operation of the measure at issue. Such scrutiny may well involve—but does not require—an assessment of the contested measure in the light of evidence regarding the actual effects of that measure in the market. In any event, there must be in every case a genuine relationship between the measure at issue and its adverse impact on competitive opportunities for imported versus like domestic products to support a finding that imported products are treated less favourably.

135. Furthermore, we do not agree with Thailand that the Panel's use of the word "potentially" reveals that the Panel found less favourable treatment based only on a remote, unsubstantiated, or "theoretical possibility" that differences in regulatory treatment could affect the conditions of competition for imported cigarettes. The Panel referred to the Appellate Body Report in *US – FSC (Article 21.5 – EC)* to note that an examination of whether a measure involves less favourable treatment "need not be based on the actual effects of the contested measure in the marketplace".¹⁹³ The Panel understood this statement to mean that "the contested measure in the marketplace can be assessed on its potential effects on the competitive conditions of the imported product concerned".¹⁹⁴ We consider that, when read in the context of this reasoning, it is clear that the terms "potentially" and "potential effects" were intended to reflect the Panel's recognition that it was not required to inquire into the "actual effects" of the additional administrative requirements.

136. In addition, we observe that the Panel *did* identify further implications of the additional administrative requirements in the Thai market affecting the competitive position of imported and domestic cigarettes. In particular, the Panel observed that an econometric study submitted by the Philippines suggested a "certain degree of price elasticity and switching patterns" between imported and domestic cigarettes, and that this was an indication that the additional administrative requirements "can potentially have a negative impact on the competitive position of [imported] cigarettes in the market".¹⁹⁵ On appeal, Thailand alleges that the Panel itself acknowledged that this evidence was

¹⁹³Panel Report, para. 7.730 (quoting Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 215 (original emphasis)).

¹⁹⁴Panel Report, para. 7.730. (original emphasis)

¹⁹⁵Panel Report, para. 7.735. This evidence was provided by the Philippines, and consists of a study conducted by an economics professor regarding cross-price elasticity between imported and domestic cigarettes in Thailand between 2007 and 2009. In particular, this study noted that "the estimated increase of market share of domestic cigarettes pursuant to an increase in the relative [retail selling price] of imported cigarettes strongly suggests that the two products are close substitutes in the eyes of Thai consumers". (*Ibid.*, para. 7.446 (quoting Panel Exhibit PHL-149, p. 9))

"uneven".¹⁹⁶ Furthermore, adds Thailand, the no less favourable treatment analysis under Article III:4 presupposes that imported and domestic products have been considered "like", and that, consequently, imported and domestic products subject to an Article III:4 analysis will always have "some" degree of competitive relationship with each other".¹⁹⁷

137. As we see it, the Panel did not acknowledge that the econometric evidence before it was "uneven". Instead, the Panel merely took note of Thailand's contention that "switching patterns are uneven across various pairs of domestic and foreign brands".¹⁹⁸ Furthermore, the Panel did not err in relying upon this econometric evidence for its finding of less favourable treatment under Article III:4. The Panel used this evidence merely to *confirm* that the additional administrative requirements may have a negative impact on imported cigarettes relative to domestic cigarettes, as these products are in close competition with each other in the Thai market.¹⁹⁹ Taking a specific example, the Panel considered that the additional administrative requirements imposed only on resellers of imported cigarettes may affect business decisions of cigarette suppliers because "an additional administrative burden can be linked to the operating costs of their businesses", which would, in turn, modify the conditions of competition to the detriment of imported cigarettes.²⁰⁰ Although Thailand criticizes the Panel for this "cursory" statement²⁰¹, we consider that the Panel sought merely to identify that the "potential operating costs associated with the additional administrative requirements" may influence business decisions in a market where products compete closely with each other.²⁰² In our view, it was reasonable for the Panel to conclude that compliance with the additional administrative requirements will involve some costs that resellers of imported cigarettes, and not resellers of like domestic cigarettes, must bear, taking account of, *inter alia*, economic evidence relating to the market.

138. Accordingly, we are not persuaded by Thailand's arguments that the Panel made its finding "without making any factual findings other than to establish the existence of the different requirements themselves".²⁰³ The Panel assessed certain implications of these measures in the Thai market by referring to econometric evidence indicating a close competitive relationship, and also by

¹⁹⁶Thailand's appellant's submission, para. 114 (quoting Panel Report, footnote 1299 to para. 7.735).

¹⁹⁷Thailand's appellant's submission, para. 132.

¹⁹⁸Panel Report, footnote 1299 to para. 7.735.

¹⁹⁹At paragraph 7.735 of its Report, the Panel stated: (i) that TTM holds a 78 per cent market share, whereas imported cigarettes account for the remaining 22 per cent; (ii) that the econometric evidence adduced by the Philippines suggests a certain degree of elasticity and switching patterns between imported and domestic cigarettes; and (iii) that, "[i]n our view, this would also indicate that additional administrative requirements, albeit slight, imposed only on imported cigarettes can potentially have a negative impact on the competitive position of these cigarettes in the market".

²⁰⁰Panel Report, para. 7.736.

²⁰¹Thailand's appellant's submission, para. 134.

²⁰²Panel Report, para. 7.736.

²⁰³Thailand's appellant's submission, para. 119.

noting that the additional administrative requirements carry certain operating costs.²⁰⁴ We note that, although the Panel could have inquired further into the implications of Thailand's measure for the conditions of competition, the mere fact that the additional administrative requirements are imposed on imported cigarettes, and not on like domestic cigarettes, provides, in itself, a significant indication that the conditions of competition are adversely modified to the detriment of imported cigarettes. We therefore consider that the Panel's analysis was sufficient to support its finding that the additional administrative requirements modify the conditions of competition to the detriment of imported cigarettes.

139. Finally, Thailand claims that the Panel failed to address Thailand's argument that resellers of imported cigarettes gain certain "financial advantages" by virtue of the additional administrative requirements.²⁰⁵ In particular, Thailand argues that resellers of imported cigarettes may claim "additional input tax credits for VAT paid on utilities, administrative expenses and other services consumed on the basis of the ratio of their VAT sales to their VAT-exempt sales".²⁰⁶ However, we observe that Thailand submitted this argument only in response to Panel questions following the first substantive meeting, and in a few other instances thereafter, and that Thailand produced no evidence to substantiate its assertion. Therefore, we do not see any basis for Thailand's contention on appeal that the Panel should have given greater consideration to this argument in conducting its substantive analysis.²⁰⁷

140. Accordingly, we reject Thailand's contention on appeal that the Panel's findings and "analysis of less favourable treatment are not sufficient as a matter of law to support a finding of a violation of

²⁰⁴In addition, we note that other Panel findings shed further light on the implications of the additional administrative requirements in the Thai market. The Panel found that failure to comply with the requirements relating to form Por.30 and the reporting and record-keeping requirements may lead to denial of tax credits. (Panel Report, para. 7.634) Moreover, the Panel found that resellers of imported cigarettes may be subject to certain penalties and other sanctions if they fail to comply with the VAT-related administrative requirements. (*Ibid.*, paras. 7.719 and 7.722) By contrast, these economic risks are not borne by resellers of domestic cigarettes.

²⁰⁵Thailand's appellant's submission, para. 136.

²⁰⁶Thailand's appellant's submission, para. 136.

²⁰⁷We also note that the GATT Panel in *US – Section 337 Tariff Act* held that:

[T]he "no less favourable" treatment requirement of Article III:4 has to be understood as applicable to each individual case of imported products. The Panel rejected any notion of balancing more favourable treatment of some imported products against less favourable treatment of other imported products. If this notion were accepted, it would entitle a contracting party to derogate from the no less favourable treatment obligation in one case, or indeed in respect of one contracting party, on the ground that it accords more favourable treatment in some other case, or to another contracting party. Such an interpretation would lead to great uncertainty about the conditions of competition between imported and domestic products and thus defeat the purposes of Article III.

(GATT Panel Report, *US – Section 337 Tariff Act*, para. 5.14)

Article III:4".²⁰⁸ We therefore find that the Panel did not err in concluding, in paragraph 7.738 of the Panel Report, that Thailand accords less favourable treatment to imported cigarettes than to like domestic cigarettes.

2. Article 11 of the DSU: the Panel's Treatment of Exhibit PHL-289

141. We now turn to Thailand's request to reverse the Panel's finding of inconsistency with Article III:4 of the GATT 1994 on the grounds that the Panel failed to comply with Article 11 of the DSU. According to Thailand, the Panel failed to ensure due process and to make an objective assessment of the matter by accepting and relying on Exhibit PHL-289 without affording Thailand any opportunity to respond to that evidence.

142. Before considering the merits of Thailand's claim of error, we consider it useful to set out the circumstances that have given rise to this issue on appeal. Exhibit PHL-289 was submitted by the Philippines at the last stage of the proceedings before the Panel and consists of an expert opinion from a Thai tax lawyer. The opinion concerns the issue of whether, as a matter of Thai law, VAT registrants reselling domestic cigarettes are required to report their sales of domestic cigarettes in form Por.30. This issue was contested throughout the Panel proceedings, with the Philippines arguing that VAT registrants are obliged to report only resales of imported, not domestic, cigarettes, and Thailand arguing that resales of both imported and domestic cigarettes must be reported. As explained above²⁰⁹, the Panel ultimately agreed with the Philippines.²¹⁰ The requirement to report resales of imported cigarettes, but not resales of like domestic cigarettes, in form Por.30 was thus one of the additional administrative requirements examined by the Panel in its Article III:4 analysis.²¹¹

143. Prior to the submission of Exhibit PHL-289, each party had adduced several exhibits in support of its position on whether or not resales of domestic cigarettes must be reported in form Por.30. Thailand submitted form Por.30, along with the instructions provided to taxpayers on how to complete that form²¹², as well as certain examples of form Por.30 actually filed by VAT

²⁰⁸Thailand's appellant's submission, para. 117.

²⁰⁹*Supra*, para. 98.

²¹⁰Panel Report, para. 7.703.

²¹¹Thailand's Article 11 claim with respect to Exhibit PHL-289 relates only to the Panel's finding in paragraph 7.704 that VAT registrants need not include information on resales of domestic cigarettes in form Por.30, and does not concern the Panel's finding in the same paragraph, that resellers of exclusively domestic cigarettes are exempt from the requirement to file form Por.30. Nor does Thailand's objection to Exhibit PHL-289 concern the other additional administrative requirements that the Panel found to be imposed only on resellers of imported cigarettes.

²¹²Form Por.30 (Thai monthly VAT form) (Panel Exhibit THA-42), submitted by Thailand with its answers to the Panel's questions following the first substantive meeting.

registrants.²¹³ With its second written submission, the Philippines submitted an expert opinion²¹⁴ and a ruling by the Director-General of the Thai Revenue Department issued in 2000 (the "2000 DG Revenue ruling").²¹⁵ The Philippines further attached a second expert opinion to its opening statement at the second substantive meeting of the Panel with the parties.²¹⁶ In its questions following the second substantive meeting, the Panel specifically requested Thailand to comment on the 2000 DG Revenue ruling provided by the Philippines.²¹⁷ In responding to that question, Thailand submitted an excerpt from a 2006 textbook on the Thai Revenue Code²¹⁸ (the "2006 textbook"), and a ruling by the Director-General of the Thai Revenue Department issued in 1995 (the "1995 DG Revenue ruling").²¹⁹ On 8 December 2009, each party submitted its comments on the other party's answers to Panel questions following the second substantive meeting. This was the last stage of the proceedings before the Panel. In its comments, the Philippines responded to Thailand's evidence, and in particular to the 1995 DG Revenue ruling, and in doing so submitted a third expert opinion (Exhibit PHL-289), which is the evidence at the centre of this issue on appeal.²²⁰

144. The Panel's Interim Report was issued to the parties on 30 June 2010. In its comments on the Interim Report, Thailand requested the Panel to revise its analysis under Article III.4 of the GATT 1994 and to find that resales of domestic cigarettes *are* required to be reported in form Por.Por.30.²²¹ Among the arguments put forth by Thailand in support of this request was that the Panel should not have relied upon Exhibit PHL-289. Thailand stressed that this exhibit had been provided only "at the last opportunity afforded to the parties to submit their views"²²², and that paragraph 15 of the Panel's Working Procedures required evidence, including Exhibit PHL-289, to be submitted no later than the first substantive meeting of the Panel with the parties.²²³ In dismissing Thailand's request, the Panel observed that nothing in the DSU or its Working Procedures precluded the Panel "from accepting evidence submitted by a party at the latest stage of the proceedings".²²⁴ The Panel also read the first sentence of the opinion in Exhibit PHL-289 as "suggesting that the

²¹³TJM and Re-seller Forms Por.Por.30 (Panel Exhibit THA-89 (BCI)), submitted by Thailand with its opening statement at the second substantive meeting.

²¹⁴Expert statement by Mr. Piphob Veraphong, 17 July 2009 (Panel Exhibit PHL-207).

²¹⁵Revenue Ruling Gor.Kor. 0811/Por.633, 27 January 2000 (Panel Exhibit PHL-253).

²¹⁶Expert Statement by Mr. Piphob Veraphong, 1 September 2009 (Panel Exhibit PHL-254).

²¹⁷In Panel Question 142(2), the Panel requested Thailand to comment on the "DG Excise's ruling, provided by the Philippines at the second substantive meeting (Exhibit PHL-253)".

²¹⁸Excerpt of page 4-266 of *Textbook on the Revenue Code* by Professor Paichit Rojanavanich, Chumporn Sensai, and Saroch Thongpracum, B.E. 2549 (2006) (Panel Exhibit THA-95).

²¹⁹Revenue Department Ruling Gor.Kor. 0802/Por.22836, 10 October 1995 (Panel Exhibit THA-96).

²²⁰Expert Statement by Mr. Piphob Veraphong, 8 December 2009 (Panel Exhibit PHL-289).

²²¹Thailand's comments on the Interim Report, para. 63. Thailand's comments were submitted to the Panel on 14 July 2010.

²²²Panel Report, para. 6.122 (quoting Thailand's comments on the Interim Report, para. 48).

²²³Panel Report, para. 6.122.

²²⁴Panel Report, para. 6.125.

intended purpose of this evidence was to rebut Thailand's arguments in relation to [the 1995 DG Revenue ruling].²²⁵ Accordingly, since Exhibit PHL-289 was evidence necessary for purposes of rebuttal or comments provided by parties, the Panel concluded that accepting this evidence was in accordance with paragraph 15 of its Working Procedures.

145. On appeal, Thailand argues that the Panel violated Thailand's due process rights and acted inconsistently with Article 11 of the DSU by accepting and relying on Exhibit PHL-289 without affording Thailand the right to comment on that evidence. Thailand points to several considerations as establishing such a violation, which may be grouped into two main lines of argument. First, Thailand emphasizes that due process requires that parties be provided with an adequate opportunity to respond to evidence adduced by the other party. Given the significance of Exhibit PHL-289 to the Panel's finding regarding the requirement to report sales of domestic cigarettes in form Por.Por.30, Thailand considers that its due process rights with respect to that piece of evidence should have been "accorded the highest importance".²²⁶ Thailand adds that the Panel's failure to ensure due process was "exacerbated" by the fact that the Panel did not accord deference to Thailand's interpretation of its own law.²²⁷ Second, Thailand contends that the Panel's acceptance of Exhibit PHL-289 was not consistent with paragraph 15 of its Working Procedures. In Thailand's view, because Exhibit PHL-289 was not rebuttal evidence, it should have been submitted no later than the first substantive meeting, or accepted only after having required the Philippines to show good cause and having afforded Thailand a right of response.

146. The Philippines, for its part, argues that the Panel complied with its duties under Article 11 of the DSU. According to the Philippines, the Panel respected both Thailand's due process rights and paragraph 15 of the Panel's Working Procedures. Thailand did have opportunities to comment on Exhibit PHL-289, and took advantage of one of them during interim review. The Philippines stresses that Thailand did not seek an opportunity to comment on Exhibit PHL-289 at the time that it was submitted, and that Thailand did not submit its own evidence, the 1995 DG Revenue ruling, at the earliest opportunity, but only in its responses to Panel questions after the second substantive meeting. The Philippines further maintains that the Panel did not give decisive weight to Exhibit PHL-289, in either the Interim Report or the Panel Report. For the Philippines, moreover, the expert opinion contained in Exhibit PHL-289 constitutes evidence that is covered by the first, rather than the second, sentence of paragraph 15 of the Panel's Working Procedures. Accordingly, the Panel was not required, pursuant to paragraph 15, to determine that the Philippines had shown good cause for the admission of Exhibit PHL-289, nor to afford Thailand an opportunity to respond to that evidence.

²²⁵Panel Report, para. 6.127.

²²⁶Thailand's appellant's submission, para. 171.

²²⁷Thailand's appellant's submission, para. 173.

147. We note that Thailand couches its claim under Article 11 of the DSU as a "due process claim".²²⁸ Due process is a fundamental principle of WTO dispute settlement.²²⁹ It informs and finds reflection in the provisions of the DSU.²³⁰ In conducting an objective assessment of a matter, a panel is "bound to ensure that due process is respected".²³¹ Due process is intrinsically connected to notions of fairness, impartiality, and the rights of parties to be heard and to be afforded an adequate opportunity to pursue their claims, make out their defences, and establish the facts in the context of proceedings conducted in a balanced and orderly manner, according to established rules. The protection of due process is thus a crucial means of guaranteeing the legitimacy and efficacy of a rules-based system of adjudication.

148. Panel working procedures should both embody and reinforce due process. Article 12.1 of the DSU states that panels "shall" follow the working procedures set out in Appendix 3 to the DSU "unless the panel decides otherwise after consulting the parties to the dispute". The working procedures adopted by a panel must conform to the DSU.²³² As the Appellate Body has previously observed, the use by panels of detailed, standardized working procedures promotes fairness and the protection of due process.²³³ The inclusion by a panel in its working procedures of a rule that is inconsistent with due process would be a clear sign that such panel has failed to ensure the protection of due process. At the same time, even when the working procedures are themselves sound, a panel's failure to adhere to those procedures may be pertinent to, albeit not necessarily determinative of, the issue of whether such panel has failed to ensure the protection of due process in a given instance.

149. We also recall that panel proceedings consist of two main stages, the first of which involves each party setting out its "case in chief, including a full presentation of the facts on the basis of submission of supporting evidence", and the second designed to permit the rebuttal by each party of

²²⁸Thailand's response to questioning at the oral hearing.

²²⁹The Appellate Body has held that "the protection of due process is an essential feature of a rules-based system of adjudication, such as that established under the DSU", and that "due process is fundamental to ensuring a fair and orderly conduct of dispute settlement proceedings". (Appellate Body Reports, *Canada – Continued Suspension / US – Continued Suspension*, para. 433; and Appellate Body Report, *Thailand – H-Beams*, para. 88, respectively. See also Appellate Body Report, *Chile – Price Band System*, para. 176.)

²³⁰See Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 107. See also Appellate Body Report, *India – Patents (US)*, para. 94; and Appellate Body Report, *Chile – Price Band System*, para. 176.

²³¹Appellate Body Report, *Chile – Price Band System*, para. 176.

²³²We observe that, in *India – Patents (US)*, the Appellate Body held that, while "panels enjoy some discretion in establishing their own working procedures, this discretion does not extend to modifying the substantive provisions of the DSU". (Appellate Body Report, *India – Patents (US)*, para. 92. See also Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 241.)

²³³See Appellate Body Reports, *Canada – Continued Suspension / US – Continued Suspension*, para. 434; Appellate Body Report, *Argentina – Textiles and Apparel*, footnote 68 to para. 79; Appellate Body Report, *EC – Bananas III*, para. 144; and Appellate Body Report, *India – Patents (US)*, para. 95.

the arguments and evidence submitted by the other parties.²³⁴ Nonetheless, the submission of evidence may not always fall neatly into one or the other of these categories, in particular when panels themselves, in the exercise of their fact finding authority, seek to pursue specific lines of inquiry in their questioning of the parties. In this respect, we wish to reiterate that due process will best be served by working procedures that provide "for appropriate factual discovery at an early stage in panel proceedings"²³⁵, and that "[d]ue process may be of particular concern in cases where a party raises *new facts* at a late stage of the panel proceedings."²³⁶ Furthermore, when the particular circumstances of specific disputes present situations that are not explicitly regulated by their working procedures, panels, in the exercise of their control over the proceedings, and subject to the constraints of due process and the DSU, enjoy a margin of discretion to deal with such situations.²³⁷

150. As a general rule, due process requires that each party be afforded a meaningful opportunity to comment on the arguments and evidence adduced by the other party. This was expressly acknowledged by the Appellate Body in *Australia – Salmon* when it stated that "[a] fundamental tenet of due process is that a party be provided with an opportunity to respond to claims made against it".²³⁸ At the same time, due process may also require a panel to take appropriate account of the need to safeguard other interests, such as an aggrieved party's right to have recourse to an adjudicative process in which it can seek redress in a timely manner, and the need for proceedings to be brought to a close. These interests find reflection in the provisions of the DSU, including Article 3.3, which calls for "[t]he prompt settlement" of WTO disputes, as this is "essential to the effective functioning of the WTO and the maintenance of a proper balance between the rights and obligations of Members". Likewise, Article 12.2 of the DSU provides that "[p]anel procedures should provide sufficient flexibility so as to ensure high-quality panel reports, while not unduly delaying the panel process". Furthermore, "in the interests of due process, parties should bring alleged procedural deficiencies to the attention of a panel at the earliest possible opportunity".²³⁹ Accordingly, ensuring due process requires a balancing of various interests, including systemic interests as well as those of the parties, and both general and case-specific considerations. In our view, panels are best situated to determine how this balance should be struck in any given proceeding, provided that they are vigilant in the protection of due process and remain within the bounds of their duties under Article 11 of the DSU.

²³⁴Appellate Body Report, *Argentina – Textiles and Apparel*, para. 79. See also Appellate Body Report, *US – FSC (Article 21.5 – EC)*, para. 240.

²³⁵Appellate Body Report, *India – Patents (US)*, para. 95.

²³⁶Appellate Body Report, *US – Gambling*, para. 271. (original emphasis)

²³⁷Appellate Body Report, *EC – Hormones*, footnote 138 to para. 152.

²³⁸Appellate Body Report, *Australia – Salmon*, para. 278. See also *ibid.*, para. 272; and Appellate Body Report, *US – Gambling*, para. 270.

²³⁹Appellate Body Report, *US – Carbon Steel*, para. 123. See also Appellate Body Report, *US – Gambling*, para. 269; Appellate Body Report, *US – FSC*, para. 166; and Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 50.

151. We begin our analysis of the Panel's treatment of Exhibit PHL-289 by examining Thailand's arguments concerning paragraph 15 of the Panel's Working Procedures, which provides:

The parties shall submit all factual evidence to the Panel no later than the first substantive meeting, except with respect to factual evidence necessary for purposes of rebuttals, answers to questions or comments on answers provided by each other. Exceptions to this procedure will be granted where good cause is shown. In such cases, the other party shall be accorded a period of time for comment, as appropriate.²⁴⁰

152. We note at the outset that, although it alleges that the Panel failed to comply with this paragraph, Thailand is not seeking from us an independent finding that the Panel violated paragraph 15 of its Working Procedures. Rather, Thailand invokes this provision to support its contention that the Panel violated Thailand's due process rights and failed to comply with its duties under Article 11 of the DSU.²⁴¹

153. We read paragraph 15 as addressing two categories of evidence. The first encompasses evidence that is submitted no later than the first substantive meeting, as well as evidence that, albeit submitted at a later stage, is necessary for purposes of rebuttal, answers to questions, or comments on answers to questions. The second category of evidence is residual. It comprises evidence that does not fall within the scope of the first sentence. For the second category of evidence, the submitting party must show good cause and the other party must be accorded an opportunity to comment.

154. Thailand contends that Exhibit PHL-289 cannot be characterized as evidence necessary for purposes of rebuttal, or comments on Thailand's answers to Panel questions, because it was evidence adduced in support of the Philippines' *prima facie* case and, in particular, to establish that resales of domestic cigarettes need not be reported in form Por.30. Yet, as explained above, the Philippines had previously submitted the 2000 DG Revenue ruling and two expert opinions in support of this assertion. Then, in response to a specific request by the Panel to comment on the 2000 DG Revenue ruling, Thailand submitted the 1995 DG Revenue ruling to show that resales of domestic cigarettes must be reported in form Por.30. The Philippines, in turn, responded in its comments on Thailand's answers by submitting Exhibit PHL-289 to show that the 2000 DG Revenue ruling reflected the current state of Thai law. As we see it, Exhibit PHL-289 was submitted to explain the discrepancies between the 1995 DG Revenue ruling and the 2000 DG Revenue ruling. As such, this exhibit was "factual evidence necessary for purposes of rebuttals ... or comments on [Thailand's] answers" within the meaning of the first sentence of paragraph 15. Thus, the Panel's acceptance of

²⁴⁰Panel Report, Annex A-1. The Panel, pursuant to Article 12.1 of the DSU, adopted its own Working Procedures following consultation with the parties.

²⁴¹Thailand's response to questioning at the oral hearing.

Exhibit PHL-289 without requiring the Philippines to show good cause or affording Thailand an opportunity to comment thereon was not inconsistent with paragraph 15 of the Panel's Working Procedures.²⁴²

155. However, the fact that the Panel's treatment of Exhibit PHL-289 was not inconsistent with paragraph 15 of its Working Procedures is, in our view, not dispositive of whether Thailand's due process rights were respected and, accordingly, of whether the Panel complied with its duties under Article 11 of the DSU. As set out above, due process generally demands that each party be afforded a meaningful opportunity to comment on evidence adduced by the other party. At the same time, a number of different considerations will need to be factored into a panel's effort to protect due process in a particular dispute, and these may include the need for a panel, in pursuing prompt resolution of the dispute, to exercise control over the proceedings in order to bring an end to the back and forth exchange of competing evidence by the parties. In the context of this dispute, there are several considerations that are germane to our assessment of Thailand's claim under Article 11 of the DSU. These include: the conduct of the parties; the legal issue to which the evidence related and the circumstances surrounding the submission of the evidence relating to that issue; and the discretion afforded under the DSU to panels in their handling of the proceedings and appreciation of the evidence.

156. With respect to the conduct of the parties, we observe that Thailand adduced two items of evidence, including the 1995 DG Revenue ruling, in response to a specific question posed by the Panel following the second substantive meeting. Exhibit PHL-289 was then submitted by the Philippines at the earliest subsequent opportunity, that is, in its comments on Thailand's answers to Panel questions.²⁴³ Although this was the last stage in the Panel proceedings, the Philippines would have had no reason to produce the expert testimony contained in Exhibit PHL-289 at an earlier stage, given that this evidence was introduced to rebut the 1995 DG Revenue ruling. Moreover, Thailand did not object to Exhibit PHL-289 when it was submitted, but rather seven months later, in its comments on the Panel's Interim Report. Although we are mindful that the parties' submission of comments on each other's responses to the Panel's questions marked the last step in the Panel proceedings, we do not consider that this precluded Thailand from objecting to Exhibit PHL-289 in a

²⁴²We note that the first sentence of paragraph 15 appears to allow for the submission of factual evidence at the very last stage of the proceedings, that is, in a party's comments on the other party's answers to questions by the Panel following the second substantive meeting. A party's submission of factual evidence so late in the proceedings should be unusual.

²⁴³Philippines' appellee's submission, paras. 189-192.

timely fashion, and requesting that the Panel either reject that evidence or give Thailand an opportunity to respond to that evidence.²⁴⁴

157. Thailand alleges that the due process violation is "more serious" because "Exhibit PHL-289 was the 'only evidence' supporting"²⁴⁵ the Panel's finding that resales of domestic cigarettes need not be reported in form Por.Por.30, and that "the parties' rights under the DSU may be affected by the importance of the evidence at issue".²⁴⁶ In response, the Philippines argues that the Panel did not attach "decisive weight"²⁴⁷ to Exhibit PHL-289, but instead reached its finding based "on several pieces of evidence constituting the totality of the evidence before it".²⁴⁸

158. We recall that the issue of whether a VAT registrant is required to report resales of VAT-exempt goods, such as domestic cigarettes, in form Por.Por.30 was contested between the parties throughout the proceedings, and each adduced several pieces of evidence in support of its position. Thus, at the time that Exhibit PHL-289 was submitted by the Philippines, both Thailand and the Panel would have been aware that it related to a key and highly disputed issue. In determining that resales of domestic cigarettes need not be reported in form Por.Por.30, the Panel explained that this finding was "based on [its] careful examination of all the evidence in its totality".²⁴⁹ In its analysis, the Panel referred to the 2006 textbook, as well as the 1995 DG Revenue ruling, which had been adduced to show that resales of VAT-exempt products must be reported in form Por.Por.30.²⁵⁰ The Panel also observed that the 2000 DG Revenue ruling, together with the second expert opinion submitted by the Philippines, indicated that businesses selling VAT-exempt domestic cigarettes do not have to report those sales in form Por.Por.30.²⁵¹ The Panel further noted that the third expert opinion submitted by the Philippines—Exhibit PHL-289—explained that the differences in the rulings issued in 1995 and 2000 reflect "a change in DG Revenue's approach to the requirements for completing Form Por.Por.30".²⁵²

²⁴⁴Although the Philippines asserts that Thailand had, and took advantage of, the opportunity to respond to Exhibit PHL-289 in its comments on the Interim Report, we do not consider that this constituted an appropriate opportunity to respond.

²⁴⁵Thailand's appellant's submission, para. 170.

²⁴⁶Thailand's appellant's submission, para. 170 (referring to Panel Report, *Korea – Alcoholic Beverages*, para. 10.25).

²⁴⁷Philippines' appellee's submission, para. 209.

²⁴⁸Philippines' appellee's submission, para. 221.

²⁴⁹Panel Report, para. 7.703. Thailand's assertion that Exhibit PHL-289 was the *only* evidence upon which the Panel based its finding that sales of domestic cigarettes need not be reported in form Por.Por.30 is also based on a statement made by the Panel in its Interim Report that was not included in the Panel's final Report. We do not consider that it is appropriate, in these appellate proceedings, for Thailand to rely upon a statement made by the Panel in its Interim Report but which was redacted from the Panel Report.

²⁵⁰Panel Report, para. 7.698.

²⁵¹Panel Report, para. 7.699.

²⁵²Panel Report, para. 7.700 and footnote 1253 thereto.

159. The above overview of the evidence considered by the Panel indicates that Exhibit PHL-289 was not the only evidence supporting the Panel's finding that resales of domestic cigarettes need not be reported in form Por.Por.30.²⁵³ If anything, the main support for the Panel's finding seems to have been found in the 2000 DG Revenue ruling, which the Panel apparently found compelling because it confirmed that "income exempted under Section 81 need not be reported in Form Por.Por.30 for the calculation of VAT".²⁵⁴

160. In the light of the above, we do not consider that the Panel's treatment of Exhibit PHL-289 amounted to a violation of due process. Thailand could have requested an opportunity to respond when the Philippines submitted the exhibit in question, but it did not.²⁵⁵ Although Exhibit PHL-289 was submitted very late in the proceedings, this evidence did not raise or relate to a new issue, previously unknown to Thailand or unexplored by the Panel, and it was not the only evidence supporting the Panel's conclusion that resales of domestic cigarettes need not be reported in form Por.Por.30. The Panel could have chosen to refuse to accept Exhibit PHL-289 or to afford Thailand an opportunity to respond to it. It did not do so. However, taking into account all of the circumstances, we consider that the Panel did not fail to protect due process in this case.²⁵⁶

²⁵³We take note of Thailand's additional argument that the Panel's failure to respect Thailand's due process rights was "exacerbated" by the fact that the Panel failed to give "due deference" to Thailand's interpretation of its own law. (Thailand's appellant's submission, para. 173.) In our view, the panel in *China – Intellectual Property Rights* correctly recognized that, "objectively, a Member is normally well-placed to explain the meaning of its own law", but that this does not relieve a party of its burden to adduce arguments and evidence necessary to sustain its proposed interpretation. (Panel Report, *China – Intellectual Property Rights*, para. 7.28) Further, a panel's duties under Article 11 of the DSU require it to conduct an objective assessment of all such arguments and evidence. In this dispute, the Panel observed, in the context of its Article III:4 analysis, that "Thailand should normally be in a position to explain the nature' of obligations under Thai law but that, to the extent that the parties disagree on the content of such obligations, the Panel was "required to objectively examine the question at issue based on the text of the concerned provision[s] as well as on the evidence before [the Panel]". (Panel Report, para. 7.684 (footnote omitted)) We see no error in the Panel's approach.

²⁵⁴Panel Report, para. 7.701.

²⁵⁵We are not suggesting that the fact that Thailand did not expressly request an opportunity to respond to Exhibit PHL-289 automatically implies that it cannot succeed in its claim that the Panel failed to ensure due process. At the same time, Thailand's failure to request an opportunity to respond is a consideration relevant to our overall assessment of whether, in the circumstances of this case, the Panel's conduct denied due process to Thailand. We observe, in this regard, that when confronted with an issue similar to the one raised here, the panel in *China – Auto Parts* rejected "China's argument that the Panel should, *sua sponte*, have accorded a period of time for other parties to comment on Exhibit CDA-48", and stated that "it is China, *not the Panel*, that should have initiated an opportunity to submit comments on Exhibit CDA-48." (Panel Reports, *China – Auto Parts*, para. 6.22 (emphasis added)) We disagree with these statements to the extent that they imply that only the conduct of the party receiving evidence submitted by the other party late in the proceedings is relevant in determining whether due process was protected. In our view, both that party and the panel to which the evidence is submitted have a responsibility to consider whether an opportunity to respond to that evidence would be useful or necessary, and to conduct themselves accordingly.

²⁵⁶We wish to emphasize, however, that we do not consider that the mere characterization of evidence as rebuttal evidence means that no due process concerns can arise in situations where a panel does not afford a party an opportunity to respond to such rebuttal evidence.

161. For all of these reasons, we *find* that Thailand has not established that the Panel failed to ensure due process and, thus, to comply with its duty under Article 11 of the DSU to make an objective assessment of the matter by accepting and relying on Exhibit PHL-289 without having afforded Thailand an opportunity to comment on that evidence.

3. Thailand's Defence Under Article XX(d) of the GATT 1994

162. Thailand also appeals the Panel's finding that:

... Thailand has not discharged its burden of showing that the administrative requirements and the imposition of penalties for failure to complete VAT filing requirements are necessary to secure compliance with the Thai VAT laws within the meaning of Article XX(d) of the GATT 1994.²⁵⁷

163. The Panel made this finding in response to Thailand's efforts to invoke Article XX(d) of the GATT 1994 to defend the additional administrative requirements found to be inconsistent with Article III:4. Article XX(d) enables Members to justify measures found to be inconsistent with the provisions of the GATT 1994 if they can establish that such measures are "necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement", and provided that the application of such measures is also consistent with the requirements of the chapeau of Article XX. Thus, in order to make out an Article XX(d) defence, a respondent must, *inter alia*, identify "laws or regulations which are not inconsistent" with the GATT 1994, and establish that the measure found to be GATT-inconsistent is "necessary" to secure compliance with such "laws or regulations".

164. Thailand requests us to reverse the Panel's finding under Article XX(d). Thailand does not challenge the substance of the Panel's reasoning on Thailand's defence, as such. Rather, Thailand contends that a reference contained in the sentence of the Panel Report immediately preceding the Panel's finding reveals that the Panel "committed a fundamental error of legal analysis in its rejection of Thailand's defence under Article XX(d)".²⁵⁸ That sentence reads:

As addressed in Section VII.F.6(b)(ii) above, however, we found that the Thai VAT laws that Thailand purports to secure compliance with through the administrative requirement[s] at issue, were *not* WTO consistent.²⁵⁹ (original italics; underlining added)

²⁵⁷Panel Report, para. 7.758.

²⁵⁸Thailand's appellant's submission, para. 153.

²⁵⁹Panel Report, para. 7.758.

165. Thus, by means of a cross-reference to Section VII.F.6(b)(i) of its Report, the Panel expressed the view that Thailand had not identified "laws or regulations which are not inconsistent" with the GATT 1994, but only VAT laws that the Panel had already found to be GATT-inconsistent. As Thailand's asserted Article XX(d) defence could not succeed if the laws or regulations with which the measures at issue purportedly secure compliance are themselves GATT-inconsistent, the Panel, in the very next sentence of its Report, reached the finding set out above.

166. Section VII.F.6(b)(ii) of the Panel Report comprises paragraphs 7.729 through 7.738. It contains the Panel's analysis of "[w]hether imported cigarettes are subject to less favourable treatment than domestic cigarettes within the meaning of Article III:4"²⁶⁰, and culminates with the Panel's conclusion that "Thailand acted inconsistently with Article III:4 by subjecting imported cigarettes to less favourable treatment compared to like domestic cigarettes *through the VAT-related administrative requirements imposed only on resellers of imported cigarettes*."²⁶¹

167. Thailand argues that the Panel's reference to Section VII.F.6(b)(ii) shows that the Panel identified as the "laws or regulations" with which the inconsistent measure purportedly secures compliance the very same measure that the Panel had found to be inconsistent with Article III:4 of the GATT 1994. Thus, the Panel's cross-reference signifies, according to Thailand, that the Panel rejected Thailand's Article XX(d) defence to the violation of Article III:4 on the grounds that it had already found that the additional administrative requirements violate Article III:4. Such circular reasoning constitutes, in Thailand's view, a "fundamental error" by the Panel that "effectively deprived Thailand of its right to assert its Article XX(d) defence" to the finding of inconsistency with Article III:4. For this reason, Thailand submits that the Panel's Article III:4 finding "is also legally flawed"²⁶², and should also be reversed.

168. The Philippines, on the other hand, considers the cross-reference made by the Panel to be a mere clerical error. The Philippines sees no basis in the Panel's reasoning to suggest that its examination of Thailand's defence consisted of a circular analysis of whether the additional administrative requirements are necessary to secure compliance with those same administrative requirements. The Philippines highlights that the Panel properly articulated the legal standard under Article XX(d) and identified Thailand's argument as being that the "administrative requirements" are necessary to secure compliance "with the Thai VAT laws". Thus, the Philippines believes that other elements of the Panel's reasoning disclose that the cross-reference in paragraph 7.758 was simply a mistake, and that the Panel really intended to refer to Section VII.E.5(b)(ii) of its Report, which deals

²⁶⁰Panel Report, heading to Section VII.F.6(b).

²⁶¹Panel Report, para. 7.738. (emphasis added)

²⁶²Thailand's appellant's submission, para. 156.

with discriminatory taxation, rather than to Section VII.F.6(b)(i) of its Report, which deals with the discriminatory administrative requirements. Accordingly, the Philippines requests the Appellate Body to modify this clerical error, replacing the reference to "Section VII.F.6(b)(ii)" with a reference to "Section VII.E.5(b)(ii)".

169. Like the participants, we, too, consider the Panel's reference to Section VII.F.6(b)(ii) to be erroneous. Read literally, this cross-reference means that the Panel considered that the additional administrative requirements could not be justified as necessary to secure compliance with those same additional administrative requirements because the additional administrative requirements had already been found to be inconsistent with Article III:4. This would be a manifestly incorrect approach to the analysis of Thailand's Article XX(d) defence.

170. The Panel's analysis and disposition of Thailand's defence under Article XX(d) of the GATT 1994 was extremely brief. In just over a page, the Panel set out the text of the provision, identified the order of analysis, the burden of proof, and the requisite elements of an Article XX(d) defence. In a single paragraph, including the cross-reference to Section VII.F.6(b)(ii) quoted above, the Panel applied this analysis to the facts before it. The brevity of this analysis has not itself been challenged on appeal. Yet it does mean that the Panel's reasoning offers few clues as to the details of the analytical steps taken by the Panel. Thus, even accepting the Philippines' assertions that the Panel properly identified the legal standard to be applied under Article XX(d) and the elements of the defence advanced by Thailand, we do not see sufficient reasoning to enable us to conclude with confidence that, although the Panel in fact referred to its finding in Section VII.F.6(b)(ii), it intended to refer to its finding in Section VII.E.5(b)(ii) of its Report, or indeed to any other Section of its Report. The reference to Section VII.F.6(b)(ii) was an obvious error, but it is not clear, on the basis of the Panel Report, what would have been the correct reference.

171. Accordingly, due to the obvious error in the penultimate sentence of paragraph 7.758 of the Panel Report, we are compelled to *reverse* the Panel's finding, in that paragraph, that Thailand did not discharge its burden of demonstrating that the additional administrative requirements are necessary to secure compliance with the Thai VAT laws within the meaning of Article XX(d) of the GATT 1994.

172. Thailand contends that, in the event that we reverse this finding by the Panel, we should also reverse the Panel's finding that the additional administrative requirements are inconsistent with Article III:4 because the Panel "effectively deprived Thailand of its right to assert its Article XX(d)

defence" to that finding.²⁶³ Thailand does not refer to any provision of the DSU or other covered agreement, nor to any jurisprudence, in support of this position.

173. We have difficulties understanding why the Panel's disposition of the Philippines' claim under Article III:4 should depend on the Panel's disposition of Thailand's defence under Article XX(d). It is true that, in examining a specific measure, a panel may be called upon to analyze a substantive obligation and an affirmative defence, and to apply both to that measure. It is also true that such an exercise will require a panel to find and apply a "line of equilibrium"²⁶⁴ between a substantive obligation and an exception. Yet this does not render that panel's analyses of the obligation and the exception a single and integrated one. On the contrary, an analysis of whether a measure infringes an obligation necessarily precedes, and is distinct from, the "further and separate" assessment of whether such measure is otherwise justified.²⁶⁵ Thus, we reject Thailand's request to reverse the Panel's Article III:4 finding on the grounds that the Panel erred in its analysis of Thailand's Article XX(d) defence.

174. In circumstances where it has reversed panel findings and legal interpretations, the Appellate Body has, within the limits of its jurisdiction, consistently sought to "facilitate the prompt settlement of the dispute"²⁶⁶ by completing the legal analysis of relevant issues.²⁶⁷ The same considerations impel us to seek to do the same in this appeal. Accordingly, we consider whether we are able to rule, ourselves, on Thailand's defence under Article XX(d) of the GATT 1994.

175. Article XX(d) of the GATT 1994 provides:

General Exceptions

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Member of measures:

....

²⁶³Thailand's appellant's submission, para. 156.

²⁶⁴Appellate Body Report, *US – Shrimp*, para. 159.

²⁶⁵In *US – Gasoline*, the Appellate Body cautioned against confusing "the question of whether inconsistency with a substantive rule existed, with the *further and separate question* ... as to whether that inconsistency was nevertheless justified". (Appellate Body Report, *US – Gasoline*, p. 23, DSR 1996:1, 1, at 21 (emphasis added)). See also GATT Panel Report, *US – Section 337 Tariff Act*, para. 5.9)

²⁶⁶Appellate Body Report, *US – Hot-Rolled Steel*, para. 235.

²⁶⁷To the extent that completion of the legal analysis requires the Appellate Body to rely upon facts, the Appellate Body can complete the analysis only if "factual findings of the panel" and/or "undisputed facts in the panel record" provide a sufficient factual basis to perform the requisite legal analysis. (See Appellate Body Report, *EC – Asbestos*, para. 78)

(d) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including those relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the protection of patents, trade marks and copyrights, and the prevention of deceptive practices[.]

176. Article XX(d) is one of the limited and conditional "General Exceptions" that allow Members pursuing certain public policy objectives to derogate from the substantive obligations in the GATT 1994, including the national treatment obligations set out in Article III.²⁶⁸ In order to justify an otherwise GATT-inconsistent measure, a Member invoking Article XX(d) as a defence bears the burden of establishing that the conditions prescribed therein are met.²⁶⁹

177. A Member will successfully discharge that burden and establish its Article XX(d) defence upon demonstration of three key elements, namely: (i) that the measure at issue secures compliance with "laws or regulations" that are themselves consistent with the GATT 1994; (ii) that the measure at issue is "necessary" to secure such compliance; and (iii) that the measure at issue meets the requirements set out in the chapeau of Article XX. Furthermore, when Article XX(d) is invoked to justify an inconsistency with Article III:4, what must be shown to be "necessary" is the treatment giving rise to the finding of less favourable treatment.²⁷⁰ Thus, when less favourable treatment is found based on differences in the regulation of imports and of like domestic products, the analysis of an Article XX(d) defence should focus on whether those regulatory differences are "necessary" to secure compliance with "laws or regulations" that are not GATT-inconsistent.

178. In all of its submissions before the Panel, Thailand devoted just six paragraphs to justifying the additional administrative requirements, and provided little or no elaboration of the necessary elements of its asserted defence under Article XX(d). We see at least four critical flaws in Thailand's presentation of its Article XX(d) defence to the Panel.

179. First, in putting forth its defence, Thailand sought to justify administrative requirements relating to VAT liability generally, rather than to justify the *differential treatment* afforded to imported versus domestic cigarettes under its measure. Second, Thailand failed to identify precisely the "laws or regulations" with which the measure at issue purportedly secures compliance, and engaged in no effort to establish that such laws and regulations are consistent with the GATT 1994.

²⁶⁸See Appellate Body Report, *US – Gasoline*, p. 24, DSR 1996:1, 1, at 22; and Appellate Body Report, *US – Shrimp*, para. 156.

²⁶⁹See Appellate Body Report, *Korea – Various Measures on Beef*, para. 157.

²⁷⁰See GATT Panel Report, *US – Section 337 Tariff Act*, para. 5.27.

Even assuming that the vague references made by Thailand in its submissions to the Panel²⁷¹ could be construed as identifying relevant laws or regulations with which the additional administrative requirements seek to ensure compliance, Thailand's arguments with respect to, third, "necessity" and, fourth, the chapeau of Article XX, were patently underdeveloped.²⁷² With respect to the necessity test, Thailand asserted that the "reporting requirements are necessary ... to the enforcement of Thailand's VAT system"²⁷³, and that the additional administrative requirements are necessary "in that it is difficult to see how Thailand could administer its VAT system *without* requiring VAT payers to maintain and submit input and output reports, the VAT Form Por.Por. 30 and the other requirements".²⁷⁴ Thailand provided no further elaboration of these assertions and adduced no evidence in support of them.²⁷⁵ As for the chapeau of Article XX, Thailand referred to it only once.

In its entirety, this reference consisted of Thailand's argument that, "[g]iven that these measures are applied to all products, imported or domestic, subject to VAT, they are not applied in a manner that constitutes an arbitrary or unjustifiable discrimination or a disguised restriction on international

²⁷¹Thailand made loose references to: "Thailand's VAT law" (Thailand's first written submission to the Panel, para. 260); "Thailand's VAT system, as established under Chapter 4 of Thailand's Revenue Code" (*ibid.*); and the "normal reporting requirements of its VAT and other tax laws" (Thailand's response to Panel Question 139, para. 147). These references encompass a myriad of provisions of Thai law addressing various matters. In one instance, Thailand also argued that the "penalties [] ensure compliance with the normal reporting requirements of its VAT and other tax laws especially where ... those reporting requirements contribute to the fight against smuggling of cigarettes". (Thailand's response to Panel Question 139, para. 147). This argument seems to have been advanced in order to justify the penalties under Article XX(d) in the event that the Panel considered such penalties to constitute "excess tax" under Article III:2 of the GATT 1994. It is unclear to us whether Thailand sought to assert the same defence in the event that, as the Panel ultimately found, the penalties were inconsistent with Article III:4.

²⁷²That the defence by Thailand was largely unelaborated with respect to "necessity" is likely due to the fact that it is difficult to make detailed arguments to demonstrate the "necessity" of a measure under Article XX(d) in the absence of a clear identification of the laws or regulations with which that measure is purportedly necessary to secure compliance.

²⁷³Thailand's second written submission to the Panel, para. 177.

²⁷⁴Thailand's first written submission to the Panel, para. 260. (original emphasis) Thailand added that the additional administrative requirements "are necessary, as that term has been interpreted by the Appellate Body in *Brazil – Retreaded Tyres*" (Thailand's second written submission to the Panel, para. 177), and, in a footnote, quoted a statement by the Appellate Body in that report, that a measure is necessary if it is "apt to make a material contribution to the achievement of its objective" (Thailand's second written submission to the Panel, footnote 139 to para. 177 (quoting Appellate Body Report, *Brazil – Retreaded Tyres*, para. 150)).

²⁷⁵We recall that the issue of "whether a measure is 'necessary' should be determined through a process of weighing and balancing a series of factors" (Appellate Body Report, *Korea – Various Measures on Beef*, para. 164) and that "two factors that, in most cases, will be relevant to a panel's determination of the 'necessity' of a measure [are] the contribution of the measure to the realization of the ends pursued by it [and] the restrictive impact of the measure on international commerce" (Appellate Body Report, *US – Gambling*, para. 306). Moreover, a panel's analysis of "necessity" must include consideration of "whether a WTO-consistent alternative measure which the Member concerned could reasonably be expected to employ is available". (Appellate Body Report, *Korea – Various Measures on Beef*, para. 166) See also Appellate Body Report, *Brazil – Retreaded Tyres*, paras. 142 and 143.

trade".²⁷⁶ This cannot suffice to establish that the additional administrative requirements fulfil the requirements of the chapeau of Article XX.²⁷⁷

180. In our view, therefore, the arguments and evidence put forward by Thailand fail, on their face, to establish the requisite elements of an Article XX(d) defence. Accordingly, we *find* that Thailand failed to make out a *prima facie* defence and, therefore, failed to establish that the additional administrative requirements are justified under Article XX(d) of the GATT 1994.

4. Conclusion

181. In the light of the above, we *uphold* the Panel's finding, in paragraph 8.3(c) of the Panel Report, that Thailand acts inconsistently with its obligations under Article III:4 of the GATT 1994 by subjecting imported cigarettes to treatment less favourable than that accorded to like domestic cigarettes.²⁷⁸

V. **Article X:3(b) of the GATT 1994**

A. *Introduction*

182. Thailand appeals the Panel's finding that Thailand acts inconsistently with Article X:3(b) of the GATT 1994 by failing to maintain or institute independent review tribunals or procedures for the prompt review of guarantee decisions.²⁷⁹

183. The Panel considered, first, the meaning of the phrase "administrative action relating to customs matters" in Article X:3(b). The Panel found that the imposition of a guarantee by the Thai Customs Department ("Thai Customs") is "administrative action relating to customs matters" within the meaning of Article X:3(b).²⁸⁰ Second, the Panel considered whether Thailand maintains or instituted tribunals or procedures for the prompt review and correction of guarantee decisions in accordance with Article X:3(b) and found that the Thai system does not comply with that obligation.²⁸¹

²⁷⁶Thailand's first written submission to the Panel, para. 260.

²⁷⁷Furthermore, we are uncertain what Thailand meant to refer to when it stated that "these measures are applied to all products, imported or domestic, subject to VAT", since the measures that had to be justified under Article XX(d) and the chapeau of Article XX were the additional administrative requirements, which are *not* applied to resellers of domestic cigarettes.

²⁷⁸See also Panel Report, para. 7.738.

²⁷⁹Panel Report, paras. 7.1087 and 8.4(g).

²⁸⁰Panel Report, para. 7.1053.

²⁸¹Panel Report, para. 7.1087.

184. On appeal, Thailand requests us to reverse the Panel's finding that Thailand acts inconsistently with Article X:3(b). Thailand contends that the Panel erred in concluding that requiring a guarantee in order to obtain the release of goods pending a final determination of customs value is "administrative action relating to customs matters" within the meaning of Article X:3(b). In the event that we reject this allegation of error and uphold the Panel's finding that requiring a guarantee falls within the scope of Article X:3(b), then Thailand further submits that providing for a right of appeal of a guarantee decision upon final assessment of duties satisfies Thailand's obligations under Article X:3(b).

185. The Philippines contends that the Panel correctly found that the guarantee decisions at issue constitute "administrative action relating to customs matters" within the meaning of Article X:3(b). The Philippines requests us to uphold this finding by the Panel and to reject Thailand's contention that providing for a right of appeal upon final assessment of duties satisfies Thailand's obligations under Article X:3(b).

B. *Article X:3(b) of the GATT 1994*

186. Article X:3(b) stipulates that WTO Members shall maintain judicial, arbitral or administrative tribunals or procedures for the "prompt review and correction of administrative action relating to customs matters." On appeal, Thailand's claims of error relate to the Panel's interpretation and application, in the context of guarantee decisions, of the phrases "administrative action relating to customs matters" and "prompt review" in Article X:3(b).

187. Before turning to our analysis we briefly set out our understanding of the operation of the measure at issue based on the findings of the Panel and on the Panel record. Section 112 of Thailand's Customs Act (the "Thai Customs Act")²⁸² provides that in the event of doubt as to the amount of duty applicable to a specific good, customs officials may undertake a detailed examination. In such circumstances, the goods in question may be released from customs pending the final assessment of duty liability, provided that the importer pays "the amount of the duty declared in the entry by the importer or the exporter" and provided that "an additional sum of money covering the maximum duty payable on the goods" is deposited as a guarantee.²⁸³ If, for example, Thai Customs questions whether the importer's declared price is an appropriate basis for customs valuation, then Thai Customs may examine the matter further. During the examination process, the importer is entitled to withdraw

²⁸²Government of the Kingdom of Thailand, The Customs Act, B.E. 2469 (Panel Exhibit PHL-20).
²⁸³Panel Report, para. 7.1017 (quoting Thai Customs Act, Section 112).

the goods against payment of a guarantee.²⁸⁴ Section 112 further stipulates that the guarantee may be given in the form of a cash deposit or, provided that the Director-General of Thai Customs so approves, it may be given in the form of a "guarantee . . . of the Ministry of Finance or a bank".

188. Once final duty liability has been established, Thai Customs issues a notice of assessment. If the final duty liability exceeds the duty paid on the declared value at the time of entry of the goods, and the guarantee has been given in the form of a cash deposit, then the amount by which it exceeds the declared duty shall be paid immediately from the cash deposit.²⁸⁵ In the event that a guarantee from a bank or the Ministry of Finance has been given, the importer or exporter shall pay the amount that exceeds the declared duty within 30 days after the date of receiving the notice of assessment. If the declared duty paid or the cash deposit exceeds the amount specified in the notice of final assessment, the excess amount, together with interest, is to be refunded to the importer.²⁸⁶

189. Both the importer and the exporter have the right to challenge the final duty assessment before a Board of Appeals (the "BoA") within 30 days from the date of the receipt of the notice of assessment, pursuant to Section 112*sexies* of the Thai Customs Act.²⁸⁷

190. The Panel found that guarantee decisions can be appealed to the Thai Tax Court only when: (i) the importer has been provided with a notice of assessment regarding the final customs value of the goods concerned; and (ii) the importer has challenged that notice before the BoA.²⁸⁸ We understand that the Philippines' claim under Article X:3(b) with respect to appeals of guarantee decisions as well as the Panel's finding with respect thereto, focused on the first of these two mandatory steps, that is, on the requirement under Thai law to await the issuance of the notice of assessment before being able

²⁸⁴Panel Report, para. 7.971. The guarantee must be in an amount equal to the difference between the declared c.i.f. price and a (higher) c.i.f. price provisionally fixed by Thai Customs, plus taxes calculated on the basis of the higher, provisional, c.i.f. price.

²⁸⁵Panel Report, para. 7.856 (quoting Thai Customs Act, Section 112*bis*).

²⁸⁶Panel Report, para. 7.857 (quoting Thai Customs Act, Section 112*quater*).

²⁸⁷In findings that are not subject to appeal, the Panel concluded that the BoA cannot be considered to be free of control or influence from Thai Customs, principally because it is staffed, at least partially, with Thai Customs agents, thus creating the possibility that individuals involved in taking customs decisions might also participate in the review of those same decisions. (Panel Report, paras. 7.1003-7.1005) Accordingly, the Panel considered that the BoA cannot be considered to be a tribunal independent of the agencies entrusted with administrative enforcement within the meaning of Article X:3(b). (*Ibid.*, para. 7.1006)

²⁸⁸Although Thailand contended that guarantee decisions could be appealed directly to the Thai Tax Court without a prior appeal to the BoA, the Panel, based on evidence submitted by the Philippines, found otherwise. (Panel Report, paras. 7.1072-7.1083; see also para. 7.91)

to appeal a guarantee decision.²⁸⁹ Furthermore, we understand the Philippines' claim to relate to guarantee decisions regardless of whether security is provided by means of a cash deposit or by means of a guarantee from a bank or the Ministry of Finance. Finally, with respect to the obligation under Article X:3(b), we note that the Philippines' claim and the Panels' findings focused on whether the Thai system ensures "prompt" review rather than on what constitutes "review and correction" of guarantee decisions.

1. The Meaning of "administrative action relating to customs matters" and "prompt review and correction" in Article X:3(b)

191. Article X:3(b) of the GATT 1994 provides as follows:

Each Member shall maintain, or institute as soon as practicable, judicial, arbitral or administrative tribunals or procedures for the purpose, *inter alia*, of the prompt review and correction of administrative action relating to customs matters. Such tribunals or procedures shall be independent of the agencies entrusted with administrative enforcement and their decisions shall be implemented by, and shall govern the practice of, such agencies unless an appeal is lodged with a court or tribunal of superior jurisdiction within the time prescribed for appeals to be lodged by importers; *Provided* that the central administration of such agency may take steps to obtain a review of the matter in another proceeding if there is good cause to believe that the decision is inconsistent with established principles of law or the actual facts. (original italics)

192. We begin our analysis of the ordinary meaning of the phrase "administrative action relating to customs matters" by considering dictionary definitions of the individual words making up this phrase. The word "action" is defined, *inter alia*, as "[a] thing done, a deed, an act", and as "an act or decision by an executive or legislative body (as of a government or a political party) or by a supranational agency".²⁹⁰ The word "administrative" is defined as "of or relating to the executive branch of a government" and "of or relating to a government agency".²⁹¹ Thus, "administrative action" refers to acts or decisions of the executive branch of a government, or of a government agency.

²⁸⁹We note the Panel's finding that delays in the BoA appeal proceedings at issue illustrate that the interposing process leading to the review by the Thai Tax Court has the "systemic capacity to impede a *prompt* review by an independent tribunal of administrative actions". (Panel Report, para. 7.1015 (original emphasis)) Based on evidence of excessive delays in multiple cases, the Panel concluded that there was a "capacity for delays in the system", and therefore concluded that Thailand acts inconsistently with its obligation under Article X:3(b) of the GATT 1994. (*Ibid.*)

²⁹⁰*Webster's Third New International Dictionary of the English Language, Unabridged*, P. Babcock Gove (ed.) (Merriam-Webster Inc., 1976), p. 21.

²⁹¹*Merriam Webster's Dictionary of Law*, L.P. Wood (ed.) (Merriam-Webster Inc., 1996), p. 13.

193. Furthermore, the word "customs" is defined as "duties levied upon imports as a branch of the public revenue; the department of the Civil Service employed in levying these duties".²⁹² We also note that the *International Convention on the Simplification and Harmonization of Customs Procedures*, as amended²⁹³ (the "*Revised Kyoto Convention*") defines the word "customs" in the context of Chapter 2 of the General Annex to that Convention.²⁹⁴ It refers to the government service responsible for the administration of customs law and the collection of duties and taxes and which also has responsibility for the application of other laws and regulations "relating to the importation, exportation, movement or storage of goods".²⁹⁵ Moreover, we observe that the term "matter", when used with a qualification is defined as "[a] thing, affair, subject, etc., of the kind denoted by, or pertaining to the thing denoted by the qualification."²⁹⁶

194. Turning to the term "relating to", we note that "relate to" is defined, *inter alia*, as "[h]ave some connection with, be connected to".²⁹⁷ The Panel also referred to the Appellate Body's interpretation of the term "related to" in the context of Article XX of the GATT 1994, where the Appellate Body found that for a measure to be "related to" a particular objective, there must be a rational relationship between the measure and the objective pursued.²⁹⁸ For such a rational relationship to exist, the measure must not be disproportionately wide in its scope and reach in relation to its objective. Similarly, in the context of Article X:3(b), we consider that measures must have a rational connection with customs matters to fall within the scope of that provision.

195. Next, we consider the phrase "administrative action relating to customs matters" in its context. We note that the second sentence of Article X:3(b) refers to "agencies entrusted with administrative enforcement". This suggests that "administrative action" in the sense of Article X:3(b) is action by agencies that "enforce", that is, "apply" relevant rules. The reference to "appeals to be lodged by importers" suggests that the relevant administrative action is action that affects "importers".

²⁹²*The Oxford English Dictionary*, 2nd edn, J.A. Simpson and E.S.C. Weiner (eds) (Clarendon Press, Oxford, 1989), Vol. IV, p. 167.

²⁹³*International Convention on the Simplification and Harmonization of Customs Procedures*, done at Kyoto, 18 May 1973, 950 UNTS 269, as amended by the *Protocol of Amendment to the International Convention on the Simplification and Harmonization of Customs Procedures*, done at Brussels, 26 June 1999, 2370 UNTS 27.

²⁹⁴The "General Annex" is the set of provisions applicable to all the customs procedures and practices referred to in the Convention (see Article 1 of the *Revised Kyoto Convention*).

²⁹⁵See also Panel Report, para. 7.1027 (quoting the *Revised Kyoto Convention*, Chapters 2 and 10 of the General Annex).

²⁹⁶*The Oxford English Dictionary*, 2nd edn, J.A. Simpson and E.S.C. Weiner (eds) (Clarendon Press, Oxford, 1989), Vol. IX, p. 481.

²⁹⁷*Shorter Oxford English Dictionary*, 6th edn, A. Stevenson (ed.) (Oxford University Press, 2007), Vol. 2, p. 2519.

²⁹⁸Panel Report, para. 7.1028 (referring to Appellate Body Report, *US – Shrimp*, para. 141).

196. We also consider relevant the context provided by Article 11.1 of the *Agreement on Customs Valuation*. It stipulates:

The legislation of each Member shall provide in regard to a determination of customs value for the right of appeal, without penalty, by the importer or any other person liable for the payment of the duty.

197. This provision imposes an obligation with respect to a specific kind of administrative action, namely, with respect to the determination of customs value. As we see it, the more specific description of one type of administrative action in Article 11.1 of the *Agreement on Customs Valuation*, and the absence of any similar qualification in Article X:3(b) of the GATT 1994, suggest that the obligation contained in Article X:3(b) is not limited to particular types of customs-related "administrative action".

198. We note Thailand's assertion that Articles 7, 9.5, and 13 of the *Anti-Dumping Agreement* "provide[] important context in considering whether the imposition of a guarantee under Article 13 of the [*Agreement on Customs Valuation*] is an 'administrative action relating to customs matters'".²⁹⁹ Thailand argues that the lack of any right to appeal against either provisional anti-dumping measures or "new shipper" guarantees under the *Anti-Dumping Agreement* suggests that guarantees within the meaning of Article 13 of the *Agreement on Customs Valuation* do not fall within the scope of "administrative action relating to customs matters" in Article X:3(b) of the GATT 1994.³⁰⁰

199. Thailand has not explained why these provisions of the *Anti-Dumping Agreement* constitute context relevant to the interpretation of the phrase "administrative action relating to customs matters", and we are not convinced that they do. We see significant conceptual differences between ordinary customs duties and anti-dumping duties. These differences speak against considering the above provisions of the *Anti-Dumping Agreement* as relevant context for the interpretation of Article X:3(b) of the GATT 1994. The *Anti-Dumping Agreement* specifically regulates questions relating to situations of what is widely understood as "unfair trade". These rules authorize a response by importing Members to offset the effects of dumping and re-establish a "level playing field". Article X:3(b), in contrast, is not a specific rule targeting "unfair" trade practices. Rather, it relates to customs matters in general. The conceptual differences between anti-dumping duties and ordinary customs duties are reflected in the different disciplines that apply in respect of the imposition of each type of duty. For example, the imposition of anti-dumping duties requires as a prerequisite, *inter alia*,

²⁹⁹Thailand's appellant's submission, para. 266.

³⁰⁰Thailand's appellant's submission, para. 270.

a determination of injury by the importing Member. In contrast, ordinary customs duties may, within tariff bindings, be applied without any such determination.

200. Even if we were to consider the above provisions of the *Anti-Dumping Agreement* as relevant context for the interpretation of the phrase "administrative action relating to customs matters" in Article X:3(b) of the GATT 1994, we do not see that these provisions support Thailand's position. We do not consider it evident that the customs guarantees at issue should be equated with provisional anti-dumping measures and "new shipper" guarantees provided in the context of an anti-dumping determination. Furthermore, Article 13 of the *Anti-Dumping Agreement* uses language that differs from the language of Article X:3(b) of the GATT 1994, and which makes clear that the review is limited to "final" determinations and determinations of review proceedings under Article 11 of the *Anti-Dumping Agreement*. The absence of any such express limitation in Article X:3(b) suggests, if anything, that the phrase "administrative action relating to customs matters" is not limited in the way Thailand contends.

201. Consequently, we consider that these provisions do not shed light on the ordinary meaning of the phrase "administrative action relating to customs matters" in Article X:3(b). Instead, reading the phrase "administrative action relating to customs matters" in the light of Article X:3(b) as a whole and in the context of Article 11.1 of the *Agreement on Customs Valuation* points to a common intention of WTO Members not to limit the obligation contained in Article X:3(b) to particular types of customs-related "administrative action".

202. Finally, we turn to consider the phrase "administrative action relating to customs matters" in the light of the object and purpose of the treaty. A basic object and purpose of the GATT 1994, as reflected in Article X:3(b), is to ensure due process in relation to customs matters. The Appellate Body referred to this due process objective in *EC – Selected Customs Matters*.³⁰¹ In that vein, the panel in *EC – Selected Customs Matters* stated that Article X:3(b) seeks to "ensure that a trader who has been adversely affected by a decision of an administrative agency has the ability to have that adverse decision reviewed."³⁰² In addition, relating more broadly to Article X:3 of the GATT 1994, the Appellate Body has found that this provision establishes certain minimum standards for transparency and procedural fairness in Members' administration of their trade regulations.³⁰³ While recognizing WTO Members' discretion to design and administer their own laws and regulations, Article X:3 also serves to ensure that Members afford the protection of due process to individual traders. As we see it, the obligation under Article X:3(b) to maintain tribunals or procedures for the

³⁰¹ Appellate Body Report, *EC – Selected Customs Matters*, para. 302.

³⁰² Panel Report, *EC – Selected Customs Matters*, para. 7.536.

³⁰³ See Appellate Body Report, *US – Shrimp*, para. 183.

prompt review and correction of administrative action relating to customs matters is an expression of this due process objective of Article X:3. In the light of the above considerations, we see no error in the Panel's intermediate finding that "administrative action relating to customs matters" encompasses "a wide range of acts applying legal instruments that have a rational relationship with customs matters".³⁰⁴

203. Next, we address the meaning of the phrase "prompt review and correction" in Article X:3(b). The word "prompt" is defined as "ready, quick; done, performed, etc., without delay".³⁰⁵ In addition, the due process objective reflected in Article X:3 of the GATT 1994 suggests that "prompt review and correction" is to be understood as review and correction of administrative action that is performed in a quick and effective manner and without delay. What is quick or performed without delay depends on the context and particular circumstances, including the nature of the specific type of action to be reviewed and corrected. Whether a system does or does not ensure prompt review thus cannot be determined in the abstract. We therefore agree with the Panel that the nature of the specific administrative action at issue informs the meaning of the word "prompt" in the particular circumstances of a Member's domestic system.³⁰⁶

204. We further note that Article X:3(b) refers to "review and correction" of administrative action. The word "review" is defined as "[a]n inspection, an examination", or in the legal context as "[c]onsideration of a judgment, sentence, etc., by some higher court or authority".³⁰⁷ The word "correction" is defined as "[t]he action of putting right or indicating errors".³⁰⁸ The reference to "correction" indicates that Article X:3(b) requires more than mere declaratory action or *ex post* review of whether administrative action conforms to domestic law or not. Compliance with the obligation to maintain tribunals or procedures for the "correction" of administrative action relating to customs matters requires that Members ensure that their system of review provides for the relevant administrative action to be set right.

205. Finally, we note that Article X:3(b) does not prescribe one particular type of review or correction of administrative action relating to customs matters. Instead it refers to "judicial, arbitral or

³⁰⁴ Panel Report, para. 7.1029.

³⁰⁵ *Shorter Oxford English Dictionary*, 6th edn, A. Stevenson (ed.) (Oxford University Press, 2007), Vol. 2, p. 2367. See also Panel Report, para. 7.1085.

³⁰⁶ Panel Report, para. 7.1086. We also note the Panel's statement, elsewhere in its Report, that "showing specific instances where prompt review was not provided could nonetheless help to prove a violation of Article X:3(b) to the extent that the non-promptness in the review process concerned can be linked to a systemic flaw in the tribunal or procedure maintained by a Member." (*Ibid.*, para. 7.997)

³⁰⁷ *Shorter Oxford English Dictionary*, 6th edn, A. Stevenson (ed.) (Oxford University Press, 2007), Vol. 2, p. 2566.

³⁰⁸ *Shorter Oxford English Dictionary*, 6th edn, A. Stevenson (ed.) (Oxford University Press, 2007), Vol. 1, p. 527.

administrative tribunals or procedures". This suggests that there are a variety of ways in which a Member may comply with the obligation of maintaining tribunals or procedures for prompt review and correction of administrative action relating to customs matters, provided that, *inter alia*, such tribunals and procedures are independent of the agencies entrusted with administrative enforcement as required by the second sentence of Article X:3(b).

2. Application of Article X:3(b) to the Facts of the Dispute

(a) Administrative Action Relating to Customs Matters

206. We now turn to consider whether the Panel correctly found that decisions by Thai Customs on the guarantees required in order to have goods released pending a final duty assessment constitute "administrative action relating to customs matters". The Panel noted the participants' agreement that customs valuation determinations fall within the scope of "administrative action relating to customs matters" in Article X:3(b).³⁰⁹ On appeal, as before the Panel, the participants' disagreement concerns whether the imposition of a guarantee as a security to cover ultimate duty liability in exchange for release of the goods also falls within the scope of Article X:3(b).

207. We recall that, pursuant to Section 112 of the Thai Customs Act, customs officials may, in case of doubt as to the amount of duty applicable to a specific good, undertake a detailed examination. In that event, the goods in question may be released from customs pending the final assessment of duty liability, provided that the importer pays the declared duty and that a cash deposit or guarantee covering the maximum duty payable on the goods is given.³¹⁰

208. We note that the Panel took into account the following definition of "guarantee" from *Black's Law Dictionary*: "[s]omething given or existing as security, such as to fulfill a future engagement or a condition subsequent."³¹¹ Read in the light of the present case, the "future engagement" is the payment of ultimate customs duties. We further note, as did the Panel, that Article 13 of the *Agreement on Customs Valuation* refers to the concept of "guarantee" in relation to customs valuation. The first sentence of Article 13 refers to different forms in which a guarantee may be provided. The second sentence, while stipulating an obligation for Members to provide for the possibility to obtain the release of goods pending a final determination of customs value, leaves considerable discretion to Members in determining the form of the guarantee to be provided. Thus, we understand that, in customs matters, guarantees include legal instruments of different forms, provided in order to secure

³⁰⁹Panel Report, para. 7.992.

³¹⁰Panel Report, para. 7.1017 (quoting Thai Customs Act, Section 112). See *supra*, paras. 187 and 188.

³¹¹Panel Report, footnote 1752 to para. 7.1037 (quoting *Black's Law Dictionary*, 7th edn., B.A. Garner (ed.) (West Group, 1999), p. 711).

the payment of ultimate customs duties. We also observe that the decisions of customs authorities imposing or accepting guarantees may relate, *inter alia*, to the amount or to the form of the security being provided.

209. The customs guarantee decisions at issue in this dispute are actions taken by Thailand's customs authorities.³¹² As such, they are acts of the executive branch of government and thus constitute administrative action in the sense of Article X:3(b). Furthermore, because they serve to secure the payment of ultimate customs duties, these guarantee decisions are connected to "customs matters" and thus fall within the scope of Article X:3(b).

210. On appeal, Thailand submits that the imposition of a guarantee does not constitute "administrative action" within the meaning of Article X:3(b) because it constitutes only an administrative step of a provisional nature. Thailand asserts that the Appellate Body's statement in *US – Shrimp (Thailand) / US – Customs Bond Directive* that "taking security for the full and final payment of duties should be viewed as a component of the imposition and collection of anti-dumping or countervailing duties" suggests that the Appellate Body characterized a security as a "provisional measure".³¹³ Thailand submits that the Appellate Body's rationale in *US – Shrimp (Thailand) / US – Customs Bond Directive* applies equally to the guarantees at issue in this dispute.

211. We disagree with Thailand. In our view, the Appellate Body's statement in *US – Shrimp (Thailand) / US – Customs Bond Directive*, that securities under the *Ad Note* to paragraphs 2 and 3 of Article VI of the GATT 1994 are accessory to final duty liability, does not stand for the proposition that such securities are "provisional" measures. The fact that two legal instruments, in that case, the security and the imposition of anti-dumping duties, are interlinked, does not, without more, suggest that one of the two instruments is necessarily provisional in nature. There, the Appellate Body explained that the "security [was] intended to provide a protection against the non-payment risk that might arise from the differences between the amount collected at the time of importation and the liability that may be finally determined."³¹⁴ This statement is consistent with the view that a security is a final and not a provisional measure with respect to that intention to avoid the risk of non-payment.

212. The Panel referred to this part of the Appellate Body report in *US – Shrimp (Thailand) / US – Customs Bond Directive*, and concluded that, in the particular circumstances of customs valuation, the imposition of a guarantee is intended to serve the distinct purpose of securing the payment of the

³¹²In the following paragraphs, when referring to the Thai system, and unless otherwise indicated, we use the word "guarantees" to cover both cash deposits and guarantees from a bank or the Ministry of Finance, within the meaning of Section 112 of the Thai Customs Act.

³¹³Thailand's appellant's submission, para. 240 (quoting Appellate Body Report, *US – Shrimp (Thailand) / US – Customs Bond Directive*, para. 231).

³¹⁴Appellate Body Report, *US – Shrimp (Thailand) / US – Customs Bond Directive*, para. 221.

ultimate amount of customs duty pending a final determination of duty liability by customs.³¹⁵ We agree with that characterization of the guarantee. With respect to the purpose of securing payment of customs duties, the guarantee is the final measure, not merely an intermediate step.

213. Thailand also argues that Article X:1 of the GATT 1994 lists several different types of measures, such as "[l]aws, regulations, judicial decisions and administrative rulings of general application", but contains no reference to guarantees and other securities. For Thailand, this suggests that the drafters did not intend Article X:3(b) to apply to guarantee decisions.³¹⁶ We are not persuaded by this argument. It is built on the premise that Article X:1 and Article X:3(b) relate to the same types of measures. However, this is not necessarily so. Article X:1 and Article X:3(b) of the GATT 1994 stipulate distinct obligations. Both use general, albeit different language. Neither provision uses the word "guarantee". Therefore, we see no basis for an assumption that the obligation of Article X:3(b) extends only to measures falling within the scope of Article X:1 of the GATT 1994.

214. Finally, Thailand argues that the concept of due process does not compel the conclusion that there must be a right of appeal against guarantee decisions. Thailand submits that guarantee decisions are not *final* administrative acts but constitute merely intermediate steps on the way towards a final customs valuation decision and that, as such, they do not constitute "administrative action relating to customs matters" in the sense of Article X:3(b). Thailand refers to the doctrine of "ripeness", reflecting the concept of deference to the expertise of an administrative agency. Thailand argues that it does not make practical sense to require courts to intervene in a decision-making process within the technical expertise of an administrative agency, before that agency has had an opportunity fully to consider the issue and render a final decision.³¹⁷

215. As already noted above, we do not consider that a guarantee is merely an intermediate step within the administrative procedure leading up to the final assessment of customs duty. Rather, a requirement to provide a guarantee in exchange for release of the goods has an administrative content of its own. As the Panel correctly found, the guarantee is a device allowing, on the one hand, the importer to withdraw their goods from customs, and, on the other hand, securing the payment of the ultimate customs duty.³¹⁸ It is a final, and not an intermediate, administrative act with respect to these particular objectives. The fact that a guarantee provides security for a claim stemming from another

³¹⁵Panel Report, para. 7.1039 (referring to Appellate Body Report, *US – Shrimp (Thailand)* / *US – Customs Bond Directive*, para. 221).

³¹⁶Thailand's appellant's submission, para. 253.

³¹⁷*Thailand's appellant's submission*, para. 278 (referring to United States Supreme Court, *Abbott Laboratories v. Gardner*, 387 U.S. 136 (1967)).

³¹⁸Panel Report, paras. 7.1039 and 7.1040.

administrative action does not change the fact that the imposition of a guarantee is an administrative action in its own right.

216. For these reasons, we agree with the Panel that the "imposition of a guarantee is an 'administrative action relating to customs matters' within the meaning of Article X:3(b)".³¹⁹

(b) Prompt Review and Correction

217. In the event that we uphold the Panel's finding that guarantee decisions fall within the scope of "administrative action relating to customs matters", then Thailand appeals the Panel's finding that Thailand's provision of a right of appeal against guarantee decisions at the time when the notice of final assessment is issued does not satisfy the obligation in Article X:3(b).³²⁰ Because we have agreed with the Panel that guarantee decisions fall within the scope of "administrative action relating to customs matters" within the meaning of Article X:3(b), the condition on which this part of Thailand's appeal is predicated is fulfilled. Consequently, we now turn to consider whether the Panel erred in finding that Thailand's provision of a right of appeal against the imposition of a guarantee only at the time when the notice of final assessment is issued does not satisfy the obligation prescribed in Article X:3(b).

218. In its assessment of whether the availability of an appeal of a guarantee decision to the Thai Tax Court following the issuance of the notice of assessment satisfies Article X:3(b), the Panel considered that the question of whether a Member provides for prompt review and correction of administrative action has to be considered in the light of the nature of the specific administrative action concerned.³²¹ The Panel also took into account that guarantee decisions could, depending on the situation, entail a heavy financial burden on importers. With respect to the present dispute, the Panel observed that there is no time-frame for the issuance of a notice of assessment, and that in some cases this has taken "up to 10 months".³²² The Panel also noted that following the issuance of a final assessment, an importer must first exhaust an appeal to the BoA before it can appeal to the Thai Tax Court.³²³ In the context of the Philippines' claim pursuant to Article X:3(b) relating to guarantee decisions, neither the Philippines nor the Panel addressed the length of time taken for BoA proceedings.³²⁴ The Panel then found that if a system does not make available the review of a

³¹⁹Panel Report, para. 7.1053.

³²⁰Thailand's appellant's submission, para. 294.

³²¹Panel Report, para. 7.1086.

³²²Panel Report, para. 7.1084.

³²³Panel Report, paras. 7.1072-7.1083; see also para. 7.91.

³²⁴Elsewhere in its Report, in the context of a claim by the Philippines under Article X:3(a), the Panel observed that specific appeals of customs valuation decisions lodged by PM Thailand between 2000 and 2002 took, on average, two years and six months for the BoA to complete. (Panel Report, para. 7.953)

guarantee decision until the final assessment has been made in respect of the customs duty, an importer may face a situation where it will not be able to withdraw imported goods due to a guarantee value set at an excessively high level.³²⁵ The Panel concluded that this is not compatible with the obligation under Article X:3(b) to maintain independent tribunals or procedures for the prompt review of the concerned administrative action.³²⁶

219. Above, we have set out the reasons why we agree with the Panel that the nature of the specific administrative action at issue informs the meaning of the word "prompt" in the particular circumstances of any given case. Turning to the situation in this dispute, we consider that the character of a guarantee is relevant in determining what can be regarded as "prompt" with respect to the review of guarantee decisions. As set out above, a "guarantee" is defined as "[s]omething given or existing as security, such as to fulfill a future engagement or a condition subsequent".³²⁷ This definition clarifies a key element of a guarantee, namely, its relation to a future event. A guarantee is tied to, but distinct from, the fulfilment of an engagement or condition in the future. Accordingly, a guarantee is effective as a security from the time it is given up to the time when the engagement or condition is fulfilled. Once the future condition is fulfilled, the guarantee no longer serves as a security.

220. We also recall our above consideration that the due process objective reflected in Article X:3 of the GATT 1994 suggests that "prompt review and correction" is to be understood as review and correction of administrative action that is performed in a quick and effective manner and without delay. It follows that the mechanism for the review of administrative action relating to customs matters must permit review to be timely and effective. In the particular circumstances of a guarantee, which is effective as a security from the time it is given until the time when the engagement or condition is fulfilled, we consider that, for a review to be considered timely and effective, it must at least be possible to challenge the guarantee during the time it serves as a security. This is so because it is during the period of time that a guarantee is required that importers are most affected by the guarantee decision.

221. In the present case, the Panel understood Thailand's measure to operate in a way that allows a challenge of the guarantee decision only once the notice of assessment is issued and the BoA has reviewed that final assessment. As set out above, Thai law provides that once the ultimate duty has been established, and if the ultimate duty liability exceeds the duty paid on the declared value at the time of entry of the goods, the amount by which it exceeds the declared duty shall be paid

³²⁵Panel Report, para. 7.1087.

³²⁶Panel Report, para. 7.1087.

³²⁷*Black's Law Dictionary*, 7th edn, B.A. Garner (ed.) (West Group, 1999), p. 711.

immediately from the cash deposit if cash was deposited as security.³²⁸ In the event that a guarantee by a bank or the Ministry of Finance has been given, the importer or exporter shall pay the amount that exceeds the declared duty within 30 days after the date of receiving the notice of assessment. If the duty initially paid or the cash deposit exceeds the amount specified in the notice of final assessment, the excess amount, together with interest, is to be refunded to the importer.³²⁹ Thus, with the fulfilment of the condition—in this case payment of the ultimate duty—the security function of the guarantee ceases.³³⁰ In providing that a guarantee can only be challenged once the notice of assessment has been issued, Section 112 of the Thai Customs Act invariably delays review of guarantee decisions and thereby shields guarantee decisions from challenge throughout the period in which they serve as a security and in which traders are most affected by these decisions.³³¹ We recognize that, where security has been given in the form of a guarantee by a bank or the Ministry of Finance, such a guarantee could be challenged within the short time period between the issuance of a notice of assessment and payment of the ultimate duty. Even in such cases, however, the review system maintained by Thailand imposes delays that are essentially coextensive with the lifetime of a guarantee's security function. Thus, this system does not ensure prompt review of the relevant administrative action.

222. For the above reasons, we find no error in the Panel's conclusion that Thailand's system for the review of guarantee decisions is not compatible with the obligation under Article X:3(b) to provide for the prompt review of administrative action relating to customs matters because such review is not available until after the final assessment of customs duty has been made. Consequently, we uphold the Panel's finding, in paragraph 8.4(g) of the Panel Report, that Thailand acts inconsistently with Article X:3(b) of the GATT 1994 by failing to maintain or institute independent review tribunals or procedures for the prompt review of guarantee decisions.³³²

³²⁸Panel Report, para. 7.856 (quoting Thai Customs Act, Section 112*bis*).

³²⁹Panel Report, para. 7.857 (quoting Thai Customs Act, Section 112*quater*).

³³⁰This occurs either immediately upon issuance of the notice of assessment when security has been given in the form of a cash deposit, or upon full payment of the assessed duty within 30 days when security has been given in the form of a guarantee by a bank or the Ministry of Finance.

³³¹We also note that the fact that a guarantee decision cannot be challenged before the issuance of the notice of assessment may in certain cases prevent an importer from obtaining release of goods from customs pending determination of final customs duties or may even lead an importer to cancel a transaction, for instance, where the amount of a guarantee is so high that the importer is unable to provide it. (See Panel Report, para. 7.1086; and Philippines' appellee's submission, para. 312)

³³²See also Panel Report, para. 7.1087.

VI. Findings and Conclusions

223. For the reasons set out in this Report, the Appellate Body:

- (a) with respect to the Panel's findings under Article III of the GATT 1994 concerning Thailand's treatment of resellers of imported cigarettes, as compared to its treatment of resellers of like domestic cigarettes:
- (i) upholds the Panel's finding, in paragraph 8.3(b) of the Panel Report³³³, that Thailand acts inconsistently with Article III:2, first sentence, of the GATT 1994 by subjecting imported cigarettes to VAT liability in excess of that applied to like domestic cigarettes;

(ii) with respect to the Panel's findings under Article III:4 of the GATT 1994:

- finds that the Panel did not err in concluding, in paragraph 7.738 of the Panel Report, that Thailand accords less favourable treatment to imported cigarettes than to like domestic cigarettes;
- finds that Thailand has not established that the Panel failed to ensure due process and, thus, to comply with its duty under Article 11 of the DSU to make an objective assessment of the matter, by accepting and relying on Exhibit PHL-289 without affording Thailand an opportunity to comment on that evidence;
- reverses the Panel's findings, in paragraph 7.758 of the Panel Report, regarding Article XX(d) of the GATT 1994; but finds that Thailand failed to establish that its measure is justified under Article XX(d) of the GATT 1994; and
- upholds the Panel's finding, in paragraph 8.3(c) of the Panel Report³³⁴, that Thailand acts inconsistently with Article III:4 of the GATT 1994 by subjecting imported cigarettes to less favourable treatment than that accorded to like domestic cigarettes; and

- (b) upholds the Panel's finding, in paragraph 8.4(g) of the Panel Report³³⁵, that Thailand acts inconsistently with Article X:3(b) of the GATT 1994 by failing to maintain or institute independent tribunals or procedures for the prompt review of guarantee decisions.

224. The Appellate Body recommends that the DSB request Thailand to bring its measures, found in this Report, and in the Panel Report as modified by this Report, to be inconsistent with the *Agreement on Customs Valuation* and the GATT 1994, into conformity with its obligations under those Agreements.

Signed in the original in Geneva this 20th day of May 2011 by:

Peter Van den Bossche
Presiding Member

Ricardo Ramirez-Hernández
Member

Yuejiao Zhang
Member

³³³See also Panel Report, para. 7.644.

³³⁴See also Panel Report, para. 7.738.

³³⁵See also Panel Report, para. 7.1087.

ANNEX I

WORLD TRADE ORGANIZATION

WT/DS371/8
23 February 2011
(11-0961)

Original: English

THAILAND – CUSTOMS AND FISCAL MEASURES ON CIGARETTES FROM THE PHILIPPINES

Notification of an Appeal by Thailand under Article 16.4 and Article 17 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), and under Rule 20(1) of the Working Procedures for Appellate Review

The following notification, dated 22 February 2011, from the Delegation of Thailand, is being circulated to Members.

Pursuant to Articles 16.4 and 17 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 20 of the *Working Procedures for Appellate Review*, Thailand hereby notifies the Dispute Settlement Body of its decision to appeal to the Appellate Body certain issues of law and legal interpretation covered in the Panel Report entitled *Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines* (WT/DS371/R), which was circulated on 15 November 2010 (the "Panel Report"). Pursuant to Rules 20(1) and 21(1) of the *Working Procedures for Appellate Review*, Thailand is simultaneously filing this Notice of Appeal and its Appellant's Submission with the Appellate Body Secretariat.

As described below, Thailand appeals certain of the Panel's findings on measures related to Thailand's Value Added Tax ("VAT") regime for cigarettes, as well as Thailand's regime for the acceptance of guarantees to secure the importer's ultimate liability for customs duties pending final determination of the customs value of imported goods.

Thailand seeks review by the Appellate Body of the following errors of law and legal interpretation by the Panel in the Panel Report:

I. The Panel's finding under Article III:2 of the GATT 1994

1. The Panel erred in law in finding a violation of Article III:2, first sentence, of the GATT 1994, not on the basis of the fiscal burdens imposed on imported and domestic products under Thai VAT law, but solely on the basis of the administrative requirements of Thailand's VAT system

and the consequences of non-compliance with those requirements.¹ The administrative requirements of Thailand's VAT system and the consequences of non-compliance are measures that fall within the scope of Article III:4, not Article III:2, first sentence, of the GATT 1994.

2. Even if the Panel were correct to address the administrative requirements of Thai VAT law under Article III:2, first sentence, of the GATT 1994, the Panel erred in law in finding a violation of Article III:2 solely on the basis of administrative requirements whereby resellers must file a VAT form declaring and offsetting their VAT credits and liabilities on re-sales of imported cigarettes for each month and whereby VAT credits are granted only with respect to actual, documented purchases of goods such as imported cigarettes.² These requirements cannot, as a matter of law, lead to taxation of imported products in excess of that imposed on domestic products within the meaning of Article III:2, first sentence.

II. The Panel's finding under Articles III:4 and XX(d) of the GATT 1994

3. The Panel erred in law in finding that certain additional administrative requirements for re-sales of imported cigarettes amounted to less favourable treatment of imported products within the meaning of Article III:4 of the GATT 1994 on the basis of a finding solely that these administrative requirements could potentially affect the competitive position of imported cigarettes that is not supported by its factual analysis and findings.³

4. The Panel erred in law in rejecting Thailand's defence under Article XX(d) of the GATT 1994 to the Philippines' claim under Article III:4 on the ground that it had already found the measures with respect to which Thailand asserted the defence (the additional administrative requirements for re-sales of imported cigarettes) to be inconsistent with Article III:4 of the GATT 1994.⁴ Instead, the Panel should have looked first at whether the laws with respect to which Thailand sought to achieve compliance were otherwise consistent with the GATT 1994.⁵

5. The Panel erred in law by accepting and relying on evidence that was submitted at the last opportunity for the parties to submit their views to the Panel and that was the only evidence to support one aspect of the Panel's finding under Article III:4 and upon which Thailand had no opportunity to comment.⁶ The Panel acted inconsistently with Article 11 of the DSU and paragraph 15 of its Working Procedures and also failed to protect Thailand's due process rights by accepting and relying on this evidence.⁷

III. The Panel's finding under Article X:3(b) of the GATT 1994

6. The Panel erred in law in finding that the provisional step of accepting a guarantee in the circumstances provided for in Article 13 of the Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994 ("GVA") constitutes an "administrative action relating to customs matters" within the meaning of and subject to a right of review under Article X:3(b) of the GATT 1994.⁸

¹See Panel Report, paras. 6.98-6.120, paras. 7.568-7.644, and para. 8.3(b). This appeal does not include the Panel's separate finding under Article III:2, first sentence, in paragraphs 7.567 and 8.3(a) of the Panel Report.

²See Panel Report, paras. 6.98-6.120; paras. 7.613-7.637; and 8.3(b).

³See Panel Report, paras. 7.724-7.738 and para. 8.3(c).

⁴See Panel Report, paras. 7.749-7.758.

⁵See Panel Report, paras. 7.738 and para. 8.3(c).

⁶See Panel Report, paras. 6.122-6.128, paras. 7.684-7.704, and para. 8.3(c).

⁷See Panel Report, paras. 6.122-6.128, paras. 7.684-7.704, and para. 8.3(c).

⁸See Panel Report, paras. 7.1016-7.1053 and para. 8.4(g).

7. Even if the Panel were correct that the acceptance of a guarantee under Article 13 of the CVA constitutes an "administrative action relating to customs matters" within the meaning of Article X:3(b), the Panel erred in law in finding that providing a right of review of the taking of a guarantee at the time of the final determination of duty liability cannot satisfy the obligation in Article X:3(b).⁹

Thailand respectfully requests the Appellate Body to reverse the findings of the Panel identified in this Notice of Appeal.

⁹See Panel Report, paras. 7.1054-7.1087, and para. 8.4(g).

World Trade Organization

Philippines – Taxes on Distilled Spirits

Report of the Appellate Body, 21 December 2011

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PHILIPPINES – TAXES ON DISTILLED SPIRITS

AB-2011-6

Reports of the Appellate Body

Note:

The Appellate Body is issuing these Reports in the form of a single document constituting two separate Appellate Body Reports: WT/DS396/AB/R; and WT/DS403/AB/R. The cover page, preliminary pages, Sections I through VI and the Annexes are common to both Reports. The page header throughout the document bears two document symbols, WT/DS396/AB/R and WT/DS403/AB/R, with the following exceptions: Section VII on pages EU-97 to EU-99, which bears the document symbol for and contains the Appellate Body's findings and conclusions in the Appellate Body Report WT/DS396/AB/R; and Section VII on pages US-97 to US-99, which bears the document symbol for and contains the Appellate Body's findings and conclusions in the Appellate Body Report WT/DS403/AB/R.

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Short Title	Full case title and citation
<i>Australia – Apples</i>	Appellate Body Report, <i>Australia – Measures Affecting the Importation of Apples from New Zealand</i> , WT/DS367/AB/R, adopted 17 December 2010
<i>Australia – Salmon</i>	Appellate Body Report, <i>Australia – Measures Affecting Importation of Salmon</i> , WT/DS18/AB/R, adopted 6 November 1998, DSR 1998:VIII, 3327
<i>Border Tax Adjustments</i>	Report of the Working Party, <i>Border Tax Adjustments</i> , L/3464, adopted 2 December 1970, BISD 18S/97
<i>Brazil – Retreaded Tyres</i>	Appellate Body Report, <i>Brazil – Measures Affecting Imports of Retreaded Tyres</i> , WT/DS332/AB/R, adopted 17 December 2007, DSR 2007:IV, 1527
<i>Canada – Periodicals</i>	Appellate Body Report, <i>Canada – Certain Measures Concerning Periodicals</i> , WT/DS31/AB/R, adopted 30 July 1997, DSR 1997:I, 449
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<i>Japan – Alcoholic Beverages II</i>	Appellate Body Report, <i>Japan – Taxes on Alcoholic Beverages</i> , WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, DSR 1996:1, 97

LIST OF ABBREVIATIONS USED IN THESE REPORTS

Short Title	Full case title and citation
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<i>US – Steel Safeguards</i>	Appellate Body Report, <i>United States – Definitive Safeguard Measures on Imports of Certain Steel Products</i> , WT/DS248/AB/R, WT/DS249/AB/R, WT/DS251/AB/R, WT/DS252/AB/R, WT/DS253/AB/R, WT/DS254/AB/R, WT/DS258/AB/R, WT/DS259/AB/R, adopted 10 December 2003, DSR 2003:VII, 3117
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<i>US – Upland Cotton (Article 21.5 – Brazil)</i>	Appellate Body Report, <i>United States – Subsidies on Upland Cotton – Recourse to Article 21.5 of the DSU by Brazil</i> , WT/DS267/AB/RW, adopted 20 June 2008, DSR 2008:III, 809
<i>US – Wheat Gluten</i>	Appellate Body Report, <i>United States – Definitive Safeguard Measures on Imports of Wheat Gluten from the European Communities</i> , WT/DS166/AB/R, adopted 19 January 2001, DSR 2001:II, 717

Abbreviation	Description
ATC	<i>Agreement on Textiles and Clothing</i>
BIR	Philippines' Bureau of Internal Revenue
DSB	Dispute Settlement Body
DSU	<i>Understanding on Rules and Procedures Governing the Settlement of Disputes</i>
Expert study	T. Allen, "Tasting and Congener Content Analysis of 31 Distilled Spirits" (30 September 2010) (Panel Exhibit PH-30 (BCJ))
GATT 1994	<i>General Agreement on Tariffs and Trade 1994</i>
HS	Harmonized Commodity Description and Coding System of the World Customs Organization
HSEN	HS Explanatory Note
ml	millilitre
NIRC	Philippines' National Internal Revenue Code of 1997
NRP	net retail price
Panel Reports	Panel Reports, <i>Philippines – Taxes on Distilled Spirits</i> , WT/DS396/R / WT/DS403/R, 15 August 2011
PHP	Philippine pesos
ppl	per proof litre
Substitutability studies	<i>Euromonitor International</i> , "Consumer perceptions regarding substitutability in the Philippines distilled spirits market" (August 2010) (Panel Exhibits EU-41 and US-41); and M.J. Abrenica and J. Ducanes, "On Substitutability between Imported and Local Distilled Spirits" (University of Philippines School of Economics Foundation, 10 October 2010) (Panel Exhibit PH-49)
<i>Working Procedures</i>	<i>Working Procedures for Appellate Review</i> , WT/AB/WP/6, 16 August 2010
WTO	World Trade Organization

WORLD TRADE ORGANIZATION
APPELLATE BODY

Philippines – Taxes on Distilled Spirits

Philippines, *Appellant/Appellee*
European Union, *Other Appellant/Appellee*
United States, *Appellee*

Australia, *Third Participant*
China, *Third Participant*
Colombia, *Third Participant*
India, *Third Participant*
Mexico, *Third Participant*
Separate Customs Territory of Taiwan, Penghu,
Kinmen and Matsu, *Third Participant*
Thailand, *Third Participant*

AB-2011-6

Present:

Van den Bossche, Presiding Member
Hillman, Member
Ramírez-Hernández, Member

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I. Introduction

1. The Philippines and the European Union each appeals certain issues of law and legal interpretations developed in the Panel Reports, *Philippines – Taxes on Distilled Spirits*¹ (the "Panel Reports"). The Panel was established to consider complaints by the European Union² and the United States³ regarding the consistency of the Philippines' excise tax regime applicable to distilled spirits with Article III:2, first and second sentences, of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994").⁴

2. Pursuant to a joint request from the European Union and the United States, the Panel issued its findings in the form of a single document containing two separate reports with common descriptive and analytical sections but separate conclusions and recommendations for each complaining party, each of which bears only the document symbol for that report.⁵ The Panel Reports were circulated to Members of the World Trade Organization (the "WTO") on 15 August 2011.

3. Before the Panel, the European Union and the United States claimed that the Philippines has acted inconsistently with Article III:2, first and second sentences, of the GATT 1994, in applying different tax treatment to distilled spirits produced from the sap of the *nipa*, coconut, cassava, *camote*, or *buri* palm, or from juice, syrup, or sugar of the cane ("designated raw materials"), and to distilled spirits made from other raw materials ("non-designated raw materials").⁶ For the reasons set out in its Reports, the Panel found, in relation to the complaint by the European Union, that the Philippines has acted inconsistently with its obligations under Article III:2, first sentence, of the GATT 1994.⁷ More specifically, the Panel found that:

... through its excise tax, the Philippines subjects imported distilled spirits made from raw materials other than those designated in its legislation to internal taxes in excess of those applied to like domestic spirits made from the designated raw materials, and is thus acting in a manner inconsistent with Article III:2, first sentence, of the GATT 1994.⁸

4. The Panel found, in relation to the complaint by the United States, that the Philippines has acted inconsistently with its obligations under Article III:2, first and second sentences, of the GATT 1994. More specifically, the Panel found that:

(a) through its excise tax, the Philippines subjects imported distilled spirits made from raw materials other than those designated in its legislation to internal taxes in excess of those applied to like domestic spirits made from the designated raw materials, and is thus acting in a manner inconsistent with Article III:2, first sentence, of the GATT 1994⁹; and

(b) through its excise tax, the Philippines applies dissimilar internal taxes on domestic distilled spirits made from designated raw materials and to directly competitive or substitutable imported distilled spirits made from other raw materials in a manner so as to afford protection to the Philippine domestic production of distilled spirits and is thus acting in a manner inconsistent with Article III:2, second sentence, of the GATT 1994.¹⁰

¹WT/DS396/R (the "EU Panel Report"); WT/DS403/R (the "US Panel Report"), 15 August 2011.

²Request for the Establishment of a Panel by the European Union, WT/DS396/4.

³Request for the Establishment of a Panel by the United States, WT/DS403/4.

⁴At its meetings on 19 January and 20 April 2010, the Dispute Settlement Body (the "DSB") established a single panel for both complaints in accordance with Articles 6 and 9 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"). (See WT/DS396/5, WT/DS403/5, para. 1)

⁵Panel Reports, para. 8.1.

⁶Panel Reports, para. 2.3.

⁷The Panel abstained from making findings with respect to the European Union's claim under Article III:2, second sentence, of the GATT 1994, because it considered that this claim was advanced as an alternative claim to be addressed should the Panel not find that the measure at issue is inconsistent with the first sentence of the same provision. (EU Panel Report, WT/DS396/R, para. 8.3)

⁸EU Panel Report, WT/DS396/R, para. 8.2.

⁹US Panel Report, WT/DS403/R, para. 8.2(a).

¹⁰US Panel Report, WT/DS403/R, para. 8.2(b).

5. On 23 September 2011, the Philippines notified the Dispute Settlement Body (the "DSB") of its intention to appeal certain issues of law covered in the Panel Reports and certain legal interpretations developed by the Panel, pursuant to Articles 16.4 and 17 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), and filed a Notice of Appeal¹¹ and an appellant's submission¹² pursuant to Rules 20 and 21, respectively, of the *Working Procedures for Appellate Review*¹³ (the "*Working Procedures*").

6. On 28 September 2011, the European Union notified the DSB of its intention to appeal certain issues of law covered in the Panel Reports and certain legal interpretations developed by the Panel, pursuant to Articles 16.4 and 17 of the DSU, and filed a Notice of Other Appeal¹⁴ and an other appellant's submission pursuant to Rule 23(1) and (3), respectively, of the *Working Procedures*. On 11 October 2011, the European Union, the Philippines, and the United States each filed an appellee's submission.¹⁵ On 14 October 2011, Australia and Mexico each filed a third participant's submission¹⁶ and, on the same day, China, India, and the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu each notified its intention to appear at the oral hearing as a third participant.¹⁷ On 17 and 20 October 2011, Colombia and Thailand, respectively, notified its intention to appear at the oral hearing as a third participant.¹⁸

7. The oral hearing in this appeal was held on 25 and 26 October 2011. The participants and one of the third participants, Australia, made oral statements. The participants and third participants responded to questions posed by the Members of the Appellate Body Division hearing the appeal.

II. Arguments of the Participants and the Third Participants

A. Claims of Error by the Philippines – Appellant

8. The Philippines maintains that the text of, and jurisprudence on, Article III:2 of the GATT 1994 make clear that this treaty provision does not prohibit the application of differential taxes to products that are not "like" or "directly substitutable", both because of their different physical characteristics and because their price is well beyond the means of the consumer. The Philippines claims that the Panel made a number of legal errors relating to the interpretation and application of this provision. According to the Philippines, the Panel's errors in this case are not a matter of failing to weigh the evidence correctly, but that the Panel misinterpreted the relevance of the evidence, and in certain instances ignored evidence, because it was applying the wrong legal standard.

9. In the view of the Philippines, the Panel treated this dispute as simply another Article III:2 trade dispute involving distilled spirits. In this respect, the Philippines argues, the Panel failed to recognize important differences in this case, which have consequences for the interpretation and application of Article III:2 in a manner that is faithful to its text and its object and purpose. The Philippines explains that the challenged measure makes no distinction based on the country of origin of the products. The specific tax provided for under Section 141(a) of the Philippines' National Internal Revenue Code of 1997 (the "NIRC") applies to distilled spirits produced from the designated raw materials (provided that such materials are produced commercially in the country where they are processed into distilled spirits), while distilled spirits produced from any other raw material are taxed at the specific tax levels provided for under Section 141(b) of the NIRC. The Philippines points out that the raw material base, not the country of origin, is the key to determining whether the lower tax of Section 141(a), or the higher, tiered taxes of Section 141(b), apply.

On 20 October 2011, Thailand submitted its delegation list for the oral hearing to the Appellate Body Secretariat and the participants and third participants in this dispute. Without prejudice to rulings the Appellate Body may make in future appeals, we have interpreted Thailand's action as a notification expressing its intention to attend the oral hearing pursuant to Rule 24(4) of the *Working Procedures*. While we wish to emphasize that strict compliance with Rule 24(4) of the *Working Procedures* requires *written* notification to the Secretariat that expresses an intention to appear at the oral hearing, we are satisfied that, in this case, the lack of strict compliance with Rule 24(4) did not raise any due process concerns.

¹¹WT/DS396/7, WT/DS403/7 (attached as Annex I to these Reports).

¹²The Philippines provided the third participants with copies of its appellant's submission that did not contain certain information that was considered business confidential information in the Panel proceedings (pursuant to the Additional Working Procedures Concerning Business Confidential Information, adopted by the Panel on 31 August 2010). This information was, however, included in the copies of the Philippines' appellant's submission filed with the Appellate Body and served on the European Union and the United States. Following an enquiry from the Appellate Body Secretariat on 14 October 2011, the Philippines provided, on 18 October 2011, copies of its appellant's submission containing the business confidential information to the third participants. The Philippines requested the third participants to treat such information as confidential. In response to questioning at the oral hearing in this appeal, the participants and third participants confirmed to the Appellate Body that the information the Philippines had designated as business confidential in its appellant's submission was governed by the confidentiality rules of Article 18.2 of the DSU.

¹³WT/AB/W/P/6, 16 August 2010.

¹⁴WT/DS396/8, WT/DS403/8 (attached as Annex II to these Reports).

¹⁵Pursuant to Rules 22 and 23(4) of the *Working Procedures*.

¹⁶Pursuant to Rule 24(1) of the *Working Procedures*.

¹⁷Pursuant to Rule 24(2) of the *Working Procedures*.

¹⁸We note that Colombia, in its notification, expressed its intention to attend the oral hearing pursuant to Rule 24(2) of the *Working Procedures*. Colombia's notification was received on 17 October 2011 and, therefore, fell outside the 21-day time-limit stipulated in Rule 24(2) of the *Working Procedures*, which ended on 14 October 2011. Nevertheless, the Division hearing this appeal decided to accept Colombia's notification as a notification made pursuant to Rule 24(4) of the *Working Procedures*.

10. According to the Philippines, its tax measure does not alter the competitive opportunities of imported distilled spirits in relation to like domestic distilled spirits in the Philippine market. Instead, it achieves the fiscal goals of a sovereign government in a manner that allows consumers to consume the same distilled spirits that they would consume even if no excise taxes were imposed. The Philippines contends that Article III:2 of the GATT 1994 does not prohibit such a measure. The Philippines requests the Appellate Body to reverse various legal findings and conclusions of the Panel under Article III:2 of the GATT 1994 and to apply Article III:2 in a manner that is consistent with its text and its object and purpose.

1. Article III:2, First Sentence, of the GATT 1994

11. The Philippines claims on appeal that the Panel erred in its interpretation and application of the term "like products" under Article III:2, first sentence, of the GATT 1994, and failed to apply the appropriate standard for the interpretation of that term when assessing the subject products' physical characteristics, consumer tastes and habits, and tariff classification. The Philippines also claims that the Panel erred in its assessment of the evidence under Article 11 of the DSU because it ignored relevant expert evidence that imported and domestic products were physically dissimilar, disregarded its own findings regarding the tariff classification of certain products, and had no evidentiary basis to support its finding that the majority of consumers would view the imported and domestic products as substitutable. The Philippines requests the Appellate Body to reverse the Panel's finding under Article III:2, first sentence, of the GATT 1994 for the following reasons.

12. The Philippines observes that "likeness" under Article III:2, first sentence, necessarily requires that the products at issue compete in the marketplace and have essentially the same physical characteristics. Therefore, the "highest degree" of both physical similarity and competitiveness in the relevant market is required in order for the products to be considered "like".¹⁹ The Philippines claims that the Panel applied the wrong standard of "likeness" under Article III:2, first sentence. To state, as the Panel does, that the concept of "like products" is not limited to "identical products" does not capture the Appellate Body's narrow definition of "like products" under Article III:2, first sentence. The Philippines argues that the test that should have been applied is whether the products are "sufficiently close" in nature such that they could be deemed to fit within the narrow category of "like products" within the meaning of Article III:2, first sentence, as interpreted by the Appellate Body.²⁰

¹⁹Philippines' appellant's submission, para. 27.

²⁰Philippines' appellant's submission, para. 29.

13. Regarding the products' properties, nature, and quality, the Philippines argues that the narrow scope of the category of "like products" means that any significant physical difference, even if not perceptible to the consumer, will be considered sufficient to disqualify a product from being considered "like" another product. The physical differences between the products at issue begin with the raw materials from which they are made, which result in other differences in physical properties and qualities. The Panel in this case found that "sugar-based" and "non-sugar-based" distilled spirits are "like" despite numerous physical differences between the products and, in particular, the additives used to make "sugar-based" whisky, brandy, gin, and tequila. According to the Philippines, the simple fact that "sugar-based" distilled spirits in the Philippines are physically different from their "non-sugar-based" counterparts should have been viewed by the Panel as disqualifying these products from being considered physically "like".²¹

14. The Philippines contends that such error by the Panel occurred not only in relation to the Panel's analysis of each imported "non-sugar-based" spirit and its domestic "sugar-based" counterpart, but also in relation to the broader category of "non-sugar-based" distilled spirits compared with "sugar-based" distilled spirits. This led the Panel to make "the extraordinary finding" that non-sugar-based whiskies were 'like' sugar-based brandies, etc."²² The Philippines contends that these groups of products are so different that even the complainants themselves did not claim that all "non-sugar-based" distilled spirits are "like" "sugar-based" distilled spirits for the purposes of Article III:2, first sentence.²³

15. The Philippines argues that the Panel applied the wrong standard by relying on a "perceptible differences" test from the perspective of the hypothetical consumer as the sole determinant of whether the products are physically different or not.²⁴ According to the Philippines, the perception of the consumer is relevant to the "likeness" criterion of consumer tastes and habits. Such a perception is not related to the physical characteristics of the product, which are empirical, physical attributes. The Philippines recalls that, in *EC – Asbestos*, the Appellate Body found that products with differences in molecular structure, chemical composition, and fibrillation capacity, which are not detectable to the consumer upon purchasing, were not considered physically "like". Moreover, the Appellate Body

²¹Philippines' appellant's submission, para. 39. The Panel found that "all distilled spirits produced in the Philippines are made from designated raw materials" and that "most of the distilled spirits produced in the Philippines are made from one particular designated raw material: sugar cane molasses". (Panel Reports, para. 2.17)

²²Philippines' appellant's submission, para. 40 (referring to Panel Reports, paras. 7.39 and 7.77).

²³Philippines' appellant's submission, para. 41 (referring to Panel Reports, paras. 7.4-7.6).

²⁴Philippines' appellant's submission, para. 44.

held that physical characteristics deserve a separate examination and should not be confused with any of the other elements in the traditional likeness analysis.²⁵

16. The Philippines thus contends that, having selected the wrong standard, the Panel found physical similarity between "sugar-based" and "non-sugar-based" distilled spirits in spite of important physical differences between these types of distilled spirits, such as the very different levels of certain key "congeners"—chemical substances produced during fermentation that affect the taste and aroma—and the use of additives in "sugar-based" distilled spirits to replicate the colour, odour, and taste traditionally associated with certain "non-sugar-based" distilled spirits. The Philippines argues that the Panel's improper analysis of "likeness" under Article III:2, first sentence, of the GATT 1994 manifests itself in the fact that the Panel did not take into account differences in quality between the "sugar-based" and the "non-sugar-based" products.

17. The Philippines claims that the Panel erred in considering that the complainants' regulatory regimes, which prohibit the marketing of whisky and brandy made from sugar cane molasses as "whisky" and "brandy", were "irrelevant".²⁶ While it is true that the Philippine market is the relevant market for the determination of "likeness" when considering the conditions of competition between the foreign and domestic products at issue, the Panel confused the analysis of competition with the analysis of the products' physical characteristics. The complainants' regulatory regimes show that the difference in raw materials is a legitimate and commonly applied basis for distinguishing between distilled spirits. If a distilled spirit is made from something other than what is specified in the relevant regulations, it may not be sold as a whisky, brandy, or other such regulated spirit within the complainants' own markets. The Philippines contends that the domestic regulatory regimes of both complainants are useful in identifying physical differences between the products that are commonly recognized as important to that particular product's identity.

18. The Philippines also claims that the Panel failed to make an objective assessment of the matter before it, in accordance with Article 11 of the DSU, because it disregarded expert evidence demonstrating that "sugar-based" and "non-sugar-based" distilled spirits are different in terms of physical characteristics and quality. In particular, the Panel disregarded critical portions of the Philippines' evidence, and substituted its own judgement for that of the expert testimony presented by the Philippines, when it found that there was no evidence that differences in the organoleptic properties create a distinction between distilled spirits made from designated raw materials and

²⁵Philippines' appellant's submission, paras. 43 and 47 (referring to Appellate Body Report, *EC – Asbestos*, paras. 111 and 114).

²⁶Philippines' appellant's submission, para. 51.

distilled spirits made from non-designated raw materials, and that the differences in chemical composition that do exist were not of assistance in its analysis of "likeness".²⁷

19. The Philippines maintains that the expert evidence that it submitted to the Panel demonstrates that "sugar-based" and "non-sugar-based" distilled spirits have different organoleptic properties, which result from differences in their chemical composition and congener content, and that this evidence remained unrebutted throughout the Panel proceedings. The Philippines claims that each of the Panel's statements and conclusions is directly contradicted by the expert evidence, and that, in making these findings in relation to all the distilled spirits under consideration, the Panel did not, and could not, rely on contradictory expert evidence from the complainants, as none was submitted.

20. Regarding consumer tastes and habits, the Philippines recalls that, in *EC – Asbestos*, the Appellate Body noted that evidence in respect of end-uses and consumer tastes and habits was particularly relevant "in cases where the evidence relating to properties establishes that the products at issue are physically quite different".²⁸ According to the Appellate Body, in such cases, "a higher burden is placed on complaining Members to establish that, despite the pronounced physical differences, there is a competitive relationship between the products."²⁹ Therefore, where products are physically different, a higher burden is imposed on the complainants to show direct competition and substitutability. Moreover, the Philippines claims that, in order to give proper meaning to the term "like" under Article III:2, first sentence, the degree of competition between products must be greater than that required for "directly competitive or substitutable" products under Article III:2, second sentence.

21. The Philippines thus contends that the Panel erred in finding that, in this case, the degree of competition and substitutability among "sugar-based" and "non-sugar-based" distilled spirits satisfies the higher standard of "likeness" under Article III:2, first sentence, while acknowledging that a large proportion of consumers do not have access to, and are not willing to purchase, "non-sugar-based" distilled spirits instead of "sugar-based" distilled spirits, and that the competition and substitutability that exists is limited to exceptional "special occasion" purchases.³⁰ The Philippines disagrees with the Panel that a product that is not accessible to 98.2 per cent of the population, but may be accessible to some unidentified minuscule segment of the population on special occasions, could be deemed to be

²⁷Philippines' appellant's submission, paras. 140 and 141 (referring to Panel Reports, para. 7.40).

²⁸Philippines' appellant's submission, para. 64 (quoting Appellate Body Report, *EC – Asbestos*, para. 118).

²⁹Philippines' appellant's submission, para. 64 (quoting Appellate Body Report, *EC – Asbestos*, para. 118).

³⁰Philippines' appellant's submission, para. 69.

engaged in the degree of competition required under Article III:2, first sentence, with a product that is purchased as a routine consumption good and that is accessible to all. The Philippines relies on the findings of the panels in *Indonesia – Autos and Dominican Republic – Import and Sale of Cigarettes* to support its argument that products that do not compete in the same market are perceived differently by consumers and cannot, therefore, be considered "like" within the meaning of Article III:2, first sentence, of the GATT 1994.³¹ According to the Philippines, the Panel in this dispute failed properly to construe "likeness" in the context of that provision by failing to recognize this additional element of differentiation in the Philippine market.

22. The Philippines further submits that distribution channels for "sugar-based" and "non-sugar-based" distilled spirits in the Philippine market are distinct, reflecting the different consumer markets they serve. The Philippines relies on the findings of the panel in *Chile – Alcoholic Beverages*, which found that, "if products have quite distinctive channels of distribution that could be a negative indicator with respect to substitutability" and that "if the products were regularly presented separately, it would be *one* piece of evidence that perhaps consumers did not group them together in their perceptions".³² The Philippines submits that local *sari-sari* stores, which are frequented by all except the most affluent of consumers, account for approximately 85 per cent of off-premise sales of "sugar-based" distilled spirits, but do not carry "non-sugar-based" distilled spirits.³³ Moreover, evidence submitted by the complainants shows that "sugar-based" distilled spirits are sold predominantly (as much as 90 per cent) through off-premise channels, while "non-sugar-based" distilled spirits are sold predominantly (as much as 90 per cent) through on-premise channels.³⁴

23. The Philippines claims, in addition, that the Panel failed to make an objective assessment of the matter before it, in accordance with Article 11 of the DSU, because, in concluding that there was no evidence of the existence of two separate markets in the Philippines, and that some consumers from the majority market "may be able to purchase high-priced distilled spirits, at least on special occasions", it disregarded critical evidence produced by the Philippines and ignored the fact that no evidence had been presented to counter that presented by the Philippines.³⁵ In particular, the Philippines argues that the Panel ignored that: (i) "non-sugar-based" distilled spirits are regularly priced over Philippine pesos ("PHP") 150 a bottle; and (ii) 98.2 per cent of Philippine households

³¹Philippines' appellant's submission, paras. 72-74 (referring to Panel Report, *Indonesia – Autos*, paras. 14.174-14.177 and 14.181; and Panel Report, *Dominican Republic – Cigarettes*, para. 7.331).

³²Philippines' appellant's submission, para. 75 (quoting Panel Report, *Chile – Alcoholic Beverages*, para. 7.59 (original emphasis)). (boldface added by the Philippines omitted)

³³Philippines' appellant's submission, para. 76 and footnote 77 thereto.

³⁴Philippines' appellant's submission, para. 76 (referring to 2010 International Wine and Spirits Record, "Philippines – Index" (Panel Exhibits EU-15 and US-15)).

³⁵Philippines' appellant's submission, para. 173 (quoting Panel Reports, paras. 7.59 and 7.119).

have a maximum of PHP 150 per week to spend on alcoholic beverages. Therefore, there are at least two market segments in the Philippines, because only 1.8 per cent of the Filipino population can afford "non-sugar-based" distilled spirits, whereas the rest of the population can afford only "sugar-based" distilled spirits.³⁶

24. The Philippines argues that the *Euromonitor International* survey³⁷, submitted by the complainants, shows that only three brands of imported distilled spirits were priced below PHP 150, and that none of these were priced lower than PHP 130, while the remainder (approximately 195 products) were priced far above this level, but that no evidence was presented showing that imported distilled spirits are regularly priced below or even near the PHP 150 threshold. In respect of market segmentation, the Philippines submits that no evidence was presented by the complainants to show that the majority of the Filipino population could afford distilled spirits over PHP 150. The Philippines argues that, while non-price-related factors (such as quality, taste, and social acceptability) prevented the downward substitution of the products at issue, price-related factors were the most significant reason why consumers could not engage in an upward substitution of the products, thus creating a market segmentation of at least two groups.³⁸ Therefore, in finding that there was "no evidence of the existence of two separate distilled spirit markets in the Philippines that reflect different levels of purchasing power"³⁹, the Panel simply rejected or ignored much of the evidence submitted by the Philippines, in violation of Article 11 of the DSU.

25. Regarding tariff classification, the Philippines claims that the Panel erred in finding that the fact that all distilled spirits at issue, irrespective of the raw materials from which they are made, fall under the same four-digit Harmonized System ("HS") tariff heading (2208) provides an indication of similarity. The Philippines relies on the findings of the Appellate Body in *Japan – Alcoholic Beverages II* that, "[i]f sufficiently detailed, tariff classification can be a helpful sign of product similarity", but that "tariff bindings that include a wide range of products are not a reliable criterion for determining or confirming product 'likeness' under Article III:2".⁴⁰ The Philippines argues that the Panel's use of the four-digit tariff heading in this case was inappropriate, because the range of

³⁶Philippines' appellant's submission, para. 174 (referring to Philippines' first written submission to the Panel, paras. 224-229; and Philippines' responses to Panel Questions 35, 36, 72, and 89).

³⁷*Euromonitor International*, "Consumer perceptions regarding substitutability in the Philippines distilled spirits market" (August 2010) (Panel Exhibits EU-41 and US-41).

³⁸Philippines' appellant's submission, para. 176 (referring to *Euromonitor International* survey, *supra*, footnote 37, p. 19).

³⁹Philippines' appellant's submission, para. 177 (quoting Panel Reports, para. 7.60). (boldface added by the Philippines omitted)

⁴⁰Philippines' appellant's submission, para. 80 (quoting Appellate Body Report, *Japan – Alcoholic Beverages II*, pp. 21-22, DSR 1996:1, 97, at 114-115).

GATT 1994. The Philippines requests the Appellate Body to reverse this finding for the following reasons.

29. First, the Philippines argues that the Panel erred in finding that the relevant inquiry under Article III:2, second sentence, is not the "degree of competition" between the products at issue but, rather, the "nature or quality" of their competitive relationship.⁴⁴ Referring to the Appellate Body reports in *Korea – Alcoholic Beverages* and *US – Cotton Yarn*, the Philippines submits that the degree of competition between the products at issue is the "central" inquiry under Article III:2, second sentence.⁴⁵ In examining simply the "nature or quality" of competition, the Panel insufficiently addressed the "degree of proximity" of competition between the products at issue.⁴⁶ The Philippines acknowledges that both quantitative and qualitative evidence are relevant in determining the degree of competition between "non-sugar-based" and "sugar-based" distilled spirits under Article III:2. However, the Philippines emphasizes that the evidence that was before the Panel shows "a great disparity in the accessibility of these products, how [they] are perceived by the consumers, and how they are treated by suppliers" in the market.⁴⁷ Therefore, had the Panel applied the correct legal standard, it would have come to the conclusion that there was "insufficient proximity in the degree of competition" between the products at issue to permit their characterization as "directly competitive or substitutable".⁴⁸

30. Second, the Philippines maintains that the Panel erred in finding "direct" competition between domestic and imported distilled spirits because "many [consumers] may be able to purchase high-priced distilled spirits, at least on special occasions."⁴⁹ The Panel impermissibly lowered the "direct competition" standard of Article III:2, which requires "close proximity in the process of purchasing a product, including its frequency, and the nature and frequency of purchasing another product".⁵⁰ The Philippines stresses that "special occasion" purchases are, by nature, "exceptional", likely requiring consumers to alter their usual consumption patterns.⁵¹ Recalling the Appellate Body's interpretation that "directly competitive or substitutable" products are those that offer an "alternative way[] of satisfying a particular need or taste", the Philippines posits that two products that are not

⁴⁴Philippines' appellant's submission, paras. 88 and 89 (quoting Panel Reports, para. 7.101).

⁴⁵Philippines' appellant's submission, paras. 90 and 91 (referring to Appellate Body Report, *Korea – Alcoholic Beverages*, paras. 129, 130, 133, and 134; and Appellate Body Report, *US – Cotton Yarn*, paras. 97 and 98).

⁴⁶Philippines' appellant's submission, para. 93.

⁴⁷Philippines' appellant's submission, para. 94.

⁴⁸Philippines' appellant's submission, para. 95.

⁴⁹Philippines' appellant's submission, para. 96 (quoting Panel Reports, para. 7.119).

⁵⁰Philippines' appellant's submission, para. 97.

⁵¹Philippines' appellant's submission, para. 98.

products that fall under HS heading 2208 is very broad; in any event, it is not sufficiently detailed to draw any particular inferences as to whether the distilled spirits at issue are "like".⁴¹

26. The Philippines further claims that the Panel failed to make an objective assessment of the matter before it, in accordance with Article 11 of the DSU, because it ignored significant and clear evidence regarding the tariff classification of whiskey and brandy when it arrived at the conclusion that the evidence on tariff classification was inconclusive. Particularly in respect of whiskey and brandy, the Panel found that the HS classification at the six-digit level, and the accompanying explanatory notes, take into account the raw material used for the production of the distilled spirit, so that whiskeys and brandies made from sugar cane molasses would not fall under the same HS subheading as whiskeys and brandies made from traditional raw materials. The Philippines contends, therefore, that the Panel's conclusion that, "at the six-digit level, the HS classification does not give ... conclusive guidance" is unsupported by the very facts that the Panel cited in its Reports.⁴²

2. Article III:2, Second Sentence, of the GATT 1994

27. The Philippines claims that the Panel erred in finding that the Philippines has acted inconsistently with Article III:2, second sentence, of the GATT 1994, because it applies dissimilar internal taxes on domestic distilled spirits made from designated raw materials and "directly competitive or substitutable" imported distilled spirits made from non-designated raw materials, "so as to afford protection to domestic production" of distilled spirits in the Philippines. More specifically, the Philippines claims that the Panel erred in finding that domestic distilled spirits made from designated raw materials and imported distilled spirits made from non-designated raw materials are "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the GATT 1994. The Philippines also claims that the Panel erred in finding that the Philippines' excise tax is applied "so as to afford protection to domestic production" of distilled spirits within the meaning of that provision.⁴³

(a) Directly Competitive or Substitutable Products

28. The Philippines claims that the Panel erred in finding that domestic distilled spirits made from designated raw materials and imported distilled spirits made from non-designated raw materials are "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the

⁴¹Philippines' appellant's submission, para. 81.

⁴²Philippines' appellant's submission, para. 159 (quoting Panel Reports, para. 7.71).

⁴³The Philippines does not appeal the Panel's finding at paragraph 7.167 of the Panel Reports that imported spirits and directly competitive or substitutable domestic distilled spirits are not similarly taxed within the meaning of Article III:2, second sentence, of the GATT 1994.

purchased with the same frequency, and that satisfy a dissimilar set of needs, cannot be considered "directly" competitive.⁵²

31. Third, the Philippines submits that the Panel incorrectly considered that it was sufficient for a small portion of the market to have "access"⁵³ to both domestic and imported distilled spirits for them to be "directly competitive or substitutable".⁵⁴ The Philippines agrees that access to both imported and domestic distilled spirits is "an important part" of the inquiry and constitutes a "threshold issue" for whether further examination of the degree of competition is required.⁵⁵ However, access alone is not sufficient to demonstrate that consumers in an affluent income bracket actually view those products as directly competitive or substitutable. In equating "access" to "direct competition", the Panel failed to give meaning to the term "directly". Moreover, evidence showing a "vast and consistent" price difference between domestic and imported distilled spirits indicates a lack of competition in that portion of the market, because it demonstrates that the pricing behaviour of suppliers of imported distilled spirits is not constrained by the pricing behaviour of suppliers of domestic distilled spirits.⁵⁶

32. Fourth, the Philippines contends that the Panel erred in finding direct competition between domestic and imported distilled spirits on the basis of competition in a "negligible, unrepresentative portion of the market".⁵⁷ For the Philippines, evidence of substitutability for the purposes of Article III:2, second sentence, "must emanate from a segment of the population that is genuinely and realistically representative of the whole market in which the products are consumed".⁵⁸ The Philippines emphasizes that 98.2 per cent of Filipino households cannot afford imported distilled spirits, and that the Panel erroneously found that these products are "directly competitive or substitutable" with domestic distilled spirits on the basis of "some degree of substitutability" in relation to 1.8 per cent of the market.⁵⁹

33. Fifth, the Philippines submits that the Panel erred in finding that instances of price overlap between domestic and imported distilled spirits demonstrate that these products are "capable of being

⁵²Philippines' appellant's submission, para. 99 (quoting Appellate Body Report, *Korea – Alcoholic Beverages*, para. 115).

⁵³Philippines' appellant's submission, para. 101 (quoting Panel Reports, para. 7.120).

⁵⁴Philippines' appellant's submission, para. 103.

⁵⁵Philippines' appellant's submission, para. 104.

⁵⁶Philippines' appellant's submission, para. 105.

⁵⁷Philippines' appellant's submission, para. 118.

⁵⁸Philippines' appellant's submission, para. 120.

⁵⁹Philippines' appellant's submission, paras. 119.

directly competitive or substitutable in the future".⁶⁰ The Philippines dismisses this finding as "speculative"⁶¹, and considers that the limited price overlap falls short of demonstrating "actual competition" between domestic and imported distilled spirits. The Philippines adds that an inquiry into potential competition is only relevant to determine "whether competition would otherwise occur if the measures were not in place".⁶² According to the Philippines, the "massive price differential" between domestic and imported distilled spirits and the actual purchasing power of the "great majority" of Filipinos demonstrate that these products are not capable of being "directly competitive or substitutable in the near future" in the absence of the excise tax.⁶³ In addition, the Panel's reference to the "future" is too indefinite and therefore insufficient to support a finding of violation of Article III:2, second sentence. The Philippines also maintains that the Panel acted inconsistently with its duties under Article 11 of the DSU in finding, without sufficient evidentiary basis, that the products at issue are capable of competing in the future.

34. Finally, in addition to its claims of error in the application of Article III:2, second sentence, to the facts of the present dispute, the Philippines claims that the Panel acted inconsistently with Article 11 of the DSU in its assessment of the *Euromonitor International*⁶⁴ and Abrenica & Ducanes⁶⁵ studies, which evaluate the substitutability between domestic and imported distilled spirits in the Philippine market. The Panel's conclusion that both studies showed "a significant degree of competitiveness or substitutability"⁶⁶ between domestic and imported distilled spirits in the Philippine market is directly contradicted by the Abrenica & Ducanes study, which showed "negligible levels of substitutability".⁶⁷ In addition, the Panel mischaracterized the methodology of the Abrenica & Ducanes study, which held the prices of other distilled spirits unchanged when the price of the selected spirit increased.⁶⁸ The *Euromonitor International* survey is, in turn, an insufficient basis on which to find substitutability, because it neither estimated the cross-price elasticity, nor isolated the effects of an increase in domestic prices on quantities of imported distilled spirits. Furthermore, the sample used in the *Euromonitor International* survey represented only the top percentage of income

⁶⁰Philippines' appellant's submission, para. 107 (quoting Panel Reports, para. 7.121 (original emphasis)).

⁶¹Philippines' appellant's submission, para. 108.

⁶²Philippines' appellant's submission, para. 111.

⁶³Philippines' appellant's submission, paras. 112 and 113.

⁶⁴*Supra*, footnote 37.

⁶⁵M.J. Abrenica and J. Ducanes, "On Substitutability between Imported and Local Distilled Spirits" (University of Philippines School of Economics Foundation, 10 October 2010) (Panel Exhibit PH-49).

⁶⁶Philippines' appellant's submission, para. 163 (quoting Panel Reports, paras. 7.62 and 7.113).

⁶⁷Philippines' appellant's submission, para. 164.

⁶⁸Philippines' appellant's submission, para. 167 (referring to Panel Reports, para. 7.56).

distribution in the Philippines, and therefore was not representative of the entire market.⁶⁹ The Philippines adds that the *Euromonitor International* survey suggests that non-price-related factors, such as consumer tastes and habits, prevented both the downward and upward substitution of the products.⁷⁰ According to the Philippines, the Panel unjustifiably disregarded these shortcomings in its examination of the studies, and thereby failed to make an objective assessment of the matter as required under Article 11 of the DSU.

(b) "So as to afford protection to domestic production"

35. The Philippines claims that the Panel erred in finding that the dissimilar taxes imposed on imported distilled spirits and on directly competitive or substitutable domestic distilled spirits are applied "so as to afford protection to domestic production" of distilled spirits. The Philippines requests the Appellate Body to reverse this finding for the following reasons.

36. The Philippines argues that the Panel's conclusion that "the vast majority of [the] imported spirits are subject to higher taxes" is not supported by the evidence submitted to the Panel.⁷¹ The Panel's conclusion that "*de facto* the measure results in all domestic distilled spirits enjoying the favourable low tax, while the vast majority of the imported spirits are subject to higher taxes"⁷² is contradicted by the fact that approximately 50 per cent of Philippine distilled spirits production is made from imported ethyl alcohol, which is subject to the lower tax rate.⁷³

37. The Philippines adds that the Panel erroneously inferred protectionism from the high tax rates applicable to some imported distilled spirits. In the Philippines' view, such inference is unwarranted in a case where 98.2 per cent of Filipino households cannot afford imported distilled spirits. The Panel erroneously dismissed the Philippines' argument on the basis of the reasoning articulated by the Appellate Body in *Korea – Alcoholic Beverages*.⁷⁴ While such reasoning may have been appropriate in the context of the competitive conditions of the Korean market, it does not preclude consideration of the Philippines' argument concerning income gaps in the present case. Moreover, in merely "transferring the reasoning" applied by the Appellate Body in the context of the factual circumstances

⁶⁹Philippines' appellant's submission, para. 169 (referring to *Euromonitor International* survey, *supra*, footnote 37, pp. 7 and 13).

⁷⁰Philippines' appellant's submission, para. 170 (referring to *Euromonitor International* survey, *supra*, footnote 37, p. 19).

⁷¹Philippines' appellant's submission, para. 128 (quoting Panel Reports, para. 7.182).

⁷²Philippines' appellant's submission, para. 127 (quoting Panel Reports, para. 7.182).

⁷³Philippines' appellant's submission, para. 128 (referring to letter from the Republic of the Philippines Department of Finance, Bureau of Internal Revenue, dated 3 February 2011 (Panel Exhibit PH-82); and Philippines' response to Panel Question 68(a)).

⁷⁴Philippines' appellant's submission, para. 129 (referring to Panel Reports, para. 7.185).

of *Korea – Alcoholic Beverages*, the Panel fell short of the "case-by-case, comprehensive" analysis that was required to assess whether there is protective application under Article III:2, second sentence, in this dispute.⁷⁵

B. *Arguments of the European Union – Appellee*

38. The European Union takes issue with the Philippines' reference to its excise tax regime as a measure that distinguishes between "sugar-based" distilled spirits and "non-sugar-based" distilled spirits. In the European Union's view, this distinction is false and misleading, because Section 141(a) of the NIRC covers not only distilled spirits made from sugar cane molasses, but also distilled spirits produced from the sap of the *nipa*, coconut, cassava, *camote*, or *buri* palm. Indeed, the European Union notes that some domestic distilled spirits are made from designated raw materials other than sugar cane molasses.

39. The European Union argues that the Philippines overemphasizes the alleged neutrality of the measure at issue, and disagrees with the contentions that the excise tax regime makes no distinction between the products' countries of origin and that "any distilled spirit from any country in the world produced from [sugar cane] is entitled to the lower specific tax."⁷⁶ The European Union notes that several imported distilled spirits, albeit produced from sugar cane, do not enjoy the lower flat tax rate for designated raw materials.⁷⁷ Moreover, Section 141(a) of the NIRC sets forth the additional requirement that the raw materials be produced commercially in the country where they are processed into distilled spirits. In the European Union's view, this further condition implies that two products that may be essentially identical might be treated differently *solely* on the basis of whether or not climate or agronomic conditions allow for commercial production of the relevant designated raw material in the country of origin.

40. The European Union submits that the Philippines' assertion that the excise tax regime pursues the aim of progressive taxation is "manifestly unfounded" and conceals a protectionist intent, given that the level of taxation does not depend on prices but, rather, on the raw materials from which

⁷⁵Philippines' appellant's submission, paras. 133-135 (quoting Panel Reports, paras. 7.179 and 7.186, in turn quoting Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 29, DSR 1996:1, 97, at 120).

⁷⁶European Union's appellee's submission, para. 10 (quoting Philippines' appellant's submission, para. 10).

⁷⁷European Union's appellee's submission, para. 12. The European Union mentions seven brands of imported distilled spirits that are excluded from the lower tax rate under Section 141(a) of the NIRC, namely "Havana Club Anejo Reserva", "Lemon Hart Jamaica Rum", "Lemon Hart White Rum", "Malibu Caribbean White Rum w/ coco", "Malibu Rum", "Myers Rum", and "Myers Rum Planters Punch". (*Ibid.*, referring to Republic of the Philippines Department of Finance, Bureau of Internal Revenue Regulation 23-2003 (Panel Exhibit PH-64), pp. 9, 11, and 12)

44. According to the European Union, the Philippines' assertion is also "legally flawed" and based on an incorrect reading of relevant case law, in that it accords "undue" importance to physical characteristics in the analysis of likeness.⁸⁵ The European Union remarks that the likeness analysis is a "holistic exercise" in which physical characteristics have to be examined together with other criteria⁸⁶, and in which "no criteri[on] is, on its own, determinative".⁸⁷ Moreover, the European Union argues that the relevant case law indicates that some differences in physical characteristics are not *per se* sufficient to render the products "unlike". For instance, the panel in *Japan – Alcoholic Beverages II* found that two of the distilled spirits at issue—vodka and shochu—were "like products" since they shared "most physical characteristics", and stated that differences in name, traditional origin, filtration, alcohol strength, and raw materials did not prevent a finding of "likeness". In addition, that panel concluded that shochu and other distilled spirits at issue in that case were not "like products" under Article III:2, first sentence, "only insofar as there existed 'substantial noticeable differences'" between them.⁸⁸ Similarly, the panel in *Mexico – Taxes on Soft Drinks* found that a difference in the raw materials used to sweeten the products at issue did not constitute a "substantial noticeable difference", and accordingly concluded that the products at issue were "like".⁸⁹

45. The European Union disagrees with the Philippines' assertion that the Panel erred in considering as irrelevant for its analysis the European Union's and the United States' regulations, which allegedly prohibit the marketing of whisky and brandy made from the designated raw materials as whisky or brandy in their respective markets.⁹⁰ The European Union takes the view that, in a case-by-case analysis, which takes into account all relevant factors, certain facts alleged by the parties may be deemed *irrelevant* or *of little relevance* by a panel, and that the Philippines is merely complaining about the weighing of evidence and the assessment of facts made by the Panel in this case. Since the Philippines has not raised a specific claim of error under Article 11 of the DSU in this respect, the European Union contends that the Appellate Body need not address the Philippines' argument on this issue.

46. The European Union takes issue with the Philippines' claim that the Panel acted inconsistently with Article 11 of the DSU because it disregarded portions of the expert evidence submitted by the

⁸⁵European Union's appellee's submission, para. 50.

⁸⁶European Union's appellee's submission, para. 51.

⁸⁷European Union's appellee's submission, para. 52 (quoting Appellate Body Report, *EC – Asbestos*, para. 111).

⁸⁸European Union's appellee's submission, para. 54 (quoting Panel Report, *Japan – Alcoholic Beverages II*, para. 6.23) (emphasis added by the European Union)

⁸⁹European Union's appellee's submission, para. 55 (quoting Panel Report, *Mexico – Taxes on Soft Drinks*, para. 8.136).

⁹⁰European Union's appellee's submission, para. 59 (referring to Philippines' appellant's submission, para. 52).

distilled spirits are produced.⁷⁸ The European Union contends that, if the Philippines had really wanted to develop a progressive taxation system, it could have adopted a pure *ad valorem* system, where all products would always be taxed according to their net retail price ("NRP").

41. The European Union also contests the Philippines' argument that there is a "clear-cut distinction" between high-priced imported distilled spirits and low-priced domestic distilled spirits⁷⁹, and that price overlaps are "exceptions and aberrations".⁸⁰ The European Union agrees with the Panel's findings that "there are a number of high-priced domestic spirits, as well as less expensive imports"⁸¹, and that the overlap in prices "is not exceptional" and "occurs for both high-priced and low-priced products".⁸² Moreover, the European Union emphasizes that the measure at issue has a profound impact even on the pre-tax prices of imported distilled spirits by, *inter alia*, preventing producers of imported distilled spirits from enjoying the benefits of economies of scale.

1. Article III:2, First Sentence, of the GATT 1994

42. The European Union requests the Appellate Body to reject the Philippines' claim that the Panel erred in interpreting and applying the concept of "like products" within the meaning of Article III:2, first sentence, of the GATT 1994.

43. With regard to physical characteristics, the European Union takes issue with the Philippines' contention that the narrow scope of the term "like products" implies that "any significant physical difference, even those that may not be perceptible to the consumer, will be considered sufficient to disqualify a product from being considered 'like' another product."⁸³ The European Union argues that the Philippines' contention is based on the "factually wrong" premise that all domestic products have similar characteristics and all imported distilled spirits have other characteristics.⁸⁴ In fact, apart from the raw materials used in the production of distilled spirits, the Panel found no proof that all domestic distilled spirits have a similar chemical composition, or that this composition would, in turn, be any different from that of all imported distilled spirits.

⁷⁸European Union's appellee's submission, paras. 19 and 20.

⁷⁹European Union's appellee's submission, para. 33.

⁸⁰European Union's appellee's submission, para. 37 (quoting Philippines' second written submission to the Panel, para. 56).

⁸¹European Union's appellee's submission, para. 35 (quoting Panel Reports, paras. 2.36, 7.51, 7.59, and 7.118).

⁸²European Union's appellee's submission, para. 37 (quoting Panel Reports, para. 7.118).

⁸³European Union's appellee's submission, para. 45 (quoting Philippines' appellant's submission, para. 30).

⁸⁴European Union's appellee's submission, para. 47.

Philippines with respect to the chemical composition and the organoleptic properties of the products at issue. The European Union contends that, although the Panel did not explicitly mention the expert evidence in question, it did take it into account. In this respect, the European Union recalls that, in *Australia – Apples*, the Appellate Body found that a panel that does not expressly reproduce certain statements may still act consistently with Article 11 when the panel's reasoning "reveals that it has nevertheless assessed the significance of the[se] statements".⁹¹ Moreover, the Panel "went to great lengths" to discuss the arguments of the Philippines on this point, and simply disagreed on the relevance and weight of those elements.⁹²

47. With regard to consumer tastes and habits, the European Union contests the Philippines' claim that the Panel erred in disregarding the fact that 98.2 per cent of Filipino consumers are unable to purchase high-priced imported distilled spirits, and can buy only low-priced domestic distilled spirits, and that a large part of domestic distilled spirits are sold through *sari-sari* stores⁹³, whereas a substantial part of imported distilled spirits are sold through larger off-premise outlets. The European Union reiterates that the Philippines' distinction between high-priced imported distilled spirits and low-priced domestic distilled spirits is "incorrect", since both domestic and imported distilled spirits cover a relatively wide spectrum of prices.⁹⁴ Moreover, the large overlap in the distribution channels of domestic and imported distilled spirits is evidenced by the fact that many supermarkets, restaurants, bars, pubs, and catering companies "offer both domestic and imported spirits side-by-side"⁹⁵, and some *sari-sari* stores do sell some imported brands.⁹⁶ Finally, the European Union contends that the Panel ultimately was not convinced that the figures provided by the Philippines proved the existence of two separate population groups with distinctive consumption patterns.⁹⁷

48. The European Union also takes issue with the Philippines' view that the Panel wrongly considered, as part of its analysis of the competitive relationship between the products at issue, the fact that even customers who cannot regularly afford high-priced distilled spirits can purchase them "at least" on "special occasions". The European Union asserts that: (i) having already found that

⁹¹European Union's appellee's submission, para. 154 (quoting Appellate Body Report, *Australia – Apples*, para. 275).

⁹²European Union's appellee's submission, para. 150.

⁹³We note that, before the Panel, the Philippines defined "*sari-sari*" stores as "small, neighborhood, over-the-counter stores that carry basic grocery and household items". (Philippines' first written submission to the Panel, para. 253)

⁹⁴European Union's appellee's submission, para. 68.

⁹⁵European Union's appellee's submission, para. 69 (referring to Panel Reports, para. 2.41).

⁹⁶European Union's appellee's submission, para. 69 (referring to the Report of the Philippine Survey and Research Center, "Sari-Sari Store Survey" (13 September 2010) A(QN)011510-120 (Panel Exhibit PH-55), pp. 12-14).

⁹⁷European Union's appellee's submission, para. 73 (referring to Panel Reports, paras. 2.31, 2.32 and 7.59).

there are significant price overlaps between domestic and imported distilled spirits, the Panel's mention of "special occasions" was made only "*ad abundantiam*"; (ii) the term "at least" clearly indicates that the Panel found that, for many customers, the products are "usually" in competition and that, only for those with lower income, these products may perhaps be in competition only on those special occasions; and (iii) as noted by the Panel, the marketing campaigns run by producers of both domestic and imported distilled spirits specifically associate consumption of their products with the celebration of important events.⁹⁸

49. The European Union contests the Philippines' assertion that the Panel acted inconsistently with Article 11 of the DSU because it disregarded the evidence on the current price of distilled spirits and on the average income of the population. The European Union submits that the Panel duly took into account the documents concerned and discussed the arguments put forward by the Philippines. Ultimately, according to the European Union, the Panel simply disagreed with the merits of the Philippines' position, and thus it did not commit error under Article 11 of the DSU.

50. Lastly, with regard to tariff classification, the European Union disagrees with the Philippines' claim that the Panel erred in its analysis when it referred to the four-digit HS heading for distilled spirits, which, according to the Philippines, is not sufficiently specific. It also takes issue with the Philippines' assertion that the Panel acted inconsistently with Article 11 of the DSU when it disregarded the fact that raw materials are crucial in determining the six-digit HS subheadings of some distilled spirits, which would prove that those distilled spirits, when made from different raw materials, are "unlike". The European Union argues that the Panel simply found that "a six-digit heading was 'not conclusive'" and that the four-digit level could "provide an *indication* of similarity".⁹⁹ Thus, the Panel appreciated the tariff classification in the context of other facts and evidence and did not give any unwarranted weight to this aspect. In addition, the European Union argues that the evidence was not unequivocal. For instance, although the Philippines argued that a Philippine whisky (being made from sugar cane) would not fall under HS subheading 2208.30, export statistics show that, in recent years, there were exports of Philippine whiskeys under that HS subheading to several countries worldwide.¹⁰⁰ Finally, the Panel's conclusions on this issue are in conformity with those reached in past disputes.¹⁰¹ Therefore, the European Union concludes, the

⁹⁸European Union's appellee's submission, para. 71.

⁹⁹European Union's appellee's submission, para. 77 (quoting Panel Reports, para. 7.63). (emphasis added by the European Union)

¹⁰⁰European Union's appellee's submission, para. 78 (referring to Panel Exhibit EU-54, containing tables on volume and value of Philippine exports of distilled spirits, 2000-2008).

¹⁰¹European Union's appellee's submission, para. 79 (referring to Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 23, DSR 1996:1, 97, at 115).

Panel properly applied the criterion of tariff classification in its analysis under Article III:2, first sentence, of the GATT 1994, and did not err under Article 11 of the DSU.

2. Article III:2, Second Sentence, of the GATT 1994

51. The European Union submits that the Panel did not err in finding that the Philippines has acted inconsistently with Article III:2, second sentence, of the GATT 1994 by applying dissimilar internal taxes on domestic distilled spirits made from designated raw materials and "directly competitive or substitutable" imported distilled spirits made from non-designated raw materials, "so as to afford protection to domestic production" of distilled spirits. More specifically, the European Union argues that the Panel correctly held that domestic distilled spirits made from designated raw materials and imported distilled spirits made from non-designated raw materials are "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the GATT 1994. The European Union also argues that the Panel correctly found that the Philippines' excise tax is applied "so as to afford protection to domestic production" of distilled spirits within the meaning of Article III:2, second sentence, of the GATT 1994.

(a) Directly Competitive or Substitutable Products

52. The European Union requests the Appellate Body to dismiss the Philippines' appeal and uphold the Panel's finding that domestic distilled spirits made from designated raw materials and imported distilled spirits made from non-designated raw materials are "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the GATT 1994.

53. First, the European Union dismisses as "purely terminological"¹⁰² the Philippines' argument that the Panel insufficiently addressed the "degree of competition"¹⁰³ between domestic and imported distilled spirits in the Philippine market. In rejecting the Philippines' argument that Article III:2, second sentence, requires "complete, absolute or exact" substitutability, the Panel did not exclude the degree of competition from its analysis.¹⁰⁴ Rather, the Panel simply stated that the issue was "not so much" the degree of competition because it was necessary to take into account both current and potential competition.¹⁰⁵ According to the European Union, this interpretation is consistent with *Korea – Alcoholic Beverages*, where the Appellate Body found that Article III:2, second sentence, requires panels to take into account "latent demand, especially in markets where there are regulatory

¹⁰²European Union's appellee's submission, para. 83.

¹⁰³European Union's appellee's submission, para. 85. (emphasis omitted)

¹⁰⁴European Union's appellee's submission, para. 84.

¹⁰⁵European Union's appellee's submission, para. 85.

barriers to trade or to competition".¹⁰⁶ The Panel's interpretation of Article III:2, second sentence, also finds support in *US – Cotton Yarn*, where the Appellate Body held that the term "competitive" has "a wider connotation than 'actually competing' and includes also the notion of a potential to compete".¹⁰⁷ The European Union adds that the Panel's finding on the extent of competition between domestic and imported distilled spirits in the Philippines is an issue of fact that is not amenable to review on appeal, except under Article 11 of the DSU.

54. Second, the European Union argues that the Philippines misreads the Panel Reports when it argues that the Panel found direct competition between the products at issue on the basis of "special occasion" consumption. The Panel rejected the Philippines' arguments regarding the existence of two separate markets for distilled spirits based on price overlaps between imported and domestic distilled spirits, and because there was no evidence of the existence of two separate population groups in terms of consumption patterns and income. Therefore, the Panel dismissed the Philippines' argument because it was "factually unfounded and unproven", and not because it considered that partial competitive overlap was sufficient to establish the requisite level of substitutability.¹⁰⁸ Moreover, the European Union stresses that Article III:2, second sentence, does not require the same frequency in consumption, and that substitutability on "certain occasions" can be relevant under that provision. For the European Union, if potential competition must be taken into account, *a fortiori*, actual competition, even if only partial, should not be disregarded.

55. Third, the European Union challenges the Philippines' assertion that the Panel wrongly assumed that "access" to imported distilled spirits by a narrow segment of the market is equivalent to "direct competition".¹⁰⁹ The Panel's findings under Article III:2, second sentence, were based on "different aspects of similarity" between the products, including their competitive relationship, channels of distribution, properties, nature and quality, common end-uses and marketing, tariff classification, and internal regulations.¹¹⁰ The Panel simply reasoned that the Philippines' argument concerning market segmentation implies that some part of the Filipino population has access to both groups of distilled spirits. Thus, the Panel rightly concluded that potential competition cannot be ruled out *a priori*. The European Union also submits that the weight to be given to the price studies, which allegedly demonstrate that producers of domestic distilled spirits are not constrained by the

¹⁰⁶European Union's appellee's submission, para. 86 (quoting Appellate Body Report, *Korea – Alcoholic Beverages*, para. 115).

¹⁰⁷European Union's appellee's submission, para. 89 (quoting Appellate Body Report, *US – Cotton Yarn*, para. 96). (emphasis omitted)

¹⁰⁸European Union's appellee's submission, para. 97.

¹⁰⁹European Union's appellee's submission, para. 99.

¹¹⁰European Union's appellee's submission, para. 101.

pricing behaviour of producers of foreign distilled spirits, is a matter falling within the Panel's discretion as trier of facts, and cannot be reviewed by the Appellate Body except under Article 11 of the DSU.¹¹¹

56. Fourth, the European Union disagrees with the Philippines that the Panel found the requisite level of substitutability on the basis of direct competition only in a "negligible or unrepresentative" portion of the market. The European Union reiterates that the Panel found no evidence that all imported distilled spirits are high-priced and all domestic distilled spirits are low-priced, and that the Filipino population can be divided into two separate groups, in terms of consumption patterns and income. Therefore, the Panel did not decide that competition exists only in a portion of the market. Rather, in the European Union's view, the Panel assessed and made findings in relation to competition in the whole Philippine market for distilled spirits.

57. Fifth, the European Union rejects the Philippines' allegation that the Panel's findings concerning potential competition are "speculative".¹¹² The Philippines' allegation that the Panel disregarded evidence to the effect that price overlaps between domestic and imported distilled spirits are "exceptional" concerns an issue of fact and, as such, should not be reviewed by the Appellate Body.¹¹³ Nonetheless, the Panel's finding that domestic and imported distilled spirits "are *currently* competitive and substitutable" is supported by evidence demonstrating overlap in the prices of both high- and low-priced distilled spirits.¹¹⁴ In addition, the Panel was also required to take into account potential competition, because current conditions of competition may be distorted by the effects of the challenged measure. Therefore, the Panel correctly noted that instances of actual competition "are a clear indication that the imported and domestic products at issue in this dispute are indeed capable of being directly competitive or substitutable in the future."¹¹⁵ The European Union adds that the Panel acted consistently with its duties under Article 11 of the DSU in reaching its finding. According to the European Union, instances of actual competition and studies demonstrating that consumers are willing or might be willing to use imported and domestic distilled spirits to satisfy the same needs support the Panel's finding that there is also potential competition between these products.

¹¹¹European Union's appellee's submission, para. 103 (referring to Appellate Body Report, *US – Upland Cotton*, para. 441).

¹¹²European Union's appellee's submission, para. 105 (referring to Philippine's appellant's submission, paras. 107-115).

¹¹³European Union's appellee's submission, para. 107.

¹¹⁴European Union's appellee's submission, para. 110 (referring to Panel Reports, para. 7.118 (original emphasis)).

¹¹⁵European Union's appellee's submission, para. 113 (quoting Panel Reports, para. 7.121).

58. Finally, the European Union argues that the Panel did not act inconsistently with its duties under Article 11 of the DSU in its assessment of the economic studies presented by the parties. The fact that the *Euromonitor International* survey is not an econometric study does not undermine its probative value with respect to consumer preferences in the Philippines. To the contrary, the survey is "very pertinent" to the extent that it shows that consumers regard local and imported distilled spirits as "largely substitutable" and that they would react to price movements by switching between these categories.¹¹⁶ The European Union also stresses that the sample used in the *Euromonitor International* survey was adjusted and "cross-compared" with published demographic information to allow closer alignment with the overall Filipino population.¹¹⁷ The European Union adds that the Panel correctly described the methodology of the Abrenica & Ducanes study, because that study did not attempt to examine consumer response to a rise in prices of all domestic distilled spirits, or a reduction in prices of all imported distilled spirits. In any event, it is not clear to the European Union why an alleged imprecise description of the methodology employed in the Abrenica & Ducanes study would amount to a violation of Article 11 of the DSU.¹¹⁸ The European Union adds that the Abrenica & Ducanes study estimates that, in a tax-neutral environment, the market share of imported distilled spirits would increase by between 13 and 24.5 per cent, thus lending support to the Panel's conclusion regarding significant substitutability.¹¹⁹

(b) "So as to afford protection to domestic production"

59. The European Union argues that the Panel did not err in finding that the dissimilar taxes imposed on imported distilled spirits and on directly competitive or substitutable domestic distilled spirits are applied "so as to afford protection to domestic production" of distilled spirits. The European Union requests the Appellate Body to dismiss the Philippines' appeal in this respect, and to uphold the Panel's finding.

60. The European Union rejects the Philippines' argument that the measure at issue has no protective effect because a significant quantity of domestic distilled spirits is produced from imported ethyl alcohol that is taxed at the lower rate. For the European Union, ethyl alcohol is not a distilled spirit, but merely an input in the production of distilled spirits, and therefore is of no relevance to the

¹¹⁶European Union's appellee's submission, para. 172.

¹¹⁷European Union's appellee's submission, para. 173.

¹¹⁸European Union's appellee's submission, para. 177. According to the European Union, the authors of the Abrenica & Ducanes study (*supra*, footnote 65) expressed their personal opinion when characterizing a cross-price elasticity ranging from -0.01 and 0.07 as "low", but the Panel was entitled to consider that this coefficient was not "insignificant or immaterial" given that the excise tax "squeezed" imported spirits into a "marginal" 2-3 per cent market share. (*Ibid.*, para. 180)

¹¹⁹European Union's appellee's submission, paras. 181 and 182 (quoting Panel Reports, para. 7.55).

current proceedings. The European Union emphasizes that "[a] brandy or whisky or vodka produced in the Philippines, by a Filipino company, and sold in the Philippines, does not become an *imported* spirit even if it were to be produced, in part or wholly, with imported ethyl alcohol."¹²⁰

61. The European Union submits that the Panel correctly eschewed revisiting the question of whether domestic and imported distilled spirits are "directly competitive or substitutable" in determining whether the measure at issue is applied "so as to afford protection to domestic production". The question of whether competition between domestic and imported distilled spirits could exist pertains to the analysis of whether these products are "directly competitive or substitutable" under Article III:2, second sentence. In contrast, the examination of whether the measure is applied "so as to afford protection to domestic production" is a separate and different issue that must be examined individually, and must focus on the structure and application of the measure at issue, not on the competitive relationship between the products. For the European Union, the Philippines' argument regarding market segmentation relates to competition in the Philippine distilled spirits market, and not the structure and application of the measure at issue.

C. *Arguments of the United States – Appellee*

62. The United States takes issue with the Philippines' assertion that this dispute essentially concerns the Philippines' fiscal policy objectives and its commitment to a policy of progressive taxation, as this raises systemic issues regarding the autonomy of WTO Members. The United States takes no position on the fiscal priorities of the Philippine Government, and argues that the issue in dispute is whether the excise tax regime discriminates against imported products, in breach of Article III:2 of the GATT 1994. Moreover, the United States contends that the Philippines' claim that its excise tax regime is origin-neutral because it distinguishes on the basis of raw materials constitutes a "distorted" presentation of the measure at issue¹²¹, and that the Philippines' distinction between "sugar-based" and "non-sugar-based" distilled spirits provides "no practical information" about the products sold in its market.¹²² The distinction drawn by the excise tax regime ensures that the lowest tax rate is applied to all distilled spirits produced from designated raw materials in the Philippines, and that imported distilled spirits made from non-designated raw materials face much higher taxes.

¹²⁰European Union's appellee's submission, para. 124. (original emphasis)

¹²¹United States' appellee's submission, para. 3.

¹²²United States' appellee's submission, para. 4 (referring to Philippines' appellant's submission, para. 5).

1. Article III:2, First Sentence, of the GATT 1994

63. The United States submits that the Panel correctly interpreted and applied Article III:2, first sentence, of the GATT 1994 and that it conducted an objective assessment of the matter, as required by Article 11 of the DSU. It notes that past panels and the Appellate Body have employed a case-by-case approach to determining whether products are "like", which takes into account all relevant factors. The United States argues that, while the Panel analyzed evidence under each factor before reaching its conclusions, the Philippines largely ignores the overall analysis of the Panel and focuses entirely on physical differences between imported and domestic products and the alleged inability of most Filipino consumers to purchase imported distilled spirits on a weekly basis.

64. With regard to physical characteristics, the United States disagrees with the Philippines' claim that any "significant" physical differences between domestic and imported distilled spirits, even those that may not be perceptible to the consumer, should be sufficient to prevent a finding of "likeness". In the United States' view, the Philippines improperly reads the term "like" to mean "identical" and makes two fundamental errors. First, it overstates the importance of physical characteristics in the analysis of "likeness". Second, it overstates the importance of certain physical differences and ignores "key" physical similarities that consumers rely on when choosing brands of spirits.¹²³

65. The United States further notes that the Philippines' arguments on physical characteristics focus entirely on the physical differences that result from the use of different raw materials, particularly congeners present in the chemical composition of the products at issue and flavourings added to domestic distilled spirits. The United States submits that this emphasis on differences in additives and congeners is "unduly narrow" for a proper assessment of physical characteristics.¹²⁴ First, some physical characteristics, such as physiological effects, are similar across all types of products, while, for other characteristics, both imported products and domestic products vary from type to type. Second, domestic producers "take great pains" to make their distilled spirits similar to imported distilled spirits of the same type, so much so that they are virtually indistinguishable on the shelf for the consumer.¹²⁵ In this context, the United States agrees with the Panel's focus on the characteristics of the final products as sold to consumers, rather than on the raw materials used, and asserts that this approach is consistent with that adopted by the panel in *Mexico – Taxes on Soft Drinks*.¹²⁶ Third, the Philippines' view is at odds with the panel's findings in *Japan – Alcoholic*

¹²³United States' appellee's submission, para. 25.

¹²⁴United States' appellee's submission, para. 31.

¹²⁵United States' appellee's submission, para. 28 (referring to Panel Reports, para. 2.25)

¹²⁶United States' appellee's submission, para. 28 (referring to Panel Report, *Mexico – Taxes on Soft Drinks*, paras. 8.30, 8.31, and 8.131).

Beverages II, where the distilled spirits that were found to be "like"—vodka and shochu—shared most physical characteristics, were not necessarily made from the same raw materials, and presented possible differences in alcoholic strength.¹²⁷ In any event, the United States stresses that, with respect to organoleptic properties, there is no evidence that these differences among different types of distilled spirits indicate two separate and identifiable product groups between Philippine domestic distilled spirits and their imported counterparts.

66. The United States argues that, while physical characteristics constitute an important criterion for determining whether products are "like", they are not dispositive; rather, they are simply part of the list of factors to be considered. According to the United States, the Philippines "entirely ignores" other relevant evidence cited by the Panel—such as marketing and end-uses—that supports the Panel's finding of "likeness".

67. The United States also contests the Philippines' claim that the Panel erred in considering as irrelevant for its analysis of "likeness" the fact that, under the European Union's and the United States' internal regulations, distilled spirits labelled and marketed as whisky and brandy must be produced from specific raw materials. The United States stresses, and all parties agree, that the "relevant market" for the determination of "likeness" is the Philippines. Accordingly, the Panel correctly reviewed the Philippines' counterparts to the United States' and the European Union's regulations, which permit the sale of products labelled as brandy, whisky, and vodka, even when they are made from raw materials not traditionally associated with those types of distilled spirits.¹²⁸

68. The United States disagrees with the Philippines' claim that the Panel acted inconsistently with Article 11 of the DSU by disregarding expert evidence submitted by the Philippines with regard to the organoleptic properties and chemical composition of distilled spirits. The United States argues that, although the Panel did not directly quote or reproduce the entirety of the expert evidence proffered by the Philippines, it did summarize and consider it along with other relevant evidence, and concluded that the expert evidence was not probative of whether the products are "like".¹²⁹

69. With respect to consumer tastes and habits, the United States takes issue with the Philippines' arguments that: (i) since most domestic consumers do not have the economic means to

¹²⁷United States' appellee's submission, para. 32 (referring to Panel Report, *Japan – Alcoholic Beverages II*, para. 6.23).

¹²⁸United States' appellee's submission, para. 38. The United States cites to evidence it submitted to the Panel in Exhibits US-22 to US-25 and US-27, which contain, *inter alia*, Republic of the Philippines Department of Trade, Bureau of Standards Administrative Orders Nos. 257, 258, 259, and 358.

¹²⁹United States' appellee's submission, para. 104 (referring to Panel Reports, footnotes 397-400 to para. 7.40).

purchase imported distilled spirits on a weekly basis, the Panel erroneously found that there was competition between domestic and imported distilled spirits; and (ii) purchases of imported distilled spirits on "special occasions" are not sufficient evidence of competition. The United States observes that the Panel drew its conclusions on consumer tastes and habits from a variety of factual elements, including that the same outlets in the Philippines that sell imported distilled spirits also sell domestic distilled spirits, the similarity in marketing campaigns of domestic and imported distilled spirits, and the overlap in price among domestic and imported distilled spirits.¹³⁰

70. The United States submits that the Appellate Body report in *Japan – Alcoholic Beverages II* does not support the Philippines' assertion that a certain quantity or volume of current competition is necessary to find "likeness". In fact, the Appellate Body in that dispute did not suggest that competition must be presently occurring in order for there to be a competitive relationship between two products. Rather, it confirmed that the analysis of "likeness" will vary from case to case and should not be interpreted inflexibly.¹³¹ Moreover, the Philippines' approach would entail that imported products could never be "like" domestic products if a measure entirely excluded them from competition in a given market. Finally, the Philippines' reference to the financial constraints of domestic consumers is based on the "false" premise that the distinguishing feature of domestic and imported distilled spirits is price. Instead, as the Panel correctly found, the excise tax regime distinguishes between distilled spirits based on the raw materials they are made from, and not on the basis of price.

71. The United States also argues that there is no support for the Philippines' proposition that a product consumed on special occasions cannot be in competition with a routinely purchased product. In fact, relevant case law indicates that, since distilled spirits are consumer goods that are purchased frequently, even a purchaser of lesser means can afford to buy a more expensive bottle "at least occasionally".¹³² Furthermore, the Panel noted that the Filipino population is not divided into two separate income groups, but is rather distributed along a continuum of income brackets.

72. The United States objects to the Philippines' contention that the Panel erred under Article 11 of the DSU by disregarding the evidence proffered by the Philippines with respect to the low income

¹³⁰United States' appellee's submission, para. 40 (referring to Panel Reports, paras. 2.36, 2.41, 2.42, 7.51, and 7.59).

¹³¹United States' appellee's submission, para. 43 (referring to Appellate Body Report, *Japan – Alcoholic Beverages II*, pp. 20-21, DSR 1996:1, 97, at 113-114).

¹³²United States' appellee's submission, para. 47 (quoting Panel Report, *Korea – Alcoholic Beverages*, para. 10.74). The United States notes that the case law mentioned refers to "directly competitive or substitutable" products under Article III.2, second sentence, of the GATT 1994. However, it argues that there is nothing to suggest that the same reasoning cannot apply to the analysis of "likeness". (*Ibid.*, para. 48)

of the vast majority of the Filipino population, which allegedly showed the existence of two separate distilled spirits markets. The United States stresses that neither the complainants nor the Panel contested the assertion that most Filipinos are low-income consumers, but adds that such evidence does not necessarily lead to the conclusion that the market is fragmented. According to the United States, the Panel's failure to draw the conclusion suggested by the Philippines from the evidence in question demonstrates that it considered other evidence more probative and relevant to the issue before it.

73. Lastly, with respect to tariff classification, the United States contests the Philippines' claim that the Panel erred in its analysis of this "likeness" criterion because the range of products falling under the four-digit HS heading is not sufficiently detailed to draw any particular inferences on whether the products are "like". The United States also disagrees with the Philippines' contention that the Panel erred under Article 11 of the DSU when it found that the six-digit HS subheadings were inconclusive despite the fact that raw materials may be relevant for the six-digit level classification of brandy and whisky. The United States stresses that the Appellate Body in *Japan – Alcoholic Beverages II* stated that tariff classification can be relevant in determining likeness, but it does not oblige panels to draw conclusions from it in all circumstances.¹³³ The United States contends that the Panel simply reviewed evidence on four-digit HS classification and found some indications of similarity, thereby making an appropriate application of the criterion to the specific facts of this dispute. Moreover, the Panel thoroughly examined the six-digit HS subheadings and found that the totality of the evidence on this point was inconclusive, thereby fulfilling its duties under Article 11 of the DSU.

2. Article III:2, Second Sentence, of the GATT 1994

74. The United States submits that the Panel did not err in finding that the Philippines has acted inconsistently with the requirements of Article III:2, second sentence, of the GATT 1994 because the Philippines applies dissimilar internal taxes on domestic distilled spirits made from designated raw materials and "directly competitive or substitutable" imported distilled spirits made from non-designated raw materials, "so as to afford protection to domestic production" of distilled spirits. More specifically, the United States argues that the Panel correctly held that domestic distilled spirits made from designated raw materials and imported distilled spirits made from non-designated raw materials are "directly competitive or substitutable" within the meaning of that provision. The United States also argues that the Panel correctly found that the Philippines' excise tax is applied "so as to

¹³³United States' appellee's submission, para. 51 (referring to Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 21, DSR 1996:1, 97, at 114).

afford protection to domestic production" of distilled spirits within the meaning of Article III:2, second sentence, of the GATT 1994.

(a) Directly Competitive or Substitutable Products

75. The United States argues that the Panel did not err in finding that domestic distilled spirits made from designated raw materials and imported distilled spirits made from non-designated raw materials are "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the GATT 1994. The United States requests the Appellate Body to uphold the Panel's finding for the following reasons.

76. First, the United States argues that the Panel's analysis sufficiently addresses the "degree" of proximity" in competition between domestic and imported distilled spirits, as required by the legal standard of Article III:2, second sentence.¹³⁴ For the United States, the Philippines seeks to minimize the significance of other types of evidence relied on by the Panel, such as evidence suggesting that consumers may purchase imported distilled spirits on special occasions, the lack of differentiation in marketing and labelling, and identity in channels of distribution.¹³⁵ The Appellate Body's statement in *US – Cotton Yarn* that "[l]ike products are necessarily in the highest degree of competitive relationship in the marketplace" is not relevant, because it compares the term "like product" to the term "directly competitive" in Article 6.2 of the *Agreement on Textiles and Clothing*.¹³⁶ According to the United States, the Panel's conclusion that there is a "significant degree of competitiveness or substitutability" between domestic and imported distilled spirits in the Philippine market disproves the Philippines' argument that the Panel did not evaluate the "degree of proximity" of competition.¹³⁷

77. Second, the United States rejects the Philippines' argument that the Panel found direct competition because some consumers may be able to buy imported distilled spirits on "special occasions". The United States contends that there is no "frequency" requirement for direct competition under Article III:2.¹³⁸ The United States adds that Philippine producers present their products as appropriate for special occasions. According to the United States, there is no evidence that the "need or taste" that distilled spirits satisfy on special occasions, including relaxation and

¹³⁴United States' appellee's submission, para. 70.

¹³⁵United States' appellee's submission, para. 66 (referring to Panel Reports, paras. 7.119, 7.123, and 7.131).

¹³⁶United States' appellee's submission, para. 68 (quoting Appellate Body Report, *US – Cotton Yarn*, para. 97).

¹³⁷United States' appellee's submission, para. 69 (quoting Panel Reports, para. 7.113).

¹³⁸United States' appellee's submission, para. 73.

The assessment of potential competition is particularly important in situations like the present case, where the challenged measure has the effect of "freezing consumer preferences" by imposing significant costs on the purchase of imported distilled spirits.¹⁴⁶ The United States further submits that the observed price overlaps for both low- and high-priced products undermine the Philippines' allegation that the market is divided into two distinct segments.¹⁴⁷ According to the United States, the Panel properly relied on evidence of similarity in product characteristics, marketing, and end-uses in finding that domestic and imported distilled spirits have the potential to be directly competitive or substitutable.¹⁴⁸ Therefore, the Panel did not exceed its discretion under Article 11 of the DSU in reaching its finding.

81. Finally, the United States argues that the Panel did not act inconsistently with Article 11 of the DSU, because it adequately examined the economic studies on substitutability and drew appropriate conclusions on the basis of that evidence. The Panel's conclusion that there was a significant degree of competitiveness or substitutability between domestic and imported distilled spirits in the Philippine market was based on a variety of evidence, including market studies, similarity of marketing campaigns, labelling, and sales locations.¹⁴⁹ Moreover, the Panel "thoroughly weighed" both the *Euromonitor International* and Abrenica & Ducanes studies, including concerns with their methodologies.¹⁵⁰ The United States also notes that the sample used in the *Euromonitor International* survey was adjusted in a manner that allowed for closer alignment with the overall Filipino population, and that respondents indicated that they would be more likely to purchase an imported brand if the price differential were smaller.¹⁵¹ Moreover, the Abrenica & Ducanes study supports the Panel's findings on substitutability, because it does show substitutability in spite of persistent price gaps between imported and domestic products, and other factors such as brand loyalty.

¹⁴⁶United States' appellee's submission, para. 85 (quoting Panel Reports, para. 7.106, in turn quoting Appellate Body Report, *Korea – Alcoholic Beverages*, paras. 119 and 120; and Panel Report, *Chile – Alcoholic Beverages*, para. 7.25).

¹⁴⁷United States' appellee's submission, para. 86.

¹⁴⁸United States' appellee's submission, para. 137 (referring to Panel Reports, paras. 7.127, 7.129, and 7.131).

¹⁴⁹United States' appellee's submission, para. 118 (referring to Panel Reports, para. 7.51; and quoting para. 7.61).

¹⁵⁰United States' appellee's submission, para. 120.

¹⁵¹United States' appellee's submission, paras. 121 and 122 (referring to *Euromonitor International* survey, *supra*, footnote 37, pp. 6 and 30).

socialization, are different such that "special occasion" products do not compete directly with other products.

78. Third, the United States posits that the Panel did not err in assessing the competitive relationship between domestic and imported distilled spirits on the basis of evidence demonstrating actual competition "within a subset" of the Philippine market.¹³⁹ For the United States, the Panel's findings simply acknowledge that, notwithstanding the relatively low income of the average Filipino consumer, a "subset" of the market may purchase imported distilled spirits even though they are generally more expensive. This is only "logical" because "the existence of current competition certainly does not show *less* likelihood of a competitive relationship."¹⁴⁰ The United States also considers that the Philippines' challenge is directed at the weighing of the evidence by the Panel. For the United States, the Panel was correct in observing that instances of "actual competition" are a clear indication that the imported and domestic distilled spirits are "*capable*" of being directly competitive or substitutable in the future.¹⁴¹

79. Fourth, the United States disagrees with the Philippines that the Panel was required to assess competition in a portion of the market that is representative of the "market as a whole."¹⁴² In the United States' view, the Philippines takes out of context the Panel's statements concerning the reliability of the methodological sample used in the cross-price elasticity studies. In addition, the Panel expressly found that the Philippine market is not segmented in the manner suggested by the Philippines, and that many consumers can purchase imported distilled spirits on special occasions.¹⁴³ For the United States, the Panel correctly held that Article III:2, second sentence, "does not protect just *some* instances or *most* instances, but rather, it protects *all* instances of direct competition".¹⁴⁴

80. Fifth, the United States posits that the Panel correctly held that there is potential competition between domestic and imported distilled spirits in the Philippine market. The United States maintains that direct competition under Article III:2, second sentence, does not require "some minimum threshold amount of actual competition", because two products may be "directly competitive or substitutable" even if direct competition is only potential and is not occurring at the present time.¹⁴⁵

¹³⁹United States' appellee's submission, para. 76.

¹⁴⁰United States' appellee's submission, para. 78. (original emphasis)

¹⁴¹United States' appellee's submission, para. 81 (quoting Panel Reports, para. 7.121). (original emphasis)

¹⁴²United States' appellee's submission, para. 87 (quoting Philippines' appellant's submission, para. 117).

¹⁴³United States' appellee's submission, para. 88 (referring to Panel Reports, paras. 7.118 and 7.119).

¹⁴⁴United States' appellee's submission, para. 88 (quoting Panel Reports, para. 7.120 (original emphasis)).

¹⁴⁵United States' appellee's submission, paras. 83 and 84.

(b) "So as to afford protection to domestic production"

82. The United States argues that the Panel did not err in finding that the dissimilar taxes imposed on imported distilled spirits and on directly competitive or substitutable domestic distilled spirits are applied "so as to afford protection to domestic production" of distilled spirits. The United States requests the Appellate Body to dismiss the Philippines' appeal in this respect, and to uphold the Panel's finding.

83. The United States submits that the Panel correctly focused on the "magnitude of the difference in taxation between domestic and imported goods, and also the design, structure and application" of the measure at issue.¹⁵² The Panel rightly observed that the design, architecture, and structure of the measure are such that the designated raw materials from which a distilled spirit must be made in order to enjoy the lower tax are all grown in the Philippines, and that the vast majority of imported distilled spirits are not made from designated raw materials. Thus, the Panel was correct in finding that "*de facto* the measure results in all domestic distilled spirits enjoying the favourable low tax, while the vast majority of the imported spirits are subject to higher taxes."¹⁵³ The United States stresses that the magnitude of the tax differential applied to imported products, which is ten to forty times higher than taxes on domestic products, is sufficient to show that the measure protects Philippine production of distilled spirits.

84. Furthermore, the United States argues that the Panel correctly focused on the measure itself, which differentiates products according to their raw material base. The fact that Philippine producers import ethyl alcohol as an input does not undermine the Panel's conclusion that the structure of the measure favours Philippine producers of distilled spirits, which are the products at issue in the present dispute, not ethyl alcohol. In addition, although it was not necessary for the Panel to inquire into the motivation for the measure, the United States stresses that the Panel had before it statements from Philippine Government officials stating that the purpose of the measure was to protect domestic production.¹⁵⁴

D. *Claim of Error by the European Union – Other Appellant*

85. The European Union claims that the Panel erred in characterizing its claims under Article III:2, second sentence, of the GATT 1994 as made in the "alternative" to its claims under the

¹⁵²United States' appellee's submission, para. 93.

¹⁵³United States' appellee's submission, para. 93 (quoting Panel Reports, para. 7.182 (original emphasis)).

¹⁵⁴United States' appellee's submission, paras. 97 and 98 (referring to, for example, a letter from the Philippines Department of Trade and Industry, dated 11 May 2009 (Panel Exhibit US-11)).

first sentence of that provision. According to the European Union, in failing to make findings in relation to the European Union's claims under Article III:2, second sentence, of the GATT 1994, the Panel acted inconsistently with Articles 7.1, 7.2, and 11 of the DSU, and exercised false judicial economy, thereby acting inconsistently with Articles 3.7 and 21.1 of the DSU. Accordingly, the European Union requests the Appellate Body to reverse the Panel's characterization of its claim under Article III:2, second sentence, as "alternative", to complete the legal analysis with respect to the European Union's claims under that provision, and to find that the Philippines has acted inconsistently with Article III:2, second sentence, of the GATT 1994.

86. Referring to the specific language used in its request for the establishment of a panel¹⁵⁵, its first written submission to the Panel¹⁵⁶, and its responses to Panel questions¹⁵⁷, the European Union maintains that it made "two *separate and independent*" claims under the first and second sentences of Article III:2, which it characterized as "main" claims.¹⁵⁸ The European Union's statement that, the Panel "would not necessarily need to analyse a breach of the second sentence" if it were to find a breach of the first sentence of Article III:2, referred to the "consequential" nature of the European Union's claims under these provisions, insofar as "directly competitive or substitutable" products are a subset of "like products".¹⁵⁹ Thus, a finding of breach under Article III:2, first sentence, would "almost automatically" lead to a finding of breach of the second sentence of the same provision.¹⁶⁰

87. According to the European Union, in failing to address its claims under Article III:2, second sentence, of the GATT 1994, the Panel acted inconsistently with Articles 7.1 and 7.2 of the DSU, which requires panels to "respect their terms of reference and to address all the relevant provisions of the WTO Agreements cited by the parties".¹⁶¹ In addition, the Panel acted inconsistently with Article 11 of the DSU because it failed to make an objective assessment of the matter before it and declined to make findings that would have assisted the DSB in making the

¹⁵⁵European Union's other appellant's submission, paras. 8 and 9 (referring to Request for the Establishment of a Panel by the European Union, WT/DS396/4, p. 3).

¹⁵⁶European Union's other appellant's submission, paras. 10-18 (referring to European Union's first written submission to the Panel, paras. 48-52 and 192).

¹⁵⁷European Union's other appellant's submission, paras. 19-23 (referring to European Union's response to Panel Question 18, paras. 11 and 12; and referring to European Union's response to Panel Question 64).

¹⁵⁸European Union's other appellant's submission, para. 20. (original emphasis)

¹⁵⁹European Union's other appellant's submission, para. 17 (referring to European Union's first written submission to the Panel, para. 52).

¹⁶⁰European Union's other appellant's submission, para. 17. The European Union also made a "subordinate claim" that each type of imported and domestic distilled spirit (gin, brandy, rum, whisky, tequila and tequila-flavoured spirits) was "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the GATT 1994. (European Union's response to Panel Question 18, para. 12)

¹⁶¹European Union's other appellant's submission, para. 31.

recommendations or rulings required.¹⁶² Finally, the European Union suggests that the Panel's analysis of the United States' claim under Article III:2, second sentence, of the GATT 1994, which considers arguments made by the European Union and is an integral part of the Panel Reports in this dispute, provide the Appellate Body with sufficient "factual findings of the Panel and/or undisputed facts in the record" to enable it to complete the legal analysis in relation to the European Union's claims under Article III:2, second sentence, of the GATT 1994.¹⁶³

E. *Arguments of the Philippines – Appellee*

88. The Philippines considers that the European Union's claim on appeal "does not contribute to the substantive adjudication of the legal matter" before the Appellate Body in this dispute.¹⁶⁴ In light of the Philippines' appeal of the Panel's findings on the United States' substantive claim under Article III:2, second sentence, of the GATT 1994, the Philippines contends that the merits of the European Union's other appeal will be fully addressed by the Appellate Body regardless of how the Appellate Body considers the European Union's claim on appeal. Accordingly, the Philippines "does not submit any particular arguments for or against" the European Union's other appeal.¹⁶⁵

F. *Arguments of the Third Participants*

1. Australia

89. Australia agrees with the Philippines that the term "like" under Article III:2, first sentence, of the GATT 1994 should be construed narrowly. However, in Australia's view, this does not mean that any physical difference would necessarily disqualify a product from being considered "like" another product. The panel in *Japan – Alcoholic Beverages II* identified the appropriate standard in that case to be "[s]ubstantial noticeable differences in physical characteristics".¹⁶⁶ Moreover, assessing the significance of differences in physical characteristics between products should not be limited to consideration of a single characteristic, but should be an assessment based on all the physical characteristics of the products at issue, such as, appearance, ingredients, flavour, and smell. According to Australia, the facts in this dispute indicate that the raw materials used in the products do

¹⁶²The European Union also suggests that, to the extent that the Panel's failure to address the European Union's claim under Article III:2, second sentence, constituted an application of the principle of judicial economy, the European Union submits that this would amount to "false application of that principle", inconsistent with Articles 3.7 and 21.1 of the DSU. (European Union's other appellant's submission, para. 35)

¹⁶³European Union's other appellant's submission, paras. 40-49 (quoting Appellate Body Report, *Australia – Salmon*, para. 118).

¹⁶⁴Philippines' appellee's submission, para. 2.

¹⁶⁵Philippines' appellee's submission, para. 3.

¹⁶⁶Australia's third participant's submission, para. 6 (quoting Panel Report, *Japan – Alcoholic Beverages II*, para. 6.23). (emphasis added by Australia)

not materially alter consumer perception of the product. Rather, consumer perception appears to be affected by the appearance, taste, and smell of the product, as well as its marketing as a particular type of spirit, such as, brandy, gin, etc.

90. With regard to the Philippines' appeal of the Panel's finding under Article III:2, second sentence, of the GATT 1994, Australia notes that the panel in *Japan – Alcoholic Beverages II* found that "the decisive criterion" in determining whether products are "directly competitive or substitutable" "is whether they have common end uses, *inter alia*, as shown by elasticity of substitution".¹⁶⁷ In this regard, the facts in this dispute indicate that domestically produced and imported distilled spirits are marketed as the same "type" of spirit, often using similar packaging and branding, and that the nature and content of the products' marketing strategies seem to indicate that they are competing in a similar market segment.

91. Australia disagrees with the Philippines' contention that products purchased on "special occasions" cannot directly compete with more frequently purchased "everyday" products, and notes that previous panels have found that products with different NRPs can be "directly competitive" even if the products are not purchased with the same frequency.¹⁶⁸ With regard to the Philippines' contention that the Panel erred by relying on speculation as to potential future competitive relationships between the products at issue, Australia observes that previous panels have taken into account evidence of both the existing market competition as well as evidence of future potential market competition between products.¹⁶⁹

92. With regard to the relationship between the first and second sentences of Article III:2 of the GATT 1994, Australia agrees with the Appellate Body's finding in *Korea – Alcoholic Beverages* that "like products" are a subset of directly competitive or substitutable products and, therefore, all "like products" are, by definition, directly competitive or substitutable.¹⁷⁰ Australia, however, disagrees with the European Union's assertion that, if a panel makes a finding that there has been a violation of Article III:2, first sentence, then this would "almost automatically lead to a finding of a breach of the

¹⁶⁷Australia's third participant's submission, para. 12 (quoting Panel Report, *Japan – Alcoholic Beverages II*, para. 6.22). The Appellate Body endorsed this view of the panel. (Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 25, DSR 1996:1, 97, at 117)

¹⁶⁸Australia's third participant's submission, para. 14 (referring to Panel Report, *Korea – Alcoholic Beverages*, para. 10.74; Panel Report, *Chile – Alcoholic Beverages*, para. 7.37).

¹⁶⁹Australia's third participant's submission, para. 15 (referring to, for example, Panel Report, *Chile – Alcoholic Beverages*, para. 7.47).

¹⁷⁰Australia's third participant's submission, para. 16 (quoting Appellate Body Report, *Korea – Alcoholic Beverages*, para. 118).

second sentence of the same provision".¹⁷¹ In Australia's view, the panel would still need to give full and separate consideration to all the elements of a claim under Article III:2, second sentence, as stated by the Appellate Body in *Japan – Alcoholic Beverages II*.¹⁷²

93. Australia observes that the Philippines has made five separate allegations under Article 11 of the DSU in respect of its claim that the Panel failed to make an objective assessment of the facts. In this regard, Australia notes that, from a systemic perspective, it would be of concern if claims under Article 11 were, in effect, requiring the Appellate Body to "second-guess a panel's conclusions".¹⁷³

2. Mexico

94. Mexico considers that the Panel's analysis of "likeness" was adequate with regard to its finding that the imported and domestic distilled spirits at issue in this dispute are "like products" within the meaning of Article III:2, first sentence, of the GATT 1994. Mexico notes, however, that the Panel's analysis was made in the context of the facts of this dispute and in the context of the Philippines' distilled spirits market in particular. According to Mexico, a "like product" analysis in any other context has to take into account the specific circumstances of each case.¹⁷⁴ Mexico cites, as an example, tequila produced in Mexico, which is made from agave and is combined with up to 49 per cent of other sugars, and is protected by a recognized appellation of origin in many countries. Mexico contends that such a situation could be decisive when analyzing the properties, nature, and quality of the product as well as its end-uses and consumer tastes and habits in the context of a market other than the one at issue in this dispute, or with regard to different provisions of the *WTO Agreement*.¹⁷⁵

95. With regard to the Philippines' appeal of the Panel's finding under Article III:2, second sentence, of the GATT 1994, Mexico considers that the Panel's analysis of "directly competitive and substitutable products" was adequate, and submits that the Appellate Body should confirm the Panel's conclusion that the Philippines has acted inconsistently with this provision.¹⁷⁶

¹⁷¹Australia's third participant's submission, para. 17 (quoting European Union's other appellant's submission, para. 17).

¹⁷²Australia's third participant's submission, para. 19 (quoting Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 24, DSR 1996:1, 97, at 116).

¹⁷³Australia's third participant's submission, para. 22.

¹⁷⁴Mexico's third participant's submission, para. 10.

¹⁷⁵Mexico's third participant's submission, para. 9.

¹⁷⁶Mexico's third participant's submission, para. 14.

III. **Issues Raised in This Appeal**

96. The following issues are raised in this appeal:

- (a) whether the Panel erred in finding that the Philippines has acted inconsistently with Article III:2, first sentence, of the GATT 1994 by applying to imported distilled spirits made from raw materials other than those designated in its legislation internal taxes in excess of those applied to "like" domestic distilled spirits made from designated raw materials, and in particular:
- (i) whether the Panel erred in finding that each type of imported distilled spirit at issue in this dispute—gin, brandy, vodka, whisky, and tequila—made from non-designated raw materials is "like" the same type of domestic distilled spirit made from designated raw materials¹⁷⁷ within the meaning of Article III:2, first sentence, of the GATT 1994;
 - (ii) whether the Panel erred in finding that all the distilled spirits at issue, whether imported or domestic, and irrespective of the raw materials from which they are made, are "like products" within the meaning of Article III:2, first sentence, of the GATT 1994; and
 - (iii) whether the Panel, in finding that the products at issue are "like" within the meaning of Article III:2, first sentence, of the GATT 1994, acted inconsistently with its duties under Article 11 of the DSU in its assessment of: (1) the products' physical characteristics; (2) the Philippine market for distilled spirits; and (3) tariff classification;
- (b) whether the Panel erred in characterizing the European Union's claim under Article III:2, second sentence, of the GATT 1994 as made in the "alternative" to its claim under the first sentence of Article III:2, and consequently acted inconsistently with Articles 7.1, 7.2, and 11 of the DSU in abstaining from making findings in relation to the European Union's claim under Article III:2, second sentence, of the GATT 1994; and

¹⁷⁷Domestic distilled spirits made from designated raw materials include also tequila-flavoured spirits.

(c) whether the Panel erred in finding that the Philippines has acted inconsistently with Article III:2, second sentence, of the GATT 1994 by applying dissimilar taxation to imported distilled spirits made from non-designated raw materials and to "directly competitive or substitutable" domestic distilled spirits made from designated raw materials, so as to afford protection to domestic production, and in particular:

- (i) whether the Panel erred in finding that all the distilled spirits at issue, whether imported or domestic, and irrespective of the raw materials from which they are made, are "directly competitive or substitutable" products within the meaning of Article III:2, second sentence, of the GATT 1994;
- (ii) whether the Panel acted inconsistently with its duties under Article 11 of the DSU in reaching its finding that the imported and domestic distilled spirits at issue, irrespective of the raw material from which they are made, are "directly competitive or substitutable" products within the meaning of Article III:2, second sentence, of the GATT 1994; and
- (iii) whether the Panel erred in finding that dissimilar taxation imposed by the Philippines on imported distilled spirits and on "directly competitive or substitutable" domestic distilled spirits is applied "so as to afford protection" to Philippine domestic production of distilled spirits.

IV. Background

A. *The Measure at Issue*

97. The measure at issue in this dispute is the excise tax regime in force in the Philippines as it applies to distilled spirits. The Panel referred to it as the "excise tax".¹⁷⁸ Under the measure at issue,

taxes are collected on distilled spirits in accordance with the criteria set out in Section 141 of the Philippines' National Internal Revenue Code of 1997 (the "NIRC"), as amended.¹⁷⁹

98. Under Section 141(a) of the NIRC, distilled spirits are subject to a specific flat tax rate if two requirements are met: (i) the distilled spirits are produced from one of the following raw materials—sap of the *nipa*, coconut, cassava, *camote*, *huri* palm, or from juice, syrup, or sugar of the cane (collectively referred to as "designated raw materials"¹⁸⁰); and (ii) the designated raw materials are produced commercially in the country where they are processed into distilled spirits. As from 1 January 2011, the flat rate set out in Section 141(a) is 14.68 Philippine pesos ("PHP") per proof litre ("ppl").¹⁸¹

99. Under Section 141(b) of the NIRC, all distilled spirits that do not meet either of the requirements set forth above are subject to three different tax rates that apply depending on the net retail price ("NRP") of a 750 millilitre ("ml") bottle of the spirit.¹⁸² As from 1 January 2011, distilled spirits falling under Section 141(b) are subject to a tax of: (i) PHP 158.73 ppl¹⁸³, if their NRP is less than PHP 250; (ii) PHP 317.44 ppl¹⁸⁴, if their NRP is between PHP 250 and PHP 675; or (iii) PHP 634.90 ppl¹⁸⁵, if their NRP is more than PHP 675.¹⁸⁶

¹⁷⁹Panel Reports, para. 2.2. Amendments to the NIRC and other relevant regulations to this dispute include: Section 1 of Republic Act No. 9334; Republic Act No. 8240; *Revenue Regulations No. 02-97 Governing Excise Taxation on Distilled Spirits, Wines and Fermented Liquors*; *Revenue Regulations No. 17-99 Implementing Sections 141, 142, 143 and 145(A) and (C)(1), (2), (3) and (4) of the National Internal Revenue Code of 1997*; *Revenue Regulations No. 9-2003 Amending Certain Provisions of Revenue Regulations No. 1-97 and Revenue Regulations No. 2-97*; *Revenue Regulations No. 23-2003 Implementing the Revised Tax Classification of New Brands of Alcohol Products and Variants Thereof*; *Revenue Regulations No. 12-2004 Providing for the Revised Tax Rates on Alcohol and Tobacco Products*; and *Revenue Regulations No. 3-2006 Prescribing the Implementing Guidelines on the Revised Tax Rates on Alcohol and Tobacco Products*. (Panel Reports, para. 2.1)

¹⁸⁰Panel Reports, para. 2.3.

¹⁸¹Equivalent to approximately US\$0.34 ppl. All the tax rates under Section 141 of the NIRC are set in "proof litres". Since distilled spirits have different alcohol contents (proof) and bottle volumes, the specific excise tax applicable to a particular spirit will vary depending on these factors. Under Philippine law, a "proof litre" is defined as a "liquor containing one-half (½) of its volume of alcohol of a specific gravity of seven thousand nine hundred and thirty-nine ten thousandths (0.7939) at fifteen degrees centigrade (15°C)". (See Republic Act 9334, p. 3, submitted as Panel Exhibits EU-2, US-2, and PH-4. See also European Union's first written submission to the Panel, footnote 18 to para. 1.5) The "proof" of an alcoholic beverage is equal to twice its alcohol content by volume.

¹⁸²Panel Reports, para. 2.4.

¹⁸³Equivalent to approximately US\$3.68 ppl.

¹⁸⁴Equivalent to approximately US\$7.36 ppl.

¹⁸⁵Equivalent to approximately US\$14.72 ppl.

and colour—upon a specific distilled spirit. Levels and combinations of various congeners differ according to the type of spirit. The typical organoleptic properties of certain distilled spirits—such as brandy, rum, whisky, or tequila—depend on the raw materials used in their production, as well as on post-distillation processes such as ageing, blending, filtering, diluting with water, and incorporating additional flavourings. For other types of distilled spirits—such as gin and vodka—the ethyl alcohol is normally stripped of its congeners so as to obtain a neutral spirit.

103. It was not disputed before the Panel that all distilled spirits, irrespective of their origin or of the raw materials used in their production, have the same end-uses in the Philippines, which the Panel described as "thirst quenching, socialization, relaxation, pleasant intoxication".¹⁹⁰ They can be drunk straight or with ice, diluted with soft drinks or fruit juices or used in the preparation of cocktails. In the Philippines, premium distilled spirits are largely consumed in restaurants, bars, pubs, clubs, and discotheques, whereas less expensive distilled spirits are mostly consumed in private homes.¹⁹¹

104. The Panel found that the vast majority of the distilled spirits imported into the Philippines are produced by distilling different raw materials, none of which is a "designated raw material" under Section 141(a) of the NIRC, with the exception of rum, which is processed from the fermentation of sugar cane. More specifically, gin is produced "by redistilling a high proof neutral spirit with juniper berries and other botanicals"¹⁹²; brandy is produced "from the fermentation of grapes" or "the distillation of wine or fortified wine"¹⁹³; vodka is a "neutral spirit" that can be produced "from the distillation of many different products, such as wheat, beets, corn, rye, potatoes, grapes or sugar cane"¹⁹⁴; whisky is produced "from the distillation of a mash of cereals or grains"¹⁹⁵; and tequila is "traditionally produced in Mexico from the fermentation of the agave plant".¹⁹⁶

105. In contrast, all the distilled spirits produced in the Philippines are made from sugar cane, one of the "designated raw materials" under Section 141(a). The ethyl alcohol distilled from sugar cane molasses is normally stripped of its natural congeners so as to obtain a neutral spirit. Subsequently, flavouring, essences, and other ingredients are added to the neutral spirit in order to give it the organoleptic properties typically associated with the specific distilled spirit concerned. The only exception is rum, whose production process, as outlined above, is identical in the Philippines and

¹⁹⁰Panel Reports, para. 2.38 (quoting European Union's first written submission to the Panel, para. 64).
¹⁹¹Panel Reports, para. 2.40 (referring to Philippines' first written submission to the Panel, paras. 263-266).

¹⁹²Panel Reports, para. 2.55.

¹⁹³Panel Reports, para. 2.62.

¹⁹⁴Panel Reports, para. 2.75.

¹⁹⁵Panel Reports, para. 2.81.

¹⁹⁶Panel Reports, para. 2.87.

100. According to the evidence before the Panel, all distilled spirits produced in the Philippines are made from designated raw materials—more precisely, from one designated raw material: sugar cane—and based on ethyl alcohol processed either in the Philippines or in other countries where sugar cane is produced commercially. Accordingly, all distilled spirits produced domestically are subject to the flat tax rate under Section 141(a) (PHP 14.68 ppl). In contrast, the vast majority of distilled spirits imported into the Philippines are processed from raw materials other than those designated, and are therefore subject to one of the three tax rates set out in Section 141(b) (PHP 158.73 ppl, PHP 317.44 ppl, or PHP 634.90 ppl, depending on their NRP).

101. The classification and applicable tax of brands of distilled spirits is generally indicated in annexes to relevant acts and regulations, and is overseen by the Philippines' Bureau of Internal Revenue ("BIR"). Once a specific brand has been classified as falling under Section 141(a) or Section 141(b), a reclassification of that brand may not occur except through an Act of Congress. However, if a taxpayer considers that the classification has not been made correctly, that taxpayer may request a ruling from the Commissioner of Internal Revenue and, in case of an adverse decision, seek review by the Secretary of Finance.¹⁸⁷

B. *The Products at Issue*

102. All products at issue in the present dispute are distilled spirits, and in particular the following types: gin, brandy, rum, vodka, whisky, tequila, and tequila-flavoured spirits. Distilled spirits are defined as concentrated forms of potable alcohol obtained through the process of distillation.¹⁸⁸ Combined, ethyl alcohol and water account for more than 99 per cent of the content of all distilled spirits. The average alcohol content ranges from 25 to 40 per cent by volume (or 50 to 80 proof).

Spirits of the same type tend to have similar alcohol content.¹⁸⁹ The distillation process starts with the fermentation of feedstock—that is, any raw material that contains natural sugar or other carbohydrates that can be converted into sugar, such as, sugar cane molasses, sugar beet, roots, juice of grapes, or mash of grains or cereals. Different chemical compounds, called "congeners", are formed during the process of fermentation. These congeners confer the typical organoleptic properties—flavour, aroma,

¹⁸⁶In order to illustrate how the Philippines' excise tax system operates concretely, the Panel provided the following two examples: (i) under Section 141(a) of the NIRC, a 750 ml bottle of 80 per cent proof whisky made from a designated raw material would be subject to a tax of PHP 8.81; and (ii) under Section 141(b) of the NIRC, a 750 ml bottle of 86 per cent proof whisky made from a non-designated raw material and sold at an NRP of between PHP 250 and PHP 675 would be subject to a tax of PHP 204.75. (Panel Reports, footnote 33 to para. 2.5)

¹⁸⁷Panel Reports, paras. 2.15 and 2.16.

¹⁸⁸Panel Reports, para. 2.22.

¹⁸⁹Panel Reports, para. 2.22 (referring to European Union's first written submission to the Panel, para. 84).

- (3) Spirits obtained exclusively by distilling fermented products of the sugar cane (sugar-cane juice, sugar-cane syrup, sugar-cane molasses), e.g., rum, tafia, cachaca.
- (4) Spirituous beverages known as gin or Geneva, containing the aromatic principles of juniper berries.
- (5) Vodka obtained by distilling fermented mash of agricultural origin (e.g., cereals, potatoes) and sometimes further treated with activated charcoal or carbon.¹⁹⁹

108. Based on the HSEN to HS heading 2208, brandy and whisky are classified at the HS six-digit level depending on the raw materials from which they are made. Brandy is one of the "[s]pirits obtained by distilling grape wine or grape marc" (HSEN to subheading 2208.20), while whisky is defined as a "spirit[] obtained by distilling fermented mash of cereal grains" (HSEN to subheading 2208.30). Rum is defined in HS subheading 2208.40 and in the relevant HSEN as a "[s]pirit[] obtained by distilling fermented sugarcane products" and, specifically, sugar cane molasses.²⁰⁰ Vodka is described as a spirit obtained by distilling "fermented mash of agricultural origin", with "cereals" and "potatoes" indicated as examples (HSEN to subheading 2208.50), thus not excluding vodka made from other raw materials. Gin is described as a spirituous beverage "containing the aromatic principles of juniper berries", but with no reference to its raw material base (HSEN to subheading 2208.60). There is no six-digit HS subheading for "tequila" or "tequila-flavoured spirits".

V. Article III:2, First Sentence, of the GATT 1994

109. We begin with the Philippines' appeal of the Panel's findings that imported distilled spirits made from non-designated raw materials and domestic distilled spirits made from designated raw materials are "like products" within the meaning of Article III:2, first sentence, of the GATT 1994 and that, as a consequence, by subjecting imported distilled spirits made from non-designated raw materials to internal taxes in excess of those applied to "like" domestic distilled spirits made from designated raw materials, the Philippines acts in a manner inconsistent with Article III:2, first sentence, of the GATT 1994.

¹⁹⁹Panel Reports, para. 2.53 (referring to Harmonized Commodity Description and Coding System, Explanatory Notes, 4th edn (WCO, 2007), p. IV-2208-1 (Panel Exhibit PH-46)).
²⁰⁰Panel Reports, para. 7.67.

elsewhere. For this reason, the parties agree, and the Panel found, that rum produced in the Philippines and imported rum are "like products".¹⁹⁷

106. All the distilled spirits relevant to this dispute fall under heading 2208 of the Harmonized Commodity Description and Coding System of the World Customs Organization ("HS"). This four-digit heading refers to "undenatured ethyl alcohol of an alcoholic strength by volume of less than 80% vol; spirits, liqueurs and other spirituous beverages".¹⁹⁸ At the six-digit level, the HS classifies distilled spirits under different subheadings:

Heading	HS 6-digit Code	Description
22.08		Undenatured ethyl alcohol of an alcoholic strength by volume of less than 80% vol; spirits, liqueurs and other spirituous beverages
	2208.20	- Spirits obtained by distilling grape wine or grape marc
	2208.30	- Whiskies
	2208.40	- Rum and other spirits obtained by distilling fermented sugarcane products
	2208.50	- Gin and Geneva
	2208.60	- Vodka
	2208.70	- Liqueurs and cordials
2208.80	- Other	

107. The content of the six-digit HS subheadings in question is clarified in the Explanatory Note accompanying the HS ("HSEN") to HS heading 2208 as follows:

[Heading 2208] includes, *inter alia*:

- (1) Spirits obtained by distilling grape wine or grape marc (Cognac, Armagnac, brandy, grappa, pisco, singani, etc.).
- (2) Whiskies and other spirits obtained by distilling fermented mash of cereal grains (barley, oats, rye, wheat, corn, etc.).

¹⁹⁷Panel Reports, para. 2.69 (referring to European Union's first written submission to the Panel, para. 97; United States' first written submission to the Panel, para. 30; and Philippines' first written submission to the Panel, para. 171). While the Panel noted that the parties agree that all rums at issue in the present dispute are "like products", it observed that some brands of imported rum, albeit made from sugar cane—one of the designated raw materials—are subject to the higher excise tax rates provided for in Section 141(b) of the NIRC (*Ibid.*, para. 2.74).
¹⁹⁸Panel Reports, para. 2.49. (footnote omitted)

1. The Products' Physical Characteristics

114. We begin by considering the Philippines' claims in respect of the Panel's assessment of the products' physical characteristics. First, we address the Philippines' claim that the Panel erred in its interpretation of the term "like ... products" in Article III:2 of the GATT 1994 with respect to the products' physical characteristics. Second, we address the relevance of the raw material base in the determination of whether two products are "like" within the meaning of Article III:2. Third, we address the Philippines' claim that, by applying a "perceptible differences test", the Panel applied the wrong standard to assess the similarity of physical characteristics and thus acted inconsistently with Article III:2, first sentence, of the GATT 1994. Finally, we address the Philippines' claim that the Panel acted inconsistently with Article 11 of the DSU in its assessment of the products' physical characteristics.

Interpretation of the Term "Like Products" with Respect to the Products' Physical Characteristics

115. The Philippines claims that the Panel's statement that the concept of "like products" is not limited to "identical products" is inconsistent with the Appellate Body's narrow definition of "like products" under Article III:2, first sentence, of the GATT 1994. The Philippines argues that the test that should have been applied is whether the products are "sufficiently close" in nature that they can be deemed to fit within the narrow category of "like" within the meaning of Article III:2, as interpreted by the Appellate Body.²⁰⁴ According to the Philippines, the narrow scope of the category of "like products" means that any significant physical difference will be considered sufficient to disqualify a product from being considered "like" another product.²⁰⁵

116. The European Union and the United States disagree with the Philippines' contention that the narrow scope of the term "like products" implies that any significant physical difference will be sufficient to disqualify a product from being considered "like" another product.²⁰⁶ The European Union and the United States argue that the Philippines overstates the importance of physical characteristics, particularly the differences in chemical composition, in the analysis of "likeness" in relation to other factors.²⁰⁷

²⁰⁴Philippines' appellant's submission, para. 29 (referring to Panel Reports, para. 7.32).

²⁰⁵Philippines' appellant's submission, para. 30.

²⁰⁶European Union's appellee's submission, paras. 45 and 52; United States' appellee's submission, para. 25.

²⁰⁷European Union's appellee's submission, para. 45; United States' appellee's submission, para. 30.

110. Specifically, the Philippines challenges the Panel's findings that: (i) all distilled spirits at issue in this dispute are "like products", whether imported or domestic, and irrespective of the raw materials from which they are made; and (ii) each type of imported distilled spirit at issue in this dispute made from non-designated raw materials is "like" the same type of domestic distilled spirit made from designated raw materials.

111. We address first the Philippines' appeal of the Panel's finding that each type of imported distilled spirit at issue in this dispute made from non-designated raw materials is "like" the same type of domestic distilled spirit made from designated raw materials. In so doing, we review the Panel's findings on the specific factors it examined in its analysis of "likeness" under Article III:2, first sentence, of the GATT 1994. Second, we consider the Panel's finding that all the distilled spirits at issue in the present dispute, whether imported or domestic, and irrespective of the raw materials from which they are made, are "like products" within the meaning of Article III:2, first sentence, of the GATT 1994.²⁰¹

A. *The Panel's Finding that Each Type of Imported Distilled Spirit Made from Non-Designated Raw Materials is "Like" the Same Type of Domestic Distilled Spirit Made from Designated Raw Materials*

112. The Panel found that each of the types of imported distilled spirit at issue in this dispute made from non-designated raw materials—namely, gin, brandy, vodka, whisky, and tequila—is "like" the same type of domestic distilled spirit made from designated raw materials.²⁰² In other words, the Panel found that within each different type of distilled spirit there is "likeness", within the meaning of Article III:2 of the GATT 1994, between imported distilled spirits made from non-designated raw materials and domestic distilled spirits made from designated raw materials.

113. The Panel addressed the "likeness" requirement of Article III:2, first sentence, of the GATT 1994 by considering evidence with respect to: (i) the products' properties, nature, and quality, that is, their physical characteristics; (ii) end-uses in the Philippines; (iii) Philippine consumers' tastes and habits; (iv) tariff classification; and (v) relevant Philippine internal regulations. No claims are raised on appeal concerning the Panel's finding that all distilled spirits at issue in this dispute share the same end-uses in the Philippines, namely "thirst quenching, socialization, relaxation, pleasant intoxication".²⁰³

²⁰¹Panel Reports, para. 7.77.

²⁰²Panel Reports, para. 7.85. The Panel observed that all parties agreed that both domestic and imported rums were made from the same raw material (sugar cane) and were "like products". (*Ibid.*, para. 7.79)

²⁰³Panel Reports, para. 7.48 (quoting European Union's first written submission to the Panel, para. 64).

120. We understand that products that have very similar physical characteristics may not be "like", within the meaning of Article III:2, if their competitiveness or substitutability is low, while products that present certain physical differences may still be considered "like" if such physical differences have a limited impact on the competitive relationship between and among the products.

121. In this respect, we do not consider, as the Philippines argues, that the Panel committed an error of interpretation when it found that "likeness under the first sentence of Article III:2 is not limited to products that are identical".²¹² This statement by the Panel may provide only a partial view of what is entailed in a determination of "likeness" under Article III:2 of the GATT 1994. However, it is consistent with the notion that, while physical characteristics are one of the relevant criteria in the determination of "likeness" under Article III:2, even products that present certain differences may still be considered "like" if the nature and extent of their competitive relationship justifies such a determination.

122. For the reasons explained above, we disagree with the Philippines' arguments that the narrow scope of the category of "like products" means that any significant physical difference will necessarily be considered sufficient to disqualify a product from being considered "like" another product²¹³ and that, in this case, "the simple fact that sugar-based spirits in the Philippines are physically different from their non-sugar-based counterparts should have been viewed by the Panel as disqualifying these products from being considered physically 'like'".²¹⁴

Relevance of the Raw Material Base in the Determination of "Likeness"

123. Turning to the Panel's assessment of the physical characteristics of the distilled spirits at issue, the Philippines claims that, because of differences in chemical composition, which affect the distilled spirits' taste, flavour and aroma, distilled spirits made from designated raw materials and distilled spirits made from non-designated raw materials are not physically similar.²¹⁵ The Panel found that for each type of distilled spirit—gin, brandy, vodka, whisky, tequila and tequila-flavoured spirits—there is similarity in physical characteristics between imported distilled spirits and domestic Philippine distilled spirits, irrespective of the raw materials from which they are made.²¹⁶ The Panel emphasized the fact that the production process for each type of distilled spirit made from designated raw materials in the Philippines is designed to ensure, as far as possible, that the final Philippine

²¹²Panel Reports, para. 7.32.

²¹³Philippines' appellant's submission, para. 30.

²¹⁴Philippines' appellant's submission, para. 39.

²¹⁵Philippines' appellant's submission, para. 31.

²¹⁶Panel Reports, para. 7.80.

117. Article III:2, first sentence, of the GATT 1994 states:

The products of the territory of any Member imported into the territory of any other Member shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products.

118. The Panel recalled that, in *Japan – Alcoholic Beverages II*, the Appellate Body found that the definition of "like products" under Article III:2, first sentence, must be construed narrowly. The Panel understood this statement by the Appellate Body as meaning that likeness under the first sentence of Article III:2, while narrow, is not limited to products that are identical.²⁰⁸ The Panel reasoned that, "had this sentence intended to cover only identical products, the agreement would have used the word 'identical', instead of using the expression 'like products'" and noted that "[I]kewise the Appellate Body, in describing like products, has never indicated that the first sentence covers only identical products".²⁰⁹ In keeping with the case-by-case approach adopted by the Appellate Body in previous disputes, the Panel stated that it would consider whether the products at issue in this dispute are "like", within the meaning of Article III:2, first sentence, of the GATT 1994, by examining all relevant factors²¹⁰, including: the products' physical characteristics; their end-uses in the Philippines; Philippine consumers' tastes and habits; the tariff classification of the products; and relevant internal regulations in the Philippines.

119. While in the determination of "likeness" a panel may logically start from the physical characteristics of the products, none of the criteria that a panel considers necessarily has an overarching role in the determination of "likeness" under Article III:2 of the GATT 1994. A panel examines these criteria in order to make a determination about the nature and extent of a competitive relationship between and among the products.²¹¹

²⁰⁸Panel Reports, para. 7.32.

²⁰⁹Panel Reports, para. 7.32.

²¹⁰The 1970 Report of the Working Party on *Border Tax Adjustments* identified the following criteria for determining, on a case-by-case basis, whether a product is "similar": the product's end-uses in a given market; consumers' tastes and habits, which change from country to country; the product's properties, nature and quality. (Report of the Working Party on *Border Tax Adjustments*, BISD 18S/97, para. 18.) Subsequent panels and the Appellate Body found that other criteria, such as tariff classification, may also assist a panel in evaluating whether products are "like" within the meaning of Article III:2, first sentence, of the GATT 1994. See, GATT Panel Report, *Japan – Alcoholic Beverages I*, para. 5.6; and Appellate Body Report, *Japan – Alcoholic Beverages II*, pp. 21–22, DSR 1996:1, 97, at 114–115.

²¹¹In *EC – Asbestos* the Appellate Body found that "a determination of 'likeness' under Article III:4 is, fundamentally, a determination about the nature and extent of a competitive relationship between and among products". (Appellate Body Report, *EC – Asbestos*, para. 99)

spirit made from non-designated raw materials.²²⁰ To achieve this result, the ethyl alcohol produced from sugar cane molasses is stripped of its congeners to produce a neutral spirit. Special additives are added to the neutral spirit in order to ensure, as much as possible, that the resulting distilled spirit has the colour, odour, and taste traditionally associated with gin, brandy, vodka, whisky, or tequila.²²¹

127. The Panel, in considering consumer perceptions, noted that the names "gin", "brandy", "vodka", "whisky", "tequila" or "tequila-flavoured spirit" are used for domestic Philippine distilled spirits, even though these are made from designated raw materials, such as sugar cane. The Panel also noted that the raw material base is not mentioned on the labels of the bottles in which the domestic distilled spirits are sold. Moreover, the Panel observed that "labels of domestic Philippine distilled spirits made from the designated raw materials tend to mimic or replicate the names of products and designs of the similar imported spirits made from other raw materials".²²²

128. The Philippines claims that domestic distilled spirits made from designated raw materials and imported distilled spirits made from non-designated raw materials are not "like products". Nevertheless, every effort is made, from the production process to the sale of domestic distilled spirits made from designated raw materials, to ensure that they replicate as closely as possible the corresponding type of imported distilled spirit made from non-designated raw materials. While the Panel addressed presentation and labelling under consumers' tastes and habits, we observe that, as distilled spirits are sold in labelled bottles, their presentation and labelling are also concerned with the physical characteristics of the product and not only with the perceptions of the consumer. The fact that domestic Philippine distilled spirits made from designated raw materials closely replicate imported distilled spirits made from non-designated raw materials supports the Panel's overall finding that, within each type, these are "like products". Even where certain differences remain, domestic distilled spirits made from designated raw materials are presented to consumers so as to be indistinguishable from imported distilled spirits made from non-designated raw materials. This suggests, in our view, that even where the products are made from different raw materials and may, as a consequence, present some physical differences that are not completely eliminated in the production process, they can be in a sufficiently close competitive relationship to be considered "like products" within the meaning of Article III:2, first sentence, of the GATT 1994.

²²⁰Panel Reports, para. 7.80.

²²¹Panel Reports, para. 2.25.

²²²Panel Reports, para. 7.61.

product has similar organoleptic properties (colour, flavour and aroma) as the same type of imported distilled spirit made from non-designated raw materials.²¹⁷

124. The Panel considered that a difference in raw materials used in the production would only be relevant to the extent that it resulted in final products that are not similar. The Panel followed the approach of the panel in *Mexico – Taxes on Soft Drinks*, which had found that soft drinks and syrups sweetened with cane sugar, and soft drinks and syrups sweetened with non-cane sugar sweeteners (high-fructose corn syrup and beet sugar), are "like products" in spite of the differences in raw materials. Thus, the Panel focused on the physical characteristics of distilled spirits as final products, and not on those of the raw materials or production processes used to make the final products.²¹⁸

125. We consider that, in spite of differences in the raw materials used to make the products, if these differences do not affect the final products, these products can still be found to be "like" within the meaning of Article III:2 of the GATT 1994.²¹⁹ Article III:2, first sentence, refers to "like products", not to their raw material base. If differences in raw materials leave fundamentally unchanged the competitive relationship among the final products, the existence of these differences would not necessarily negate a finding of "likeness" under Article III:2. As we have explained above, the determination of what are "like products" under Article III:2 is not focused exclusively on the physical characteristics of the products, but is concerned with the nature and the extent of the competitive relationship between and among the products. We consider, therefore, that as long as the differences among the products, including a difference in the raw material base, leave fundamentally unchanged the competitive relationship among the final products, the existence of these differences does not prevent a finding of "likeness" if, by considering all factors, the panel is able to come to the conclusion that the competitive relationship among the products is such as to justify a finding of "likeness" under Article III:2.

126. As noted above, in finding physical similarities between the products at issue, the Panel attached particular importance to the fact that the production process for each type of distilled spirit made from designated raw materials in the Philippines is designed to ensure, as far as possible, that the final product has organoleptic properties similar to those of the same type of imported distilled

²¹⁷Panel Reports, para. 7.80.

²¹⁸Panel Reports, para. 7.37 (referring to Panel Report, *Mexico – Taxes on Soft Drinks*, para. 8.131).

²¹⁹The panel in *Japan – Alcoholic Beverages II* found that "the term 'like products' [in Article III:2] suggests that for two products to fall under this category they must share, apart from commonality of end-uses, essentially the same physical characteristics" (Panel Report, *Japan – Alcoholic Beverages II*, para. 6.22 (emphasis added)). The GATT panel in *Japan – Alcoholic Beverages I* found that the fact that vodka and shochu were made of similar raw materials was an indication of the fact that they were "like products". (GATT Panel Report, *Japan – Alcoholic Beverages I*, para. 5.7)

Application of the "Perceptible Differences Test" to Assess the Similarity of Physical Characteristics

129. The Panel found that the differences in chemical composition of distilled spirits shown by the gas chromatography results did not assist it in its "likeness" analysis because the differences in chemical composition between distilled spirits made from the same raw materials were in most cases greater than those between distilled spirits made from different raw materials. This led the Panel to conclude that differences in chemical composition did not show a distinction between distilled spirits made from designated raw materials and those made from non-designated raw materials.²²³ For each type of distilled spirit—gin, brandy, vodka, whisky, tequila and tequila-flavoured spirits—the Panel found that there was no evidence of "perceptible differences" between the physical qualities and characteristics of the imported spirit and those of the domestic Philippine spirit, nor between the physical qualities and characteristics of the spirit made from the designated raw materials and those of the spirit made from other raw materials.²²⁴

130. The Philippines argues that the Panel applied the wrong standard because it relied on a "perceptible differences test" from the perspective of the hypothetical consumer as the sole determinant of whether the products are physically different or not.²²⁵ The Philippines claims that, in a "likeness" analysis, the perception of the consumer is not related to the physical characteristics of the product, which are empirical, physical attributes. Rather, according to the Philippines, the perception of the consumer is relevant to the criterion of consumer tastes and habits. The Philippines thus contends that, having selected the wrong standard, the Panel found physical similarity between "sugar-based" and "non-sugar-based" distilled spirits in spite of "numerous physical differences" between these types of distilled spirits, such as the very different levels of certain key congeners and the use of additives in "sugar-based" distilled spirits.²²⁶

131. We observe that the criteria to establish "likeness" under Article III:2, first sentence, of the GATT 1994 are not exhaustive and are not set forth in Article III:2, nor in any other provision of the covered agreements. Rather, these criteria are tools available to panels for organizing and assessing the evidence relating to the competitive relationship between and among the products in order to establish "likeness" under Article III:2, first sentence. While distinct, these criteria are not mutually

²²³Panel Reports, para. 7.40.

²²⁴Panel Reports, paras. 7.42, 7.43, 7.45, 7.46, and 7.47.

²²⁵Philippines' appellant's submission, para. 44.

²²⁶Philippines' appellant's submission, para. 38.

exclusive.²²⁷ Certain evidence, such as that relating to the perceptibility of differences, may well fall under more than one criterion.²²⁸

132. By finding that there was no evidence of "perceptible differences" in the physical characteristics of the products, the Panel appears to have focused on how the products are perceived by users in its analysis of the products' physical characteristics. While consumer perception of products is highly relevant to the overall determination of "likeness" under Article III:2, we believe that this element may reach beyond the products' properties, nature, and qualities, which concern the objective physical characteristics of the products. Indeed, consumer perception of products may be more concerned with consumers' tastes and habits than with physical characteristics.

133. However, in light of the above, while the Panel refers to "perceptible" differences only in the context of the physical characteristics of the products, we do not consider that the Panel committed an error in its analysis of the products' physical characteristics by finding that, within each type, there is physical similarity between imported and domestic distilled spirits, irrespective of whether they are made from designated raw materials or from non-designated raw materials.²²⁹

Article 11 of the DSU

134. As noted above, the Philippines claims, in addition, that the Panel acted inconsistently with Article 11 of the DSU, because it disregarded critical portions of the Philippines' evidence and substituted its own judgement for that of the expert testimony presented by the Philippines. Specifically, the Philippines argues that the Panel acted inconsistently with Article 11 of the DSU when it found that there was no evidence that differences in organoleptic properties create a distinction between distilled spirits made from designated raw materials and distilled spirits made from non-designated raw materials, and when it found that the differences in chemical composition that do exist were not of assistance in its analysis of "likeness".²³⁰

135. Before turning to the issues raised by the Philippines on appeal, we recall that Article 11 of the DSU requires a panel to "make an objective assessment of the matter before it, including an objective assessment of the facts of the case". According to the Appellate Body, Article 11 of the DSU requires a panel to "consider all the evidence presented to it, assess its credibility, determine its

²²⁷Appellate Body Report, *EC – Asbestos*, para. 111.

²²⁸For instance, in *EC – Asbestos*, the Appellate Body considered health risks under a "physical characteristics" criterion as well as under the criterion of "consumers' tastes and habits". (Appellate Body Report, *EC – Asbestos*, paras. 114 and 120).

²²⁹Panel Reports, para. 7.75.

²³⁰Philippines' appellant's submission, paras. 140 and 141 (referring to Panel Reports, para. 7.40).

weight, and ensure that its factual findings have a proper basis in that evidence."²³¹ Within these parameters, "it is generally within the discretion of the panel to decide which evidence it chooses to utilize in making findings"²³², and a panel "is not required to discuss, in its report, each and every piece of evidence."²³³ The failure by a panel to reproduce certain material evidence in its report would not be inconsistent with Article 11 if the panel's reasoning reveals that it has nevertheless assessed the significance of this evidence.

136. Panels "are not required to accord to factual evidence of the parties the same meaning and weight as do the parties."²³⁴ In this regard, the Appellate Body will not "interfere lightly" with a panel's fact-finding authority, and will not "base a finding of inconsistency under Article 11 simply on the conclusion that [it] might have reached a different factual finding".²³⁵ Instead, for a claim under Article 11 to succeed, the Appellate Body must be satisfied that the panel has exceeded its authority as the initial trier of facts.²³⁶ As the initial trier of facts, a panel must provide "reasoned and adequate explanations and coherent reasoning"²³⁷, base its finding on a sufficient evidentiary basis²³⁸, and treat evidence with "even-handedness".²³⁹

137. The Philippines presented to the Panel gas chromatography results as well as an expert study²⁴⁰ (the "expert study") showing that "sugar-based" and "non-sugar-based" distilled spirits have distinct chemical compositions. This evidence shows, for example, that brandies and whiskies made from grape and grain respectively have generally a higher congener content than brandies and whiskies made from sugar cane molasses. The expert study also contains an expert opinion of the differences in taste and aroma that result from the differences in chemical composition.

138. We note that the differences in congener content are one of several factors the Panel examined in its assessment of the physical characteristics of the products at issue. The Panel did not consider that these chemical differences created a distinction between distilled spirits made from designated and distilled spirits made from non-designated raw materials, because even greater differences in congener content exist among distilled spirits made from non-designated raw

²³¹Appellate Body Report, *Brazil – Retreaded Tyres*, para. 185 (referring to Appellate Body Report, *EC – Hormones*, paras. 132 and 133).

²³²Appellate Body Report, *EC – Hormones*, para. 135.

²³³Appellate Body Report, *Brazil – Retreaded Tyres*, para. 202.

²³⁴Appellate Body Report, *Australia – Salmon*, para. 267.

²³⁵Appellate Body Report, *US – Wheat Gluten*, para. 151.

²³⁶Appellate Body Report, *US – Wheat Gluten*, para. 151.

²³⁷Appellate Body Report, *US – Upland Cotton (Article 21.5 – Brazil)*, footnote 618 to para. 293.

²³⁸See Appellate Body Report, *US – Carbon Steel*, para. 148.

²³⁹Appellate Body Report, *US – Upland Cotton (Article 21.5 – Brazil)*, para. 292.

²⁴⁰T. Allen, "Tasting and Congener Content Analysis of 31 Distilled Spirits" (30 September 2010) (Panel Exhibit PH-30 (BCI)).

materials.²⁴¹ The Panel thus addressed the differences in congener content among "sugar-based" and "non-sugar-based" distilled spirits, although it reached different conclusions than the expert consulted by the Philippines. In light of the above, we consider that, as the trier of facts, the Panel acted within the bounds of its discretion in attributing less weight than the Philippines did to the differences in congener content in the analysis of the physical characteristics of the products.

139. As noted above, the expert study submitted by the Philippines also maintains that the differences in congener content result in important differences in the organoleptic properties of brandies, whiskies, gins, and vodkas made from sugar cane as compared to those made from non-designated raw materials. The Panel, however, having reviewed the evidence concerning the production process of distilled spirits made from designated raw materials and the gas chromatography results, noted in paragraph 2.26 of its Reports that "there is no evidence to suggest that a non-expert consumer would be able to distinguish between imported and domestic spirits of the same type based only on the different raw materials used in their respective production". Furthermore, in paragraphs 7.39 and 7.40, having once again considered the production process of distilled spirits made from designated raw materials, and the fact that these closely replicate those made from non-designated raw materials, the Panel concluded that, in respect of colour, flavour, and aroma, there is no difference between these two categories of distilled spirits.

140. In light of the importance that the Philippines attached to the expert study on the congener content and organoleptic properties of distilled spirits, the Panel could have cited it directly and given it more prominence. However, the Panel did refer to the gas chromatography results on which the expert opinion is based.²⁴² On the basis of these gas chromatography results, and of the evidence concerning the production process of distilled spirits made from designated raw materials, the Panel reached the conclusion that there are no differences in the organoleptic properties of distilled spirits made from designated raw materials and distilled spirits made from non-designated raw materials. Therefore, we do not consider that the Panel's treatment of the expert study amounts, in the circumstances of this dispute, to disregarding or failing to engage with significant evidence that was relevant to the Philippines' case.

141. In light of the above, we conclude that the Panel did not disregard or fail to engage with the evidence submitted by the Philippines concerning congener content and organoleptic properties of distilled spirits, but that it acted within its discretion as the trier of facts in weighing the evidence. We

²⁴¹Panel Reports, para. 7.40.

²⁴²Panel Reports, para. 7.40 and footnote 399 thereto.

therefore consider that the Panel did not fail to make an objective assessment of the facts within the meaning of Article 11 of the DSU.

2. Consumers' Tastes and Habits

142. We now turn to the Philippines' challenge of the Panel's findings on consumers' tastes and habits. First, we address the Philippines' claim that the Panel erred in finding that the degree of competition or substitutability of the products at issue supported its overall finding of "likeness" under Article III:2, first sentence, of the GATT 1994. Second, we address the Philippines' claim that differences in distribution channels reflect the different consumer markets that distilled spirits made from designated raw materials and distilled spirits made from non-designated raw materials serve. Third, we address the Philippines' claim that, in its assessment of the Philippine market for distilled spirits, the Panel acted inconsistently with Article 11 of the DSU.

143. The Philippines contends that, in respect of consumers' tastes and habits, the Panel erred in finding that the degree of competition and substitutability among domestically produced "sugar-based" and imported "non-sugar-based" distilled spirits satisfies the higher standard of "likeness" under Article III:2, first sentence. The Philippines argues that the Panel acknowledged that a large proportion of consumers do not have access to high-priced "non-sugar-based" distilled spirits and that the competition and substitutability that exists between the two categories is limited to exceptional "special occasion" purchases.²⁴³

144. The European Union responds that the Philippines' distinction between high-priced imported distilled spirits and low-priced domestic distilled spirits is "incorrect", since both domestic and imported distilled spirits cover a relatively wide spectrum of prices.²⁴⁴ The United States observes that the Panel drew its conclusions on consumer tastes and habits from a variety of factual elements, including that the same outlets in the Philippines that sell imported distilled spirits also sell domestic distilled spirits, the similarity in marketing campaigns of domestic and imported distilled spirits, and the overlap in price among domestic and imported distilled spirits.²⁴⁵

145. The Panel found that the evidence submitted by the parties suggest a *significant* degree of competitiveness or substitutability for distilled spirits in the Philippine market.²⁴⁶ The Panel based

²⁴³Philippines' appellant's submission, paras. 69-70.

²⁴⁴European Union's appellee's submission, para. 68.

²⁴⁵United States' appellee's submission, para. 40 (referring to Panel Reports, paras. 2.36, 2.41, 2.42, 7.51, and 7.59).

²⁴⁶Panel Reports, para. 7.62. (emphasis added)

this finding on an analysis of two studies²⁴⁷ (the "substitutability studies") submitted by the parties regarding consumer perceptions in the Philippine distilled spirits market, and on the analysis of the Philippine market for distilled spirits.

146. The Panel considered that both substitutability studies suggest that a simultaneous increase in the price of domestic Philippine distilled spirits and decrease in the price of imported distilled spirits, such as that which would result from an equalization in the respective levels of the excise tax, could result in the substitution of the consumption of domestic distilled spirits for imported distilled spirits in the Philippine market.²⁴⁸ Regarding the Philippine distilled spirits market, the Panel noted that: (i) a large proportion of the Philippine population has a limited ability to purchase distilled spirits beyond certain price levels; (ii) there are a number of high-priced domestic Philippine distilled spirits, as well as less expensive imports; and (iii) many consumers may be able to purchase high-priced distilled spirits, at least on special occasions.²⁴⁹

147. With respect to each *type* of distilled spirit at issue, the Panel further found that manufacturers' marketing campaigns, which make no distinction between distilled spirits made from designated and non-designated raw materials, suggest a "closer similarity" than the "general similarity" it had already found between all distilled spirits relevant in the present dispute.²⁵⁰ Moreover, the Panel considered that the labels of domestic Philippine distilled spirits made from designated raw materials do not suggest to the consumer that these products are different from imported distilled spirits made from non-designated raw materials.²⁵¹

148. We observe that both the analysis of "likeness" under Article III:2, first sentence, of the GATT 1994, and the analysis of direct competitiveness and substitutability under Article III:2, second sentence, require consideration of the competitive relationship between imported and domestic products. However, "likeness" is a narrower category than "directly competitive and substitutable". Thus, the degree of competition and substitutability that is required under Article III:2, first sentence, must be higher than that under Article III:2, second sentence. On this point, we recall that, in *Canada – Periodicals*, the Appellate Body considered that a relationship of "imperfect substitutability" would still be consistent with the notion of "directly competitive or substitutable products", under the second sentence of Article III:2 of the GATT 1994, and that "[a] case of perfect

²⁴⁷*Euromonitor International* survey, *supra*, footnote 37, submitted by the European Union and the United States; and Abrenica & Ducanes, *supra*, footnote 65, submitted by the Philippines.

²⁴⁸Panel Reports, para. 7.57.

²⁴⁹Panel Reports, para. 7.59.

²⁵⁰Panel Reports, para. 7.82.

²⁵¹Panel Reports, para. 7.82.

markets they serve. The Philippines submits that local *sari-sari* stores (small local stores)²⁵⁶, which are frequented by all except the most affluent of consumers, account for approximately 85 per cent of off-premise sales of "sugar-based" spirits, but do not carry "non-sugar-based" spirits.²⁵⁷ Moreover, the Philippines argues that evidence submitted by the European Union and the United States shows that "sugar-based" spirits are sold predominantly through off-premise channels, while "non-sugar-based" spirits are sold predominantly through on-premise channels such as bars, restaurants, and hotels.²⁵⁸

152. The Panel addressed distribution channels under Article III:2, second sentence, of the GATT 1994. In that context, the Panel found that some establishments (especially *sari-sari* stores) that offer domestic Philippine distilled spirits do not carry imported distilled spirits, but that all outlets where imported distilled spirits are sold, either for consumption on-premise or off-premise, also offer domestic Philippine distilled spirits. The Panel considered this to be "an indication of similarity between the products at issue."²⁵⁹

153. *Sari-sari* stores, which represent an important distribution channel for domestic distilled spirits made from designated raw materials, do not distribute imported distilled spirits made from non-designated raw materials. However, most other on-premise and off-premise outlets carry both domestic and imported distilled spirits. In our view, the fact that domestic and imported distilled spirits in the Philippines do not share all channels of distribution does not establish that the degree of substitutability is such that they are not "like products" within the meaning of Article III:2, first sentence, of the GATT 1994. In particular, the fact that one channel of distribution is used only for domestic spirits (*sari-sari* stores) is not sufficient to establish that the products are not "like".²⁶⁰

154. In light of all the above, we do not consider that the Panel committed an error to the extent it found that the degree of competition or substitutability between imported distilled spirits of a

²⁵⁶Before the Panel, the Philippines defined "*sari-sari*" stores as "small, neighborhood, over-the-counter stores that carry basic grocery and household items". (Philippines' first written submission to the Panel, para. 253)

²⁵⁷Philippines' appellant's submission, para. 76 and footnote 77 thereto.

²⁵⁸Philippines' appellant's submission, para. 76.

²⁵⁹Panel Reports, para. 7.123.

²⁶⁰The panel in *Korea – Taxes on Alcoholic Beverages* found that "[c]onsiderable evidence of overlap in channels of distribution and points of sale ... is supportive of a finding that the identified imported and domestic products are directly competitive or substitutable". (Panel Report, *Korea – Taxes on Alcoholic Beverages*, para. 10.86) Similarly, the panel in *Chile – Alcoholic Beverages* found that "the consistent practice of putting these products on adjoining shelf space in similar outlets is one piece of evidence supporting a finding of substitutability", but that "if the products were regularly presented separately, it would be one piece of evidence that perhaps consumers did not group them together in their perceptions". (Panel Report, *Chile – Alcoholic Beverages*, paras. 7.57 and 7.59 (original emphasis))

substitutability would fall within Article III:2, first sentence".²⁵² In *Korea – Alcoholic Beverages*, the Appellate Body observed that "like products" are a subset of directly competitive or substitutable products", so that "perfectly substitutable products fall within Article III:2, first sentence", while "imperfectly substitutable products can be assessed under Article III:2, second sentence".²⁵³

149. We do not understand the statements by the Appellate Body in *Canada – Periodicals* and in *Korea – Alcoholic Beverages* to mean that *only* products that are perfectly substitutable can fall within the scope of Article III:2, first sentence. This would be too narrow an interpretation and would reduce the scope of the first sentence essentially to *identical products*. Rather, we consider that, under the first sentence, products that are close to being perfectly substitutable can be "like products", whereas products that compete to a lesser degree would fall within the scope of the second sentence.

150. The Panel found that the degree of substitutability within the *types* of distilled spirits is higher than for *all* distilled spirits, because domestic distilled spirits of a particular type made from designated raw materials are marketed, presented, and labelled so as to resemble as closely as possible imported distilled spirits of the same type made from non-designated raw materials.²⁵⁴ We have already found, in our discussion of the products' physical characteristics, that the fact that each type of domestic distilled spirit made from designated raw materials is produced and presented in a manner so as to replicate as closely as possible the same type of imported distilled spirit made from non-designated raw materials, supports the conclusion that there is a closer competitive relationship within each type of distilled spirit than there is among all distilled spirits.²⁵⁵ We consider this to be so, regardless of whether aspects of this replication process pertain to the physical characteristics of the products, or appeal to the tastes and habits of the consumers through labelling and packaging. Thus, in respect of consumers' tastes and habits, we understand the Panel to have found that the competitive relationship between each type of domestic distilled spirit made from designated raw materials and the same type of imported distilled spirit made from non-designated raw materials is that of products that are close to being perfectly substitutable.

151. The Philippines further contends that distribution channels for "sugar-based" and "non-sugar-based" spirits in the Philippine market are distinct, reflecting the different consumer

²⁵²Appellate Body Report, *Canada – Periodicals*, p. 28, DSR 1997:1, 449, at 473.

²⁵³Appellate Body Report, *Korea – Alcoholic Beverages*, para. 118. See also Appellate Body Report, *Canada – Periodicals*, p. 19, DSR 1997:1, 449, at 464–465.

²⁵⁴Panel Reports, para. 7.82.

²⁵⁵*Supra*, section V.A.1.

factual evidence of the parties the same meaning and weight as do the parties."²⁶⁷ In light of the above, it is our view that the Panel did consider and review the evidence submitted by the Philippines concerning its distilled spirits market and, in particular, evidence of the price levels of distilled spirits and the expendable income of the population. Although the Panel attributed different weight to this evidence than that advocated by the Philippines, it did so, in our view, within its discretion as the trier of facts.

3. Tariff Classification

158. We turn next to the criterion of tariff classification. First, we address the Philippines' claim that the Panel erred in finding that HS heading 2208 provides an indication of similarity between domestic distilled spirits made from designated raw materials and imported distilled spirits made from non-designated raw materials. Second, we address the Philippines' claim that the Panel acted inconsistently with Article 11 of the DSU in its assessment of the HS six-digit subheadings for brandy and whisky.

159. The Panel considered the fact that all distilled spirits at issue in this dispute, irrespective of the raw materials from which they are made, fall under HS heading 2208, as an indication of similarity.²⁶⁸ The Panel also found that the HS six-digit subheadings for gin and vodka (2208.50 and 2208.60, respectively) make no distinction between distilled spirits on the basis of the raw materials from which they are made, and that no HS six-digit subheadings exist for tequila and tequila-flavoured spirits. In contrast, the HS six-digit subheading for brandy (2208.20) "covers 'brandy' as a [S]pirit obtained by distilling grape wine or grape marc"²⁶⁹ and the HS six-digit subheading for whisky (2208.30) "covers 'Whiskies', as spirits made from a 'mash of cereal grains'".²⁷⁰ Accordingly, the Panel considered that, at the six-digit level, the HS classification did not provide "conclusive guidance".²⁷¹

160. The Philippines claims that the Panel erred in considering the fact that all distilled spirits at issue, irrespective of the raw materials from which they are made, fall under the same four-digit HS heading (2208), as an indication of similarity. The Philippines argues that the Panel's reliance on

²⁶⁷Appellate Body Report, *Australia – Salmon*, para. 267. In *US – Wheat Gluten*, the Appellate Body also stated that "in view of the distinction between the respective roles of the Appellate Body and panels ... we will not interfere lightly with the panel's exercise of its discretion". (Appellate Body Report, *US – Wheat Gluten*, para. 151).

²⁶⁸Panel Reports, para. 7.63.

²⁶⁹Panel Reports, para. 7.66.

²⁷⁰Panel Reports, para. 7.69.

²⁷¹Panel Reports, para. 7.71.

particular type, made from non-designated raw materials, and domestic distilled spirits of the same type, made from designated raw materials, supports its overall finding that these products are "like" within the meaning of Article III:2, first sentence, of the GATT 1994.

155. The Philippines claims, in addition, that, in its analysis of consumers' tastes and habits under Article III:2, first sentence²⁶¹, and of competition under the second sentence²⁶², the Panel acted inconsistently with Article 11 of the DSU. The Philippines contends that, in concluding that there was no evidence of the existence of two separate markets in the Philippines, and that some consumers from the majority market "may be able to purchase high-priced distilled spirits, at least on special occasions", the Panel disregarded critical evidence produced by the Philippines and ignored the fact that no evidence had been presented to counter that presented by the Philippines.²⁶³

156. The Philippines contends that the evidence it submitted to the Panel demonstrates that imported "non-sugar-based" spirits are priced regularly above PHP 150 per bottle and that, therefore, only 1.8 per cent of its population can afford imported distilled spirits.²⁶⁴ The European Union argued before the Panel that the group of consumers able to afford imported distilled spirits represents 15 per cent of the population, amounting to 13.7 million people.²⁶⁵ In weighing the evidence, the Panel found that "a large proportion of the Philippine population has a limited ability to purchase distilled spirits beyond certain price levels", but that the market is not divided into two segments, as there are lower-priced imported distilled spirits that compete with domestic distilled spirits, as well as high-priced domestic spirits that compete with imported distilled spirits. The Panel concluded that, "in terms of income, the population in the Philippines does not appear to be divided into two separate groups, but is rather distributed along a continuum of income brackets".²⁶⁶ In doing so, the Panel did take into account the evidence submitted by the Philippines regarding the pricing of spirits and the income levels of its population, as well as some contrasting evidence presented by the European Union and the United States. Based on that evidence, the Panel reached conclusions that differ from those of the Philippines, both under Article III:2, first sentence, and Article III:2, second sentence.

157. We have recalled, above, that a panel enjoys a margin of discretion in assessing the value of, and the weight to be ascribed to, the evidence before it, and that panels "are not required to accord to

²⁶¹Panel Reports, para. 7.59.

²⁶²Panel Reports, para. 7.119.

²⁶³Philippines' appellant's submission, para. 173 (quoting Panel Reports, paras. 7.59 and 7.119).

²⁶⁴Philippines' appellant's submission, para. 174.

²⁶⁵Panel Reports, footnote 528 to para. 7.120.

²⁶⁶Panel Reports, para. 7.59.

raw materials are "like" imported brandies and whiskies made from non-designated raw materials. Accordingly, we do not agree with the Panel's conclusion that at the six-digit level the HS classification provides no "conclusive guidance" as to the similarity of brandies and whiskies made from designated and non-designated raw materials.

164. We observe, however, that tariff classification is only one of the criteria that the Panel reviewed in its analysis of "likeness" under Article III:2 of the GATT 1994. We have already agreed with the Panel's conclusions that the criteria of products' physical characteristics and consumers' tastes and habits do support a finding that the products at issue are "like" within the meaning of Article III:2. Moreover, we recall that the Panel's finding that the end-uses of the products at issue are similar was not appealed. Thus, the fact that the Panel overlooked the significance of HS six-digit level classification for brandy and whisky does not, in our view, undermine its overall finding that the products at issue are "like". Therefore, we do not consider that this is an error that rises to the level of a failure by the Panel to comply with its duties under Article 11 of the DSU.

165. In light of the above, we do not consider that the Panel committed an error under Article 11 of the DSU, as the Philippines contends, in respect of the six-digit HS subheadings.

4. Regulatory Regimes

166. The Philippines claims that the Panel erred in considering that the regulatory regimes in force in the European Union and in the United States, which prohibit the marketing of whisky and brandy made from sugar cane molasses as "whisky" and "brandy", are "irrelevant".²⁷⁷ The Philippines contends that the domestic regulatory regimes of both complainants are useful in identifying physical differences between the products that are commonly recognized as important to that particular product's identity.

167. In our view, the fact that, in the European Union and in the United States, whisky and brandy made from sugar cane molasses cannot be marketed and sold as "brandy" and "whisky" may be an indication that consumers in those countries would perceive these products as having quite distinct physical properties. In contrast, in the Philippines, not only can domestically distilled spirits made from designated raw materials be marketed and sold as "brandy" and "whisky", but also, as we have already considered above, every effort is made in the production, marketing, and sale of brandy or whisky made from designated raw materials to ensure that they replicate as closely as possible imported brandy or whisky made from non-designated raw materials.

²⁷⁷Philippines' appellant's submission, para. 51.

the four-digit tariff heading in this case was inappropriate, because the range of products that fall under heading 2208 is very broad. This tariff heading is not sufficiently detailed to draw any particular inferences as to whether the distilled spirits at issue are "like".²⁷²

161. In *Japan – Alcoholic Beverages II*, the Appellate Body stated that tariff classification can be a helpful sign of similarity only if it is sufficiently detailed.²⁷³ We do not consider that HS heading 2208, which groups together all distilled spirits, as well as other liquors and unflavoured neutral spirits for human consumption or for industrial purposes, constitutes a tariff classification that is sufficiently detailed to provide an indication of "likeness", within types of distilled spirits, between domestic distilled spirits made from designated materials and imported distilled spirits made from non-designated materials.²⁷⁴

162. Turning to the Panel's finding in respect of the HS six-digit subheadings, the Philippines claims that the Panel failed to make an objective assessment of the matter before it, as required by Article 11 of the DSU, because it ignored significant and clear evidence regarding the tariff classification of whisky and brandy when it arrived at the conclusion that the evidence on tariff classification was inconclusive.²⁷⁵ Particularly in respect of whisky and brandy, the Panel found that the HS classification at the six-digit level, and the accompanying explanatory notes (HSENS), take into account the raw material used for the production of a particular distilled spirit, so that whisky and brandy made from sugar cane molasses would not fall under the same HS subheading as whisky and brandy made from traditional raw materials.

163. We observe that the six-digit HS subheading for brandy refers to spirits obtained by distilling grape wine or grape marc. The six-digit HS subheading for whisky contains no reference to the raw material from which this spirit is produced. However, the HSENS to the six-digit HS codes for both brandy and whisky specify the material from which the spirit is distilled, namely, grape wine or grape marc for brandy and mash of cereal grains for whisky.²⁷⁶ This, in our view, provides an indication that tariff classification would not suggest that domestic brandies and whiskies made from designated

²⁷²Philippines' appellant's submission, para. 81.

²⁷³Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 21, DSR 1996:1, 97, at 114.

²⁷⁴We observe that the HS heading 2208 refers to "undematured ethyl alcohol of an alcoholic strength by volume of less than 80%: spirits, liqueurs and other spirituous beverages". Gin, brandy, rum, vodka, whisky, tequila and tequila-flavoured spirits are all covered by HS heading 2208, but also covered are chocolate, vanilla, milk, and honey liqueurs or "crèmes" as well as unflavoured neutral spirits for human consumption or for industrial purposes of less than 80 per cent volume. (Panel Reports, paras. 2.51-2.53 (referring to, *inter alia*, the HSEN to heading 2208 (Panel Exhibit PH-46))

²⁷⁵Philippines' appellant's submission, para. 159.

²⁷⁶Panel Reports, paras. 2.51-2.53 (referring to, *inter alia*, the HSEN to heading 2208 (Panel Exhibit PH-46)).

168. The determination of "likeness" under Article III:2, first sentence, of the GATT 1994 should be made on a case-by-case basis. If two spirits are considered to be "like products" in a given market, this does not necessarily mean that they would be considered "like products" in another market. It is thus conceivable that brandy and whisky made from designated raw materials and those made from non-designated raw materials may be considered as "like products" by consumers in the Philippine market, but that they may not be considered as "like products" by consumers in another market. As we have explained above, we consider that, in order to establish whether two products are "like" within the meaning of Article III:2 of the GATT 1994, a panel needs to examine the nature and the extent of the competitive relationship between and among products, which will depend on the market where these products compete.

169. We are, therefore, of the view that the Panel did not err in considering as relevant the regulatory framework of the Philippines, rather than that of the European Union or the United States, in its analysis of the competitive relationship between each type of domestic distilled spirit made from designated raw materials and the same type of imported distilled spirit made from non-designated raw materials in the market where the products compete, that is, the Philippine market.

5. Conclusions

170. As we have explained above, the determination of "likeness" under Article III:2, first sentence, of the GATT 1994 is, fundamentally, a determination about the nature and extent of a competitive relationship between and among imported and domestic products. The Panel reviewed the products' physical characteristics, end-uses, and consumers' tastes and habits, as well as tariff classification and relevant Philippine internal regulations, and concluded that an analysis of these factors shows that each type of imported distilled spirit at issue in this dispute made from non-designated raw materials is "like" the same type of domestic distilled spirit made from designated raw materials, within the meaning of Article III:2, first sentence, of the GATT 1994.

171. We are of the view that, overall, the Panel did not commit an error in the interpretation and application of Article III:2, first sentence, of the GATT 1994. In particular, we consider that the Panel's analyses of the products' physical characteristics and of consumers' tastes and habits supports the overall conclusion that distilled spirits of a particular type made from designated raw materials and distilled spirits of the same type made from non-designated raw materials are "like products" within the meaning of Article III:2 of the GATT 1994. This finding is, in our view, further supported by the Panel's finding on end-uses, which the Philippines does not challenge on appeal. The Panel found that specific types of distilled spirits share the same end-uses, that is, "thirst quenching,

socialization, relaxation, pleasant intoxication", irrespective of the raw materials from which they are made.²⁷⁸

172. In light of the above, we uphold the Panel's finding, in paragraph 7.85 of the Panel Reports, that each type of imported distilled spirit at issue in this dispute—gin, brandy, vodka, whisky, and tequila—made from non-designated raw materials is "like" the same type of domestic distilled spirit made from designated raw materials, within the meaning of Article III:2, first sentence, of the GATT 1994.

173. Moreover, for the reasons explained above, we consider that the Panel did not act inconsistently with Article 11 of the DSU in its evaluations of the products' physical characteristics, of the Philippine market for distilled spirits, and of tariff classification.

174. As a consequence, we also uphold the Panel's finding, in paragraphs 7.90 and 8.2 of the Panel Reports, that, by imposing on each type of imported distilled spirit at issue in this dispute—gin, brandy, rum, vodka, whisky, and tequila—made from non-designated raw materials, internal taxes in excess of those applied to "like" domestic distilled spirits of the same types, made from designated raw materials, the Philippines has acted inconsistently with Article III:2, first sentence, of the GATT 1994.²⁷⁹

B. *The Panel's Finding that All Distilled Spirits at Issue in This Dispute, whether Imported or Domestic and Irrespective of Their Raw Material Base, are "Like Products"*

175. We now turn to the Panel's finding at paragraph 7.77 of its Reports that "the distilled spirits at issue in the present dispute, whether imported or domestic, and irrespective of the raw materials from which they are made, are like products within the meaning of the first sentence of Article III:2 of the GATT 1994".²⁸⁰

176. The Philippines contends that the Panel's error in assessing the products' physical characteristics also led it to make the "extraordinary" finding that all distilled spirits at issue in this dispute are "like products", such that "non-sugar-based" whiskies are "like" "sugar-based" brandies, etc.²⁸¹ The Philippines adds that these types of products are so different that the

²⁷⁸Panel Reports, para. 7.81.

²⁷⁹Panel Reports, para. 7.90, EU Panel Report, para. 8.2, and US Panel Report, para. 8.2(a).

²⁸⁰Panel Reports, para. 7.77.

²⁸¹Philippines' appellants' submission, para. 40.

complainants themselves did not claim that all "non-sugar-based" distilled spirits are "like" all "sugar-based" distilled spirits for the purposes of Article III:2 of the GATT 1994.²⁸²

177. It is not immediately clear from paragraph 7.77 of the Panel Reports, when read in isolation, whether the Panel actually concluded that *all* distilled spirits at issue in this dispute are "like products", irrespective of their raw material base and their origin or type (brandy, whisky, rum, gin, vodka, tequila, tequila-flavoured spirits), or whether it simply stated that the distilled spirits at issue in this dispute *may be* "like products", irrespective of raw material base and origin. We observe, however, that before reaching its conclusion in paragraph 7.77, the Panel stated, in the two preceding paragraphs, that *all* distilled spirits at issue in this dispute are similar in respect of physical characteristics and end-uses, and that factors such as marketing campaigns, the significant degree of competition or substitutability, tariff classification, and domestic regulations suggest similarity between *all* distilled spirits at issue in this dispute, irrespective of their raw material base and origin. Moreover, in paragraph 7.78, the Panel stated that, "in addition" to its conclusion in paragraph 7.77, it would then turn "to each type of spirit (gin, brandy, rum, vodka, whisky, tequila and tequila-flavoured spirits), in order to consider whether those spirits, imported or domestic and irrespective of the raw materials from which they are distilled, are 'like products'". These statements by the Panel may be read as suggesting that the conclusion in paragraph 7.77 was in fact that *all* distilled spirits at issue in this dispute are "like products" within the meaning of Article III:2, first sentence, of the GATT 1994.

178. In addition, we note that the Panel later stated that, under Article III:2, second sentence, it considered the issue of "direct competitiveness or substitutability" as if *arguendo* it had found that the products at issue were *not* like.²⁸³ As we consider further below, the Panel addressed, under Article III:2, second sentence, whether *all* distilled spirits at issue in this dispute are directly competitive or substitutable products on an *arguendo* basis. This suggests that, under Article III:2, first sentence, the Panel did find that *all* distilled spirits at issue in this dispute are "like products". Had this not been the case, there would have been no need for the Panel to consider *arguendo* the issue of whether *all* distilled spirits at issue are directly competitive or substitutable under Article III:2, second sentence.

179. To the extent that the Panel found, in paragraph 7.77 of its Reports, that *all* distilled spirits at issue in this dispute, regardless of the different types, are "like products" within the meaning of Article III:2, first sentence, of the GATT 1994, we disagree with this finding by the Panel.

²⁸²Philippines' appellant's submission, para. 41.

²⁸³Panel Reports, para. 7.99.

180. The Panel's own findings suggest that the degree of physical similarity and competition among *all* distilled spirits at issue in this dispute is not such as to fulfil the narrow definition of "likeness" in Article III:2, first sentence, of the GATT 1994. We observe that, in paragraph 7.40 of its Reports, the Panel stated that it had found "evidence that each of the different types of distilled spirits has specific organoleptic properties". It clearly follows from this that, in the Panel's view, all distilled spirits do not have the same organoleptic properties.²⁸⁴

181. Moreover, in respect of consumers' tastes and habits, the Panel found that the evidence suggested a *significant* degree of competitiveness or substitutability for distilled spirits in the Philippine market.²⁸⁵ To the extent that this finding by the Panel refers to *all* distilled spirits in the Philippine market, we do not consider that a *significant* degree of competitiveness or substitutability would support a finding of "likeness" under Article III:2, first sentence, of the GATT 1994. We have considered above that, based on the findings of the Appellate Body in *Canada – Periodicals*²⁸⁶ and in *Korea – Alcoholic Beverages*²⁸⁷, under Article III:2, first sentence, products that are close to being perfectly substitutable can be "like products", whereas products that compete to a lesser degree would fall within the scope of the second sentence of Article III:2. This, in our view, suggests that a finding of "likeness" under the first sentence requires a degree of competition that is higher than merely *significant*.

182. Finally, we disagree with the Panel's finding that, the fact that all distilled spirits at issue in this dispute, irrespective of the raw materials from which they are made, fall under HS heading 2208, provides an indication of similarity.²⁸⁸ We recall that, in *Japan – Alcoholic Beverages II*, the Appellate Body stated that tariff classification can be a helpful sign of similarity only if it is sufficiently detailed.²⁸⁹ As already noted above, we do not consider that HS heading 2208, which groups together all distilled spirits, as well as other liquors and unflavoured neutral spirits for human consumption or for industrial purposes, constitutes a sufficiently detailed tariff classification to support a finding that *all* distilled spirits at issue in this dispute are "like" within the meaning of Article III:2, first sentence, of the GATT 1994.

²⁸⁴For example, with respect to colour, the Panel found that all gins and all vodkas have a clear (transparent) colour, while all whiskies have a "similar golden" colour, and all brandies have a colour that "goes from golden to mahogany." (Panel Reports, paras. 2.55, 2.62, 2.75, and 2.81)

²⁸⁵Panel Reports, para. 7.62.

²⁸⁶Appellate Body Report, *Canada – Periodicals*, p. 28, DSR 1997:1, 449, at 473.

²⁸⁷Appellate Body Report, *Korea – Alcoholic Beverages*, para. 118.

²⁸⁸Panel Reports, para. 7.63.

²⁸⁹Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 21, DSR 1996:1, 97, at 114.

183. In light of the above, we do not consider that the Panel's conclusions on the products' physical characteristics, consumers' tastes and habits, and tariff classification support a finding that *all* distilled spirits at issue in this dispute are "like products" within the meaning of Article III:2, first sentence, of the GATT 1994. Therefore, to the extent that paragraph 7.77 of the Panel Reports stands for the proposition that *all* distilled spirits at issue in this dispute are "like products", regardless of types, we *reverse* this finding by the Panel.

VI. Article III:2, Second Sentence, of the GATT 1994

184. In this section, we address both the Philippines' appeal and the European Union's other appeal regarding Article III:2, second sentence, of the GATT 1994. We begin with the other appeal of the European Union.

A. *European Union's Other Appeal*

185. The European Union claims that the Panel erred in characterizing its claim under Article III:2, second sentence, of the GATT 1994 as made in the "alternative"²⁹⁰ to its claim under the first sentence of Article III:2. According to the European Union, by failing to address its claim under Article III:2, second sentence, the Panel acted inconsistently with Articles 7.1, 7.2, and 11 of the DSU.²⁹¹ Moreover, to the extent that the Panel's failure to address the European Union's claim under Article III:2, second sentence, constituted application of the principle of judicial economy, the European Union submits that the Panel exercised "false" judicial economy in violation of Articles 3.7 and 21.1 of the DSU.²⁹² The European Union requests the Appellate Body: to reverse the Panel's characterization of its claim under the second sentence of Article III:2 as "alternative" to its claim under the first sentence thereof; to complete the legal analysis; and to find that the Philippines has acted inconsistently with Article III:2, second sentence, of the GATT 1994.²⁹³

186. The Philippines does not contest the specific claim raised by the European Union in its other appeal. The Philippines essentially considers that the merits of the claim raised by the European Union in its other appeal will be fully addressed by the Appellate Body in any case, because the Philippines has appealed the finding of inconsistency made by the Panel in response to the United States' claim under Article III:2, second sentence, of the GATT 1994.²⁹⁴

²⁹⁰Panel Reports, paras. 7.1, 7.5, 7.17, 7.92, 7.93, 7.95; and EU Panel Report, para. 8.3.

²⁹¹European Union's other appellant's submission, para. 29.

²⁹²European Union's other appellant's submission, para. 35.

²⁹³European Union's other appellant's submission, para. 50.

²⁹⁴Philippines' appellee's submission, para. 3.

187. The European Union's request for the establishment of a panel describes the specific claims raised by the European Union under Article III:2 of the GATT 1994 in the following terms:

[T]he Philippines has acted inconsistently with the first sentence of Article III:2 of the GATT 1994, by making distilled spirits imported from other WTO Members, including the [European Union], subject, directly or indirectly, to internal taxes or other internal charges in excess of those applied, directly or indirectly, to like domestic products. Moreover, *separately and in combination* with the first sentence of Article III:2, by applying internal taxes or other internal charges to imported and/or domestic products in a manner contrary to the principles set forth in paragraph 1 of Article III of the GATT 1994, the Philippines has acted inconsistently with the second sentence of Article III:2 of the GATT 1994.²⁹⁵ (emphasis added)

188. We consider that the European Union's panel request clearly indicates that the European Union made separate and independent claims under the first and second sentences of Article III:2, of the GATT 1994. We further note that, in response to questioning by the Panel, the European Union specified the products at issue in each of its claims under the first and second sentences of Article III:2 and stated:

In essence, the [European Union's] main claims are as follows:

- Under Article III:2, first sentence, of the GATT [1994]:
 - (i) the EU claims that for each type of spirit (e.g. gin, vodka, whisky, rum, brandy, tequila etc.) the products distilled from the designated raw materials are "like" those distilled from the non-designated raw materials. Thus, by way of example, a whisky produced from the designated raw materials (e.g. sugar-cane) is like a whisky produced from other raw materials (e.g. malt).
- Under Article III:2, second sentence, of the GATT [1994]:
 - (i) the EU submits that all distilled spirits falling under heading HS2208 are "directly competitive and substitutable", irrespective of the raw materials they are distilled from. In other words, by way of example, the EU claims that imported gin is directly competitive and substitutable with Filipino vodka, that imported brandy is directly competitive

²⁹⁵WT/DS396/4, p. 3.

and substitutable with domestic whisky, etc.²⁹⁶ (emphasis and footnote omitted)

189. In our view, this response by the European Union demonstrates that its claims under the first and second sentences of Article III:2 were not only separate and independent, but also involved *distinct product groupings*. Before the Panel, the European Union claimed that the Philippines had acted inconsistently with Article III:2, *first sentence*, of the GATT 1994 by applying to *each type* of imported distilled spirit made from non-designated raw materials (gin, brandy, rum, whisky, vodka, tequila) internal taxes in excess of those applied to "like" domestic distilled spirits of the same type made from designated raw materials. In addition, the European Union claimed that the Philippines had acted inconsistently with Article III:2, *second sentence*, of the GATT 1994 by applying dissimilar taxes to *all* imported distilled spirits at issue made from non-designated raw materials and to *all* "directly competitive or substitutable" domestic distilled spirits made from designated raw materials, so as to afford protection to domestic production.²⁹⁷

190. The Panel's incorrect characterization of the European Union's claim under the second sentence of Article III:2 may stem, in part, from the European Union's statement in its first written submission that, "if the Panel were to establish that the Philippines violates Article III:2, first sentence, it would not necessarily need to analyse a breach of the second sentence of the same provision: such a breach would inevitably be covered."²⁹⁸ This statement is legally incorrect, because the second sentence of Article III:2 requires the European Union to establish *separately*: (i) that imported and domestic distilled spirits are "directly competitive or substitutable"; (ii) that such directly competitive or substitutable products are "not similarly taxed"; and (iii) that dissimilar taxation of the directly competitive or substitutable products is applied "so as to afford protection to domestic production".²⁹⁹ Moreover, because the European Union's claims under the first and second sentences of Article III:2 involved distinct product groupings, a finding that *each type* of

²⁹⁶European Union's response to Panel Question 18, para. 11. The European Union did "not take a definitive position on 'likeness' between different types of spirits ... [and] does not exclude that two or more different types of spirits could be held 'like.'" Yet, the European Union did not consider it necessary for the Panel to engage in such analysis, because it would be "long and complex". (*Ibid.*)

²⁹⁷The European Union also made a "subordinate claim" that each type of imported and domestic distilled spirit (gin, brandy, rum, whisky, vodka, tequila) were "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the GATT 1994. (European Union's response to Panel Question 18, para. 12)

Having found that *all* the distilled spirits at issue, whether imported or domestic, and irrespective of the raw material from which they are made, are "directly competitive or substitutable" under Article III:2, second sentence, of the GATT 1994, the Panel did not address the European Union's "subordinate claim" (Panel Reports, para. 7.138), and its failure to do so has not been appealed by the European Union.

²⁹⁸European Union's first written submission to the Panel, para. 52. (footnote omitted)

²⁹⁹See Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 24, DSR 1996:1, 97 at 116. (emphasis omitted)

imported distilled spirit (gin, brandy, rum, whisky, vodka, tequila) is "like" the same type of domestic distilled spirit under the first sentence does not establish, without more, that *all* the imported and domestic distilled spirits at issue are "directly competitive or substitutable" under the second sentence of Article III:2 of the GATT 1994.

191. Thus, we consider that the European Union's claim under the second sentence of Article III:2 could not have been properly understood as having been made in the "alternative", that is, to be addressed only if the Panel were to reject the European Union's claim under the first sentence of that provision.³⁰⁰ Accordingly, we *reverse* the Panel's findings, in paragraphs 7.1, 7.5, 7.17, 7.92, 7.93, 7.95, and 8.3 of the EU Panel Report, that the European Union's claim under Article III:2, second sentence, of the GATT 1994 was made in the "alternative" to its claim under the first sentence of that provision.

192. Having erroneously concluded that the European Union's claim under Article III:2, second sentence, was made in the "alternative", the Panel examined the consistency of the Philippines' excise tax with the second sentence of Article III:2 *only* with respect to the United States' claim under that provision, though it took into account "all the arguments and evidence on record, including those submitted by the European Union and third parties".³⁰¹ In failing to examine the *European Union's* claim under Article III:2, second sentence, the Panel failed to conduct an objective assessment of the matter before it, as required by Article 11 of the DSU, in relation to that specific claim of the European Union. Moreover, the Panel found that the Philippines had acted inconsistently with the second sentence of Article III:2, and made recommendations that the Philippines bring itself into conformity with its obligations under that provision, only in its Report addressing the complaint by the United States (DS403).³⁰² In erroneously abstaining from making findings under Article III:2, second sentence, and in failing to make recommendations that the Philippines bring itself into conformity with that provision in its Report addressing the complaint by the European Union (DS396), the Panel failed to "make such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the covered agreements" in the dispute in DS396, as required under Article 11 of the DSU.³⁰³ For these reasons, we *find* that the Panel acted inconsistently with its obligations under Article 11 of the DSU, in paragraph 8.3 of the EU Panel

³⁰⁰Without prejudice to the European Union's right under Article 17.6 of the DSU to appeal any issues of law covered in the Panel Reports and legal interpretations developed by the Panel, we consider that this matter could have been raised at the interim review stage of the panel proceedings.

³⁰¹Panel Reports, para. 7.95.

³⁰²US Panel Report, paras. 8.2(b) and 8.4.

³⁰³EU Panel Report, para. 8.3.

Report, in failing to examine, and in abstaining from making findings in relation to, the European Union's separate and independent claim under Article III:2, second sentence, of the GATT 1994.

193. We must now determine whether there are "sufficient factual findings in the panel report or undisputed facts in the panel record"³⁰⁴ to enable us to complete the legal analysis in relation to the European Union's separate and independent claim under Article III:2, second sentence, of the GATT 1994. We note here and discuss below that the findings made by the Panel under Article III:2, second sentence, of the GATT 1994 provide a sufficient basis for us to complete the legal analysis in relation to the European Union's claim under that provision.³⁰⁵

B. *Philippines' Appeal*

194. We examine next the issues raised in the Philippines' appeal regarding the Panel's findings under Article III:2, second sentence, of the GATT 1994, which contains a general prohibition against "internal taxes or other internal charges" applied to "imported or domestic products in a manner contrary to the principles set forth in paragraph 1". Article III:1 of the GATT 1994, in turn, provides that internal taxes and other internal charges "should not be applied to imported or domestic products so as to afford protection to domestic production". The *Ad Note* to Article III:2 clarifies the conditions under which a measure conforming to the first sentence of Article III:2 will be nonetheless inconsistent with the second sentence of that provision as follows:

A tax conforming to the requirements of the first sentence of paragraph 2 would be considered to be inconsistent with the provisions of the second sentence only in cases where competition was involved between, on the one hand, the taxed product and, on the other hand, a directly competitive or substitutable product which was not similarly taxed.

195. As noted earlier, the Appellate Body has explained that three separate issues must be addressed when assessing the consistency of an internal tax measure with Article III:2, second sentence, of the GATT 1994. First, whether the imported and domestic products are "*directly competitive or substitutable*"; second, whether such directly competitive or substitutable imported and domestic products are "*not similarly taxed*"; and third, whether dissimilar taxation of the directly

competitive or substitutable imported products is "*applied ... so as to afford protection to domestic production*".³⁰⁶

196. The Philippines appeals the Panel's assessment of two elements of the three-part test of Article III:2, second sentence, of the GATT 1994. First, the Philippines claims that the Panel erred in finding that all distilled spirits at issue in this dispute, whether imported or domestic, and irrespective of the raw material from which they are made, are "directly competitive or substitutable" products within the meaning of Article III:2, second sentence.³⁰⁷ Second, the Philippines claims that the Panel erred in finding that dissimilar taxation of the imported and domestic distilled spirits at issue is applied "so as to afford protection" to Philippine production of distilled spirits under Article III:2, second sentence.³⁰⁸ The Philippines does *not* appeal the Panel's finding that imported distilled spirits made from non-designated raw materials and directly competitive or substitutable domestic distilled spirits made from designated raw materials are not "similarly taxed" within the meaning of Article III:2, second sentence, of the GATT 1994.³⁰⁹

I. Directly Competitive or Substitutable Products

197. In examining whether the imported and domestic distilled spirits at issue are "directly competitive or substitutable" in the Philippine market, the Panel initially noted that the substitutability studies submitted by the parties suggest "a significant degree of competitiveness or substitutability" in the Philippines between the distilled spirits at issue.³¹⁰ The Panel then rejected the Philippines' argument that the price gap between imported and domestic distilled spirits, combined with the income disparity in the Philippines, demonstrates the existence of two distinct segments in the Philippine distilled spirits market. The Panel reasoned that the overlap in prices both for high- and low-priced brands of imported and domestic distilled spirits suggests that the Philippine market is not segmented.³¹¹ Moreover, in terms of purchasing power, many Filipino consumers "may be able to purchase high-priced distilled spirits, at least on special occasions".³¹² The Panel added that the Philippines' argument concerning market segmentation implies that "at least a narrow segment of the market has access to both groups of spirits".³¹³ For the Panel, such instances of actual competition

³⁰⁶Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 24, DSR 1996:1, 97, at 116. (original emphasis)

³⁰⁷Panel Reports, para. 7.138.

³⁰⁸Panel Reports, para. 7.187.

³⁰⁹Panel Reports, para. 7.167.

³¹⁰Panel Reports, para. 7.113 (referring to *Euromonitor International* survey, *supra*, footnote 37, and Abrenica & Ducanes, *supra*, footnote 65).

³¹¹Panel Reports, para. 7.118.

³¹²Panel Reports, para. 7.119.

³¹³Panel Reports, para. 7.120.

³⁰⁴Appellate Body Report, *US – Section 211 Appropriations Act*, para. 343 (referring to Appellate Body Report, *Australia – Salmon*, para. 118).

³⁰⁵Panel Reports, paras. 7.95-7.188.

indicate that imported and domestic distilled spirits are "capable of being directly competitive or substitutable in the future".³¹⁴

198. On this basis, the Panel concluded that there is "a direct competitive relationship" between domestic and imported distilled spirits made from different raw materials in the Philippine market.³¹⁵ This factor, combined with other similarities in terms of channels of distribution³¹⁶, the products' physical characteristics³¹⁷, end-uses and marketing³¹⁸, tariff classification³¹⁹, and internal regulations³²⁰ suggest that the imported and domestic distilled spirits at issue, irrespective of the raw materials from which they are made, are "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the GATT 1994.³²¹

199. On appeal, the Philippines challenges the Panel's assessment of the *competitive relationship* between imported and domestic distilled spirits in the Philippine market. The Philippines does *not* challenge the other factors taken into account by the Panel in its determination that imported and domestic distilled spirits are "directly competitive or substitutable", such as similarity in channels of distribution, physical characteristics, end-uses and marketing, tariff classification, and internal regulations.³²²

200. The Philippines claims that the Panel made in essence three errors in its assessment of the competitive relationship between imported and domestic distilled spirits in the Philippine market. First, the Philippines argues that the Panel insufficiently addressed the "degree of competition" between imported and domestic distilled spirits in the Philippine market. Second, the Philippines maintains that the Panel erroneously found direct competition or substitutability between imported and domestic spirits on the basis of a "non-representative" segment of the Philippine market having "access" to distilled spirits "at least on special occasions". Third, the Philippines posits that the Panel incorrectly held that there is potential competition between imported and domestic distilled spirits in the Philippines. In addition, the Philippines argues that the Panel acted inconsistently with its duties under Article 11 of the DSU in its assessment of the two studies that purported to evaluate the degree

³¹⁴Panel Reports, para. 7.121. (original emphasis)

³¹⁵Panel Reports, para. 7.137.

³¹⁶Panel Reports, para. 7.123.

³¹⁷Panel Reports, para. 7.127.

³¹⁸Panel Reports, paras. 7.129 and 7.131.

³¹⁹Panel Reports, paras. 7.133 and 7.134.

³²⁰Panel Reports, para. 7.135.

³²¹Panel Reports, para. 7.138.

³²²Panel Reports, paras. 7.122-7.135.

of substitutability between domestic and imported distilled spirits in the Philippine market. We address each of these arguments in turn.

(a) "Degree" of Competition

201. The Philippines argues that the Panel applied an incorrect standard in finding that the analysis under the second sentence of Article III:2 of the GATT 1994 should focus on the "nature" and "quality" of competition, but not on the "degree of competition" between domestic and imported distilled spirits in the Philippines.³²³ Referring to the Appellate Body reports in *Korea – Alcoholic Beverages* and *US – Cotton Yarn*, the Philippines stresses that the degree of competition between imported and domestic products is the "central" inquiry under Article III:2, second sentence.³²⁴ According to the Philippines, had the Panel applied the correct standard, it would have come to the conclusion that there is "insufficient proximity" in the degree of competition between the products at issue to permit their characterization as "directly competitive or substitutable".³²⁵

202. Both the European Union and the United States respond that the Panel correctly focused its analysis on the degree of competition between imported and domestic distilled spirits in the Philippine market. For the European Union, the Philippines' argument is "purely terminological".³²⁶ In stating that the issue was "not so much" the degree of competition, the Panel simply rejected the Philippines' argument that Article III:2, second sentence, requires "complete, absolute or exact" substitutability.³²⁷ For the United States, the Philippines seeks to minimize the significance of other types of evidence upon which the Panel relied, such as the lack of differentiation between imported and domestic distilled spirits in labelling and marketing.³²⁸ Moreover, the Panel's conclusion that there is a "significant degree of competitiveness or substitutability" between domestic and imported distilled spirits in the Philippine market disproves the Philippines' argument that the Panel did not evaluate the "degree of proximity" of competition.³²⁹

³²³Philippines' appellant's submission, para. 88.

³²⁴Philippines' appellant's submission, paras. 90 and 91 (referring to Appellate Body Report, *Korea – Alcoholic Beverages*, paras. 129, 130, 133, and 134; and Appellate Body Report, *US – Cotton Yarn*, paras. 97 and 98).

³²⁵Philippines' appellant's submission, para. 95.

³²⁶European Union's appellee's submission, para. 83.

³²⁷European Union's appellee's submission, para. 84. (emphasis omitted)

³²⁸United States' appellee's submission, para. 66 (referring to Panel Reports, para. 7.131).

³²⁹United States' appellee's submission, para. 69 (quoting Panel Reports, para. 7.113 (emphasis omitted)).

where the imported and domestic products are "interchangeable" or offer "alternative ways of satisfying a particular need or taste".³³⁵

206. Moreover, in applying the standard it articulated to the facts before it, the Panel reviewed the substitutability studies³³⁶, which purport to evaluate the degree of substitutability between imported and domestic distilled spirits in the Philippine market. The Panel found that the substitutability studies indicate that there is "a significant degree of competitiveness or substitutability" in the Philippine market between the imported and domestic distilled spirits at issue.³³⁷ For the Panel, these studies, combined with instances of price competition for both high- and low-priced brands of imported and domestic distilled spirits³³⁸, potential for consumption of high-priced spirits on "special occasions"³³⁹, instances of actual competition in a narrow segment of the Philippine consumer market³⁴⁰, and potential competition between imported and domestic distilled spirits in the Philippine market³⁴¹ sufficiently demonstrate that there is "a direct competitive relationship between domestic and imported distilled spirits" in the Philippines.³⁴² For the Panel, such a direct competitive relationship, combined with similarities between imported and domestic distilled spirits in terms of their properties, nature and quality³⁴³, end-uses and marketing³⁴⁴, tariff classification³⁴⁵, and domestic Philippine regulation of distilled spirits³⁴⁶ sufficiently evidences that these products are "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the GATT 1994.³⁴⁷

207. In our view, the Panel's analysis sufficiently demonstrates that it appropriately assessed the degree of competition between imported and domestic distilled spirits in the Philippine market. We note, in this respect, that the Panel expressly derived, from its statement that the "question before us ... is not so much what the 'degree of competition' between the products at issue is, but what is the 'nature' or 'quality' of their 'competitive relationship'"³⁴⁸, the conclusion that it "should not place too

³³⁵ Appellate Body Report, *Korea – Alcoholic Beverages*, para. 115.

³³⁶ *Euromonitor International survey, supra*, footnote 37; Abrenica & Ducanes, *supra*, footnote 65.

³³⁷ Panel Reports, para. 7.113 (referring to *Euromonitor International survey, supra*, footnote 37, p. 19; and Abrenica & Ducanes, *supra*, footnote 65). (emphasis added)

³³⁸ Panel Reports, para. 7.118.

³³⁹ Panel Reports, para. 7.119.

³⁴⁰ Panel Reports, para. 7.120.

³⁴¹ Panel Reports, para. 7.121.

³⁴² Panel Reports, para. 7.127.

³⁴³ Panel Reports, para. 7.127.

³⁴⁴ Panel Reports, para. 7.131.

³⁴⁵ Panel Reports, paras. 7.133 and 7.134.

³⁴⁶ Panel Reports, para. 7.135.

³⁴⁷ Panel Reports, para. 7.137.

³⁴⁸ Panel Reports, para. 7.101 (quoting Appellate Body Report, *Korea – Alcoholic Beverages*, paras. 128-134).

203. The Philippines' allegation of error is directed at the following statement by the Panel:

The question before us under Article III of the GATT 1994 is not so much what the "degree of competition" between the products at issue is, but what is the "nature" or "quality" of their "competitive relationship".³³⁰

204. Although the statement challenged by the Philippines, read in isolation, could be viewed as de-emphasizing the role played by this particular factor in the Panel's assessment, a careful review of the Panel's analysis indicates that the Panel appropriately ascertained the extent of the competitive relationship between imported and domestic distilled spirits in the Philippine market. At the outset of its analysis, the Panel articulated the standard that it would apply to determine whether the products at issue were "directly competitive or substitutable" in the following terms:

We start by looking at the direct competitive relationship between the relevant products, i.e. the extent to which consumers are willing to use the different products to satisfy the same, or similar, needs ("consumers' tastes and habits"). We will focus our analysis on how those products relate to each other in the market. Although at some level all products may be said to be "at least indirectly competitive," given that consumers have limited disposable income for competing needs, the second sentence of Article III:2 only regulates situations where products compete directly.³³¹ (footnote omitted)

205. We consider that the standard articulated by the Panel appropriately framed the analysis as one aimed at determining whether competition between imported and domestic distilled spirits in the Philippines is *sufficiently direct* so that these products could be properly characterized as "directly competitive or substitutable". In so doing, the Panel followed the guidance provided by the Appellate Body in *Korea – Alcoholic Beverages*, in which the Appellate Body held that imported and domestic products are "directly competitive or substitutable" when they are "in competition" in the marketplace.³³² The Appellate Body held further that the term "directly" suggests "a degree of proximity in the competitive relationship between the domestic and the imported products."³³³ The requisite degree of competition is met where the imported and domestic products are characterized by a high, but imperfect, degree of substitutability.³³⁴ As the Appellate Body found, this will be the case

³³⁰ Panel Reports, para. 7.101.

³³¹ Panel Reports, para. 7.104.

³³² Appellate Body Report, *Korea – Alcoholic Beverages*, para. 114.

³³³ Appellate Body Report, *Korea – Alcoholic Beverages*, para. 116.

³³⁴ Appellate Body Report, *Korea – Alcoholic Beverages*, para. 118; Appellate Body Report, *Canada – Periodicals*, p. 28, DSR 1997:1, 449, at 473. See also Appellate Body Report, *US – Cotton Yarn*, footnote 68 to para. 97.

much emphasis on quantitative analyses".³⁴⁹ Thus, the Panels reference to the "degree of competition" in the statement challenged by the Philippines related exclusively to a *quantitative* assessment of the competitive relationship between domestic and imported distilled spirits in the marketplace. In de-emphasizing the role played by quantitative analyses of substitutability, the Panel followed the guidance provided by the Appellate Body in previous cases. In *Korea – Alcoholic Beverages*, the Appellate Body expressly found that a particular degree of competition need not be shown in quantitative terms³⁵⁰, and cautioned panels against placing undue reliance on "quantitative analyses of the competitive relationship", because cross-price elasticity is not "the decisive criterion" in determining whether two products are directly competitive or substitutable.³⁵¹

208. For these reasons, we do not agree with the Philippines that the Panel insufficiently assessed the degree of competition between domestic and imported distilled spirits in the Philippine marketplace. Rather, the Panel appropriately sought to determine the degree or extent to which domestic and imported distilled spirits are in direct competition in the Philippine market.

(b) Market Segmentation

209. The second set of issues raised by the Philippines' appeal of the Panel's assessment of competition relates to the Panel's rejection of its argument that imported and domestic distilled spirits are not "directly competitive or substitutable" in the Philippines because they are sold in two separate and distinct market segments.

210. Before the Panel, the Philippines argued that there is a "huge gap" in its market between the prices of "sugar-based" and "non-sugar-based" distilled spirits. Such a general gap in prices, compounded by the income disparity in the Philippine market, prevents most consumers in the Philippines from purchasing "non-sugar-based" distilled spirits, thus suggesting the existence of two market segments: one for domestic, low-priced distilled spirits made from designated raw materials, and another for imported, high-priced distilled spirits made from non-designated raw materials.³⁵²

211. Although the Panel recognized that the prices of imported brands of distilled spirits, even before taxes, tend to be higher than the corresponding domestic brands of distilled spirits, the Panel considered that the evidence shows overlap in the prices of imported and domestic distilled spirits

³⁴⁹Panel Reports, para. 7.105. (emphasis added)

³⁵⁰Appellate Body Report, *Korea – Alcoholic Beverages*, paras. 130 and 131.

³⁵¹Appellate Body Report, *Korea – Alcoholic Beverages*, para. 134. (emphasis omitted)

³⁵²Panel Reports, para. 7.114.

which is "not exceptional" and occurs for both high- and low-priced products.³⁵³ For the Panel, such price overlaps suggest that the Philippine market is not segmented, and that in some cases there is price competition between imported and domestic products.³⁵⁴

212. With regard to the purchasing power of Philippine consumers, the Panel found that, while "a large proportion" of Philippine consumers may not have access to high-priced distilled spirits, "many others may be able to purchase high-priced distilled spirits, at least on special occasions."³⁵⁵ Moreover, for the Panel, the Philippines' argument that distilled spirits made from non-designated raw materials are only available to a "narrow segment" of the population implies that at least that segment of the market has access to both groups of spirits.³⁵⁶ This was sufficient for the Panel to find a direct competitive relationship between imported and domestic distilled spirits in the Philippines because:

Article III of GATT 1994 does not protect just *some* instances or *most* instances, but rather, it protects *all* instances of direct competition. It follows that the competitive relationship does not need to occur throughout the *whole* market for a panel to find that a measure is inconsistent with the second sentence of Article III. We thus conclude that, even if the Philippine distilled spirits market were segmented, actual direct competition exists within at least a segment of that market.³⁵⁷ (original emphasis; footnote omitted)

213. On appeal, the Philippines argues that these findings do not provide a sufficient basis for the Panel to conclude that imported distilled spirits made from non-designated raw materials and domestic distilled spirits made from designated raw materials are "directly competitive or substitutable" in the Philippine market. The Philippines essentially argues that the Panel erred in finding direct competition on the basis of a "non-representative" segment of its population having "access" to both types of spirits "at least on special occasions".

214. Both the European Union and the United States argue that the Panel correctly rejected the Philippines' argument that its distilled spirits market is divided into two distinct segments on the basis of evidence suggesting instances of price overlap between imported and domestic distilled spirits, and of evidence suggesting that, in terms of income, the Philippine population is distributed along a "continuum of income brackets".³⁵⁸

³⁵³Panel Reports, para. 7.118.

³⁵⁴Panel Reports, para. 7.118.

³⁵⁵Panel Reports, para. 7.119.

³⁵⁶Panel Reports, para. 7.120.

³⁵⁷Panel Reports, para. 7.120.

³⁵⁸European Union's appellee's submission, para. 96; United States' appellee's submission, para. 88 (referring to Panel Reports, para. 7.59).

215. At the outset, we note that the Panel rejected the Philippines' argument that imported and domestic distilled spirits are in two distinct market segments in the Philippines primarily on the basis of evidence demonstrating overlaps in the *prices* of imported and domestic distilled spirits, both for high- and low-priced products.³⁵⁹ We consider that price is very relevant in assessing whether imported and domestic products stand in a sufficiently direct competitive relationship in a given market. This is because evidence of price competition indicates that the imported product exercises competitive constraints on the domestic product, and *vice versa*. In this respect, we agree with the Philippines that evidence of major price differentials could demonstrate that the imported and domestic products are in completely separate markets. However, in this case, the Panel made a factual finding that there is overlap in the prices of imported and domestic distilled spirits in the Philippines, and that such overlap is not "exceptional" but rather occurs for both high- and low-priced products.³⁶⁰ The Philippines does not challenge this factual finding on appeal, but rather argues that existing price overlaps do not show a sufficiently direct degree of competition. In our view, such instances of price overlap both for high- and low-priced distilled spirits sufficiently support the Panel's conclusion that "the market is not segmented and that in some cases imported and domestic products compete with respect to price."³⁶¹

216. Turning to the purchasing power of the Filipino population, the Panel found that, "in terms of income, the population in the Philippines does not appear to be divided into two separate groups, but is rather distributed along a continuum of income brackets."³⁶² For the Panel, this suggested that, even though a "large proportion" of Philippine consumers do not have "access" to high-priced distilled spirits, many others "may be able to purchase high-priced distilled spirits, at least on special occasions."³⁶³

217. The Philippines argues that the Panel's reference to "special occasion" purchases was in error, because the term "directly competitive or substitutable" products in Article III:2, second sentence, requires identity in the "nature and frequency"³⁶⁴ of the consumers' purchasing behaviour. According to the Philippines, "[i]f a proposed alternative cannot be purchased with the same frequency as the

³⁵⁹Panel Reports, para. 7.118.

³⁶⁰Panel Reports, para. 7.118.

³⁶¹Panel Reports, para. 7.118. See, for example, Panel Reports, paras. 2.66, 2.67, 2.72, and 2.73.

³⁶²Panel Reports, para. 7.59.

³⁶³Panel Reports, para. 7.119.

³⁶⁴Philippines' appellant's submission, para. 97.

original product and is not purchased according to the same set of needs and wants, the products cannot be considered to be 'directly' competitive."³⁶⁵

218. We do not agree with the Philippines that Article III:2, second sentence, of the GATT 1994 requires *identity* in the "nature and frequency" of the consumer's purchasing behaviour. If that were the case, the competitive relationship between the imported and domestic products in a given market would only be assessed with reference to *current* consumer preferences. However, as the Appellate Body expressly held in *Korea – Alcoholic Beverages*, "the requisite relationship *may* exist between products that are not, at a given moment, considered by consumers to be substitutes but which are, nonetheless, *capable* of being substituted for one another."³⁶⁶ Therefore, requiring identity in frequency and nature of consumers' purchase decisions, as suggested by the Philippines, would not sufficiently account for *latent* demand for imported distilled spirits in the Philippine market.

219. Moreover, in determining whether imported and domestic distilled spirits offer "alternative ways of satisfying a particular need or taste"³⁶⁷ in the Philippines, the Panel was required to examine both "latent and *extant* demand"³⁶⁸ for imported distilled spirits in the Philippine market. Viewed in this light, we read the Panel's statement that many consumers may be able to purchase high-priced distilled spirits "at least on special occasions" merely as providing additional support to its conclusion that there is at least some extant demand for imported distilled spirits in the Philippine market.

220. Moreover, the Philippines argues that the Panel incorrectly found direct competition on the basis of a "narrow segment" of the population having "access" to imported distilled spirits. We are not persuaded. To begin with, we note that the Panel did not accept that the Philippine market is divided into two distinct segments in terms of purchasing power, but rather, is distributed "along a continuum of income brackets".³⁶⁹ In the passage challenged by the Philippines, the Panel engaged with the Philippines' argument concerning segmentation in the Philippines' distilled spirits market simply on an *arguendo* basis. It reasoned that, even assuming that the Philippine market were segmented, at least one segment of the market has "access" to both domestic and imported distilled spirits.³⁷⁰ In our view, it was reasonable for the Panel to draw, from the Philippines' argument that imported distilled spirits are only available to a "narrow segment" of its population, the inference that there is actual competition between imported and domestic distilled spirits at least in the segment of

³⁶⁵Philippines' appellant's submission, para. 99.

³⁶⁶Appellate Body Report, *Korea – Alcoholic Beverages*, para. 114. (original emphasis)

³⁶⁷Appellate Body Report, *Korea – Alcoholic Beverages*, para. 115.

³⁶⁸Appellate Body Report, *Korea – Alcoholic Beverages*, para. 116. (emphasis added)

³⁶⁹Panel Reports, para. 7.59.

³⁷⁰Panel Reports, para. 7.120.

price competition³⁷⁷, provide support for its finding that there is "a direct competitive relationship between domestic and imported distilled spirits" in the Philippines.³⁷⁸

(c) Potential Competition

223. The Philippines further claims that the Panel erred in its application of Article III:2, second sentence, of the GATT 1994 in finding that instances of actual competition indicated *potential* competition between imported and domestic distilled spirits in the Philippine market. The Philippines argues that "aberrational and exceptional" instances of price overlap between imported and domestic distilled spirits fall short of establishing both actual and potential competition in the marketplace.³⁷⁹ The Philippines adds that the inquiry into *potential* competition is limited to determining "whether competition would otherwise occur if the measures were not in place".³⁸⁰ The "massive [pre-tax] price differential" between domestic and imported distilled spirits demonstrates that the lack of direct competition or substitution in the Philippine market cannot be attributed to the excise tax at issue.³⁸¹ Furthermore, the Philippines maintains that the Panel acted inconsistently with Article 11 of the DSU in finding that the products at issue are capable of competing in the future without a sufficient evidentiary basis.³⁸²

224. Both the European Union and the United States respond that the Panel correctly concluded that there is potential competition between domestic and imported distilled spirits in the Philippine market. The European Union emphasizes that the Philippines does not challenge the Panel's factual finding that price overlap is not "exceptional".³⁸³ For its part, the United States argues that direct competition under Article III:2 does not require "some minimum threshold amount of actual competition"³⁸⁴, because two products may be "directly competitive or substitutable" even if direct competition is only potential and is not occurring at the present time.³⁸⁵ Both the European Union and the United States also argue that the Panel did not exceed its discretion under Article 11 of the DSU in reaching its findings concerning potential competition.

225. The Philippines' challenge is directed at the following statement by the Panel:

³⁷⁷Panel Reports, para. 7.118.
³⁷⁸Panel Reports, para. 7.137.
³⁷⁹Philippines' appellant's submission, paras. 109 and 110.
³⁸⁰Philippines' appellant's submission, para. 111.
³⁸¹Philippines' appellant's submission, para. 112.
³⁸²Philippines' appellant's submission, paras. 185 and 186.
³⁸³European Union's appellee's submission, para. 107.
³⁸⁴United States' appellee's submission, para. 83.
³⁸⁵United States' appellee's submission, para. 84.

the market that the Philippines admitted has access to both imported and domestic distilled spirits. Moreover, we note that the Panel buttressed this conclusion with statements from domestic Philippine companies that their products face competition from imported distilled spirits, and that their marketing strategies convey an image of their products as drinks that compete with imported distilled spirits.³⁷¹

221. More importantly, we do not agree with the Philippines that Article III:2, second sentence, requires that competition be assessed in relation to the market segment that is most representative of the "market as a whole".³⁷² To the contrary, the Panel was correct in concluding that Article III of the GATT 1994 "does not protect just *some* instances or *most* instances, but rather, it protects *all* instances of direct competition."³⁷³ This reading is consistent with the Appellate Body's finding that the object and purpose of the GATT 1994, as reflected in Article III, is "requiring equality of competitive relationships and protecting expectations of equal competitive relationships".³⁷⁴ Moreover, current demand for imported spirits in the Philippine market is a function of actual retail prices, which could be distorted by the excise tax system and other related effects, such as higher distribution costs, and lower volumes and economies of scale.³⁷⁵ In this regard, we recall that under the excise tax system imported distilled spirits are subject to taxes that are 10 to 40 times higher than those applied to domestic distilled spirits. Therefore, current consumer demand for imported distilled spirits in the Philippines is likely to be *understated* by the effects of the excise tax system.

222. For these reasons, it was reasonable for the Panel to conclude that actual competition in a segment of the market further supports its conclusion that imported and domestic distilled spirits are capable of being substituted in the Philippines. This inference, together with other quantitative and qualitative elements relied on by the Panel, such as the substitutability studies³⁷⁶ and instances of

³⁷¹Panel Reports, footnote 528 to para. 7.120 (referring to European Union's first written submission to the Panel, paras. 127-136; and Panel Exhibits EU-22, EU-25, EU-29, EU-43, EU-58, EU-59, EU-60, EU-63, EU-64, EU-65, and EU-87). These exhibits essentially consist of printouts of Philippine distilled spirit producers' websites, Philippine distilled spirits' press advertisements, and excerpts from Philippine distilled spirit producers' annual reports.

³⁷²Philippines' appellant's submission, para. 117.

³⁷³Panel Reports, para. 7.120 (referring to Panel Report, *Chile – Alcoholic Beverages*, para. 7.43) (original emphasis)

³⁷⁴Appellate Body Report, *Korea – Alcoholic Beverages*, para. 120.

³⁷⁵See Appellate Body Report, *Korea – Alcoholic Beverages*, paras. 122 and 123. See also Panel Report, *Chile – Alcoholic Beverages*, para. 7.78.

³⁷⁶Panel Reports, paras. 7.112 (referring to *Euromonitor International survey, supra*, footnote 37, p. 19; and Abrenica & Ducanes, *supra*, footnote 65) and 7.113.

In our view, an Article III analysis should not depend on predicting income distribution patterns, but rather on whether there is evidence that consumers are willing, or may be willing, to use the different products to satisfy the same or similar needs. In this respect, the instances of actual competition ... are a clear indication that the imported and domestic products at issue in this dispute are indeed *capable* of being directly competitive or substitutable in the future.³⁸⁶ (original emphasis)

226. We do not agree with the Philippines that this statement is in error. As noted earlier, the Philippines does not appeal the Panel's finding that there are overlaps in the prices of imported and domestic distilled spirits, both for high- and low-priced products.³⁸⁷ We have also agreed with the Panel that such price overlaps support the Panel's finding that "in some cases imported and domestic products compete with respect to price."³⁸⁸ In our view, such instances of *actual* competition are also highly probative in relation to *potential* competition, particularly in this case where imported distilled spirits are subject to excise taxes that are 10 to 40 times higher than those applicable to domestic distilled spirits. Therefore, the excise tax system could have the effect of "creating and even freezing preferences for domestic goods" in the Philippines.³⁸⁹ For this reason, instances of *current* substitution are likely to *underestimate* latent demand for imported spirits as a result of distortive effects introduced by the excise tax at issue. This is particularly the case for "experience goods" such as distilled spirits, which consumers "tend to purchase because they are familiar with them and with which consumers experiment only reluctantly".³⁹⁰

227. In addition, we do not agree with the Philippines that an analysis of potential competition under Article III:2, second sentence, is limited to an assessment of whether competition would otherwise occur if the challenged taxation were not in place.³⁹¹ In our view, such a "but for" test reflects an overly restrictive interpretation of the term "directly competitive or substitutable" products, one which assumes that internal taxation is the *only* factor restricting potential substitutability. On the contrary, as noted by the Appellate Body, "consumer demand may be influenced by measures other than internal taxation", such as "earlier protectionist taxation, previous import prohibitions or quantitative restrictions".³⁹²

³⁸⁶Panel Reports, para. 7.121.

³⁸⁷Panel Reports, para. 7.118.

³⁸⁸Panel Reports, para. 7.118.

³⁸⁹Appellate Body Report, *Korea – Alcoholic Beverages*, para. 120 (quoting Panel Report, *Japan – Alcoholic Beverages II*, para. 6.28).

³⁹⁰Appellate Body Report, *Korea – Alcoholic Beverages*, para. 123.

³⁹¹Philippines' appellant's submission, para. 111.

³⁹²Appellate Body Report, *Korea – Alcoholic Beverages*, para. 123.

228. Accordingly, we do not consider that the Panel erred in drawing from instances of current price competition the inference that domestic and imported distilled spirits are capable of being substituted in the Philippine market. Latent demand for imported distilled spirits in the Philippines is likely to be *underestimated* by the effects of the excise tax at issue both on consumer perception and on price levels for imported distilled spirits.

229. In addition to its claim that the Panel erred in its application of Article III:2, second sentence, to the facts of this case, the Philippines also claims that the Panel acted inconsistently with Article 11 of the DSU in finding that imported and domestic distilled spirits are "*capable* of being directly competitive or substitutable in the future"³⁹³ without a sufficient evidentiary basis. We recall that the Appellate Body has emphasized that a claim that a panel failed to comply with its duties under Article 11 of the DSU "must stand by itself and should not be made merely as a subsidiary argument or claim in support of a claim that the panel failed to apply correctly a provision of the covered agreements."³⁹⁴ The Philippines advances, in support of its claims of violation under Article 11 of the DSU, essentially the same arguments that it puts forward in support of its claims that the Panel erred in its application of Article III:2, second sentence, of the GATT 1994. We have found that the Panel did not err in deriving from instances of actual competition a conclusion with respect to potential competition between imported and domestic distilled spirits in the Philippines market. Therefore, in the absence of additional elements demonstrating that the Panel acted inconsistently with Article 11 of the DSU in reaching this finding, we do not agree that the Panel committed error under that provision. Accordingly, we dismiss the Philippines' claim that the Panel acted inconsistently with its duties under Article 11 of the DSU in finding that imported and domestic distilled spirits are "*capable* of being directly competitive or substitutable in the future".³⁹⁵

(d) Substitutability Studies – Article 11 of the DSU

230. Finally, the Philippines claims that the Panel failed to conduct an objective assessment of the facts in its examination of the studies that aimed at evaluating the substitutability between domestic and imported distilled spirits in the Philippine market.³⁹⁶

231. According to the Philippines, the Panel's conclusion that *both* substitutability studies show "a significant degree of competitiveness or substitutability" between domestic and imported distilled

³⁹³Panel Reports, para. 7.121. (original emphasis)

³⁹⁴Appellate Body Report, *Chile – Price Band System (Article 21.5 – Argentina)*, para. 238. See also Appellate Body Report, *US – Steel Safeguards*, para. 498.

³⁹⁵Panel Reports, para. 7.121. (original emphasis)

³⁹⁶Philippines' appellant's submission, para. 162.

According to the United States, the Philippines in essence disagrees with the weight accorded by the Panel to the substitutability studies.⁴⁰⁴

234. For its part, the Panel observed that, while the *Euromonitor International* survey did not attempt to estimate the cross-price elasticity for imported and domestic distilled spirits in the Philippines⁴⁰⁵, the Abrenica & Ducanes study estimates it to range between -0.01 and 0.07, which the authors consider "low", therefore demonstrating that "local and imported brands [of distilled spirits] are non-substitutable".⁴⁰⁶ The Panel then observed that both studies were based on scenarios where prices of imported and domestic distilled spirits change simultaneously. According to the Panel, the studies' conclusions with respect to substitutability would have been clearer had the studies attempted to "isolate the effects of an increase in the price of domestic spirits on the quantities consumed of imported spirits".⁴⁰⁷ Nonetheless, the Panel concluded that:

... the studies support the proposition that there is a significant degree of competitiveness or substitutability in the Philippines' market between the distilled spirits at issue in the present dispute. This refers both to distilled spirits as a general category, as well as to specific types of distilled spirits such as gin, brandy, vodka and whisky.⁴⁰⁸ (footnote omitted)

235. We recall that Article 11 of the DSU requires a panel to "consider all the evidence presented to it, assess its credibility, determine its weight, and ensure that its factual findings have a proper basis in that evidence."⁴⁰⁹ Within these parameters, "it is generally within the discretion of the panel to decide which evidence it chooses to utilize in making findings"⁴¹⁰, and panels "are not required to accord to factual evidence of the parties the same meaning and weight as do the parties."⁴¹¹ For a claim under Article 11 to succeed, the Appellate Body must be satisfied that the panel has exceeded its authority as initial trier of facts, which requires it to provide "reasoned and adequate explanations

spirits in the Philippine market is directly contradicted by one of those studies (the Abrenica & Ducanes study), which finds "negligible" levels of substitutability.³⁹⁷ The Philippines adds that the *Euromonitor International* survey is an insufficient basis for a finding of substitutability, because it does not estimate the cross-price elasticity coefficient, does not isolate the effects of an increase in domestic prices on volumes of imported spirits, and is based on a sample that is not representative of the entire market.³⁹⁸ The Philippines adds that the Panel inaccurately described the methodology of the Abrenica & Ducanes study, because it erroneously observed that this study was based on scenarios where the prices of imported and domestic distilled spirits changed simultaneously.³⁹⁹

232. The European Union responds that the Abrenica & Ducanes study estimated that in a tax-neutral environment the market share of imported distilled spirits would increase by between 13 and 24.5 per cent, thus lending support to the Panel's conclusion on substitutability.⁴⁰⁰ The *Euromonitor International* survey also supports the Panel's conclusion with respect to substitutability, because it shows, on the basis of a representative sample, that consumers regard local and imported products as "largely substitutable" and that they would react to price movements by switching between those categories.⁴⁰¹ The European Union adds that the Panel correctly described the methodology of the Abrenica & Ducanes study, because that study did not attempt to examine consumer response to a rise in prices of all domestic spirits, or a reduction in prices of all imported spirits.⁴⁰²

233. Similarly, the United States posits that the Panel adequately examined the substitutability studies, and drew appropriate conclusions on the basis of that evidence. The Panel's conclusion that there is a "significant degree of competitiveness or substitutability" between domestic and imported distilled spirits in the Philippine market was based on a variety of evidence, including the substitutability studies, similarity of marketing campaigns, labelling, and sales locations.⁴⁰³ The United States notes that both studies found that, while small, there is substitutability in spite of persistent price gaps between imported and domestic products and other factors such as brand loyalty.

⁴⁰⁴United States' appellee's submission, para. 125.

⁴⁰⁵Panel Reports, para. 7.112 (referring to *Euromonitor International* survey, *supra*, footnote 37, p. 5).

⁴⁰⁶Panel Reports, para. 7.112 (referring to Abrenica & Ducanes, *supra*, footnote 65, pp. 2, 11, 12, and 20).

⁴⁰⁷Panel Reports, para. 7.112.

⁴⁰⁸Panel Reports, para. 7.113.

⁴⁰⁹Appellate Body Report, *Brazil – Retreaded Tyres*, para. 185 (referring to Appellate Body Report, *EC – Hormones*, paras. 132 and 133).

⁴¹⁰Appellate Body Report, *EC – Hormones*, para. 135.

⁴¹¹Appellate Body Report, *Australia – Salmon*, para. 267.

³⁹⁷Philippines' appellant's submission, paras. 163 and 164 (quoting Panel Reports, paras. 7.62 and 7.113).

³⁹⁸Philippines' appellant's submission, paras. 165 and 169.

³⁹⁹Philippines' appellant's submission, paras. 166 and 167 (quoting Panel Reports, para. 7.56).

⁴⁰⁰European Union's appellee's submission, paras. 181 (quoting Panel Reports, para. 7.55) and 182.

⁴⁰¹European Union's appellee's submission, para. 172.

⁴⁰²European Union's appellee's submission, para. 176.

⁴⁰³United States' appellee's submission, para. 118 (quoting Panel Reports, para. 7.61).

distilled spirits in the Philippines is similarly a matter falling within the purview of the Panel's fact-finding authority under Article 11 of the DSU.

238. We are also not persuaded by the Philippines' argument that the *Euromonitor International* survey did not provide a sufficient basis to rebut the Abrenica & Ducanes study's conclusion that the cross-price elasticity between imported and domestic distilled spirits in the Philippines was "low". In our view, the fact that the *Euromonitor International* survey did not attempt to estimate the cross-price elasticity or to isolate the effects of increases in domestic spirits' prices on the volume of imported spirits does not undermine the Panel's assessment of its probative value with respect to substitutability in the Philippine market. Moreover, it was for the Panel to determine the credibility of the results of the study, in light of the Philippines' objections concerning the sample upon which it is based. In our view, the Panel's finding that there is a "significant degree" of substitutability between imported and domestic distilled spirits in the Philippine market is borne out by the *Euromonitor International* survey conclusion that:

[o]n average, at an import price decrease of 25% and domestic increase of 50%, consumers were 4.9% more willing to purchase imports and 4.0% less likely to purchase domestics"; "On average, at an import price decrease of 40% to 60% and domestic increase of 100% to 200%, consumers were 10.1% more willing to purchase imports and 6.5% less likely to purchase domestics"; and, "If price were no issue, on average, consumers were 43% more likely [to] purchase local brands and 86% more likely to purchase imported ones."⁴¹⁹ (footnote omitted)

239. Thus, we consider that the Philippines' challenge is directed at the Panel's weighing of the evidence contained in the *Euromonitor International* survey and in the Abrenica & Ducanes study.

Article 11 of the DSU required the Panel to "consider all the evidence presented to it, assess its credibility, determine its weight, and ensure that its factual findings have a proper basis in that evidence".⁴²⁰ Within these parameters, the Panel did not exceed the bounds of its discretion simply by according to the evidence contained in the two studies a weight that is different than that attributed by the Philippines.⁴²¹

240. Turning to the Philippines' argument concerning the Panel's alleged mischaracterization of the methodology upon which the Abrenica & Ducanes study was based, it is not clear why the Panel's

⁴¹⁹Panel Reports, para. 7.54 (quoting *Euromonitor International* survey, *supra*, footnote 37, pp. 30 and 33).

⁴²⁰Appellate Body Report, *Brazil – Retreaded Tyres*, para. 185 (referring to Appellate Body Report, *EC – Hormones*, paras. 132 and 133).

⁴²¹See Appellate Body Report, *Australia – Salmon*, para. 267.

and coherent reasoning"⁴¹², base its finding on a sufficient evidentiary basis"⁴¹³, and treat evidence with "even-handedness".⁴¹⁴

236. Against these parameters, we turn to the specific issues raised by the Philippines on appeal. We begin with the Philippines' argument that the Panel failed to conduct an objective assessment of the matter before it because the Abrenica & Ducanes study directly contradicts the Panel's finding that "the studies support the proposition that there is a significant degree of competitiveness or substitutability" between domestic and imported distilled spirits in the Philippine market.⁴¹⁵ We agree with the Philippines that the Panel could have better explained how the Abrenica & Ducanes study could be viewed as evidence of a "significant degree" of substitutability, particularly in light of the study's conclusion that substitutability between imported and domestic distilled spirits in the Philippine market, estimated to range between -0.01 and 0.07, was "low".⁴¹⁶ However, we consider that the weight and significance to be attributed to that estimated cross-price elasticity coefficient is a matter falling within the Panel's discretion as initial trier of facts. We recall that, under the excise tax system, imported distilled spirits are subject to taxation that is 10 to 40 times higher than that applicable to domestic distilled spirits. Therefore, the excise tax could have the effect of creating or even freezing consumer preferences for domestic distilled spirits in the Philippine market. Viewed in this light, even a "low" cross-price elasticity of between -0.01 and 0.07 could be found "significant", particularly at the higher end of that range. In this respect, we agree with the panel in *Chile – Alcoholic Beverages* that a low coefficient of cross-price elasticity is not "fatal" to a claim of direct competitiveness or substitutability because "the econometric measurement of the degree of substitution may not ... always adequately reflect the extent of substitution" by virtue of the effects of the internal taxation on consumer preferences and the foreign suppliers' pricing behaviour.⁴¹⁷

237. Moreover, despite its conclusion that the cross-price elasticity between domestic and imported distilled spirits in the Philippines is "low", the Abrenica & Ducanes study in fact also concluded that the market share of imported distilled spirits in the Philippines would increase by between 13 and 24.5 per cent in a tax-neutral environment.⁴¹⁸ The assessment of the significance of such market share increases in terms of the degree of competition between domestic and imported

⁴¹²Appellate Body Report, *US – Upland Cotton (Article 21.5 – Brazil)*, footnote 618 to para. 293.

⁴¹³See Appellate Body Report, *US – Carbon Steel*, para. 148.

⁴¹⁴Appellate Body Report, *US – Upland Cotton (Article 21.5 – Brazil)*, para. 292.

⁴¹⁵Panel Reports, para. 7.113.

⁴¹⁶A coefficient of cross-price elasticity of -0.01 means that the choice probability for the imported spirit would decline by 1 per cent due to a 10 per cent increase in the price of domestic spirits. Conversely, the choice probability for the imported spirit would increase by 7 per cent as a result of a 10 per cent increase in the price of domestic spirits. (See Abrenica & Ducanes, *supra*, footnote 65, p. 12)

⁴¹⁷Panel Report, *Chile – Alcoholic Beverages*, paras. 7.69 and 7.70.

⁴¹⁸Panel Reports, para. 7.55 (referring to Abrenica & Ducanes, *supra*, footnote 65, p. 14).

allegedly inaccurate description of such methodology as one based on simultaneous changes in the prices of both imported and domestic spirits would amount to a violation of its duties under Article 11 of the DSU. The Appellate Body has held that "not every error in the appreciation of a particular piece of evidence will rise to the level of a failure by the Panel to comply with its duties under Article 11 of the DSU."⁴²² According to the Appellate Body, this will only be the case where such error "undermine[s] the objectivity of the Panel's assessment".⁴²³ In this case, the Philippines has not demonstrated that the Panel's alleged mischaracterization of the methodology used in the Abrenica & Ducanes study calls into question the objectivity of the Panel's assessment of the substitutability studies. In any event, the Philippines seems correct in arguing that, in the first part of the Abrenica & Ducanes study, consumer preferences were initially assessed in a scenario where prices of the selected brand increased, while prices for all other brands remained unchanged. However, in the second part of the study, changes in the market share for imported distilled spirits were estimated under three tax-neutral scenarios (uniform excise tax, *ad valorem* tax, and no tax) in which prices of imported brands would fall, while those of their local counterparts simultaneously would increase.⁴²⁴

241. Accordingly, we do not consider that the Panel acted inconsistently with its duties under Article 11 of the DSU in its examination of the *Euromonitor International* survey and of the Abrenica & Ducanes study.

(c) Conclusion

242. In light of all of the above, we consider that the Panel did not err in its assessment of the competitive relationship between the imported and domestic distilled spirits at issue in the Philippine market. In our view, studies showing a significant degree of substitutability in the Philippine market between imported and domestic distilled spirits, as well as instances of price competition and evidence of actual and potential competition between imported and domestic distilled spirits in the Philippine market, sufficiently support the Panel's conclusion that there is "a direct competitive relationship [in the Philippines] between domestic and imported distilled spirits, made from different raw materials".⁴²⁵ This factor, combined with the other elements upon which the Panel relied, such as overlap in the channels of distribution⁴²⁶, and similarities in the products' physical characteristics⁴²⁷, end-uses, and marketing⁴²⁸, sufficiently support the Panel's finding that all imported

⁴²² Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1318.

⁴²³ Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1318.

⁴²⁴ See Panel Reports, para. 7.55 (referring to Abrenica & Ducanes, *supra*, footnote 65, p. 13).

⁴²⁵ Panel Reports, para. 7.137.

⁴²⁶ Panel Reports, para. 7.123.

⁴²⁷ Panel Reports, para. 7.127.

and domestic distilled spirits at issue are "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the GATT 1994.

243. Accordingly, we uphold the Panel's finding, at paragraph 7.138 of the Panel Reports, that all the distilled spirits at issue in the present dispute, whether imported or domestic, and irrespective of the raw materials from which they are made, are "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the GATT 1994.

2. "So As to Afford Protection to Domestic Production"

244. We now turn to the Philippines' claim that the Panel erred in finding that the Philippines' excise tax is applied in a manner "so as to afford protection to domestic production" within the meaning of Article III:2, second sentence, of the GATT 1994.

245. We recall that, in reviewing the "design, architecture and structure" of the measure at issue, the Panel observed that all designated raw materials listed in Section 141(a) of the NIRC are grown in the Philippines and "all domestic distilled spirits are produced from designated raw materials", thus being subject to the lower flat tax rate of PHP 14.68 ppl.⁴²⁹ By contrast, the vast majority of imported distilled spirits are not made from designated raw materials and are therefore subject to the higher tax rates provided for in Section 141(b), varying from PHP 158.73 to PHP 634.90 ppl. For the Panel, this meant that "*de facto* the measure results in all domestic distilled spirits enjoying the favourable low tax, while the vast majority of the imported spirits" are subject to taxes between 10 and 40 times higher.⁴³⁰

246. The Panel rejected the Philippines' argument that the measure at issue has no impact on competitive conditions in its market by virtue of the low purchasing power of the vast majority of the Philippine population and of the pre-tax price differences between domestic and imported distilled spirits. The Panel observed that, in *Korea – Alcoholic Beverages*, the Appellate Body rejected a "very similar argument" and found that, since the products at issue "ha[d] already been found to be directly competitive or substitutable", such argument was "misplaced at this stage of the analysis".⁴³¹ The Appellate Body in that dispute further stated that "Article III is not concerned with trade volumes" and

⁴²⁸ Panel Reports, paras. 7.129 and 7.131.

⁴²⁹ Panel Reports, para. 7.182. (original emphasis)

⁴³⁰ Panel Reports, paras. 7.182 and 7.183.

⁴³¹ Panel Reports, para. 7.185 (quoting Appellate Body Report, *Korea – Alcoholic Beverages*, para. 152).

therefore "[i]t is ... not incumbent on a complaining party to prove that tax measures are capable of producing any particular trade effect."⁴³²

247. In light of the above considerations, the Panel concluded that:

... the design, architecture, and structure of the measure, including the magnitude of the tax differential applicable to imported and domestic products, reveal the protective nature of the measure. ... [T]he dissimilar taxation imposed by the Philippine excise tax on imported distilled spirits and on directly competitive or substitutable domestic spirits is applied "so as to afford protection" to Philippine domestic production of distilled spirits.⁴³³

248. The Philippines claims that the Panel's finding is in error for two reasons. First, the facts "simply do not support" the Panel's conclusion that "the vast majority of imported spirits are subject to higher taxes"⁴³⁴ because approximately 50 per cent of the domestic production of distilled spirits is made from imported ethyl alcohol, a "significant quantity" of which is, in turn, subject to the lower flat tax rate under Section 141(a) of the NIRC.⁴³⁵ Second, the Philippines submits that the Panel erroneously rejected its argument that the excise tax could have no protectionist intent given that the vast majority of Philippine households cannot afford imported distilled spirits. In particular, by merely "transferring the reasoning"⁴³⁶ applied by the Appellate Body to the facts in *Korea – Alcoholic Beverages* and dismissing the Philippines' argument "for the same reasons"⁴³⁷, the Panel engaged in a "legally deficient" inquiry⁴³⁸ and fell short of the case-by-case, "comprehensive and objective analysis" that is required under Article III:2, second sentence, of the GATT 1994.⁴³⁹

249. The European Union and the United States respond that the Panel was correct in finding that the excise tax is applied "so as to afford protection to domestic production". In particular, the European Union stresses that ethyl alcohol is merely an input used in the production of distilled spirits

⁴³²Panel Reports, para. 7.185 (quoting Appellate Body Report, *Korea – Alcoholic Beverages*, para. 153).

⁴³³Panel Reports, para. 7.187.

⁴³⁴Philippines' appellant's submission, para. 128 (quoting Panel Reports, para. 7.182).

⁴³⁵Philippines' appellant's submission, para. 128 (referring to Letter from the Commissioner of the Philippines Bureau of Internal Revenue, dated 3 February 2011, to the President of Distilled Spirits Association of the Philippines (Panel Exhibit PH-82), and Philippines' response to Panel Question 68(a)).

⁴³⁶Philippines' appellant's submission, para. 134.

⁴³⁷Panel Reports, para. 7.186.

⁴³⁸Philippines' appellant's submission, para. 132.

⁴³⁹Philippines' appellant's submission, paras. 133 (quoting Panel Reports, para. 7.179, in turn quoting Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 29, DSR 1996:1, 97, at 120; and referring to Appellate Body Report, *Korea – Alcoholic Beverages*, para. 137).

and is therefore of no relevance to the current dispute.⁴⁴⁰ It further submits that, at this stage of its analysis, the Panel rightly refrained from re-addressing the question of whether domestic and imported spirits are "directly competitive or substitutable".⁴⁴¹ The United States argues that the Panel correctly focused on the "magnitude of the difference in taxation, ... the design, structure and application" of the measure at issue.⁴⁴² Likewise, the Panel appropriately focussed on the final products at issue, rather than on inputs used by domestic producers.⁴⁴³ The United States maintains further that it was not necessary for the Panel to inquire into the motivations for the measure, and emphasizes that the Philippines does not dispute the fact that imported distilled spirits are subject to higher taxes than all domestic distilled spirits.⁴⁴⁴

250. We recall that, in *Japan – Alcoholic Beverages II*, the Appellate Body stated that the question of whether dissimilar taxation affords protection is not one of intent, but rather of application of the measure at issue. This requires a "comprehensive and objective analysis of the structure and application of the measure in question on domestic as compared to imported products".⁴⁴⁵ The Appellate Body observed that, "[a]lthough it is true that the aim of a measure may not be easily ascertained, nevertheless its protective application can most often be discerned from the design, the architecture, and the revealing structure of a measure."⁴⁴⁶ The Appellate Body further stated that dissimilar taxation must be more than *de minimis*, and that in certain cases "[t]he very magnitude of the dissimilar taxation ... may be evidence of such a protective application."⁴⁴⁷ In *Korea – Alcoholic Beverages*, the Appellate Body added that the protective application of dissimilar taxation can only be determined "on a case-by-case basis, taking account of all relevant facts".⁴⁴⁸

251. Against this background, we now turn to the specific issues raised by this part of the Philippines' appeal. The Philippines claims that the Panel erred in finding that the "vast majority of imported spirits are subject to higher taxes" because approximately 50 per cent of domestic production is made from imported ethyl alcohol, which is taxed at the lower rate.⁴⁴⁹

⁴⁴⁰European Union's appellee's submission, paras. 122 and 123.

⁴⁴¹European Union's appellee's submission, paras. 128-130.

⁴⁴²United States' appellee's submission, para. 93.

⁴⁴³United States' appellee's submission, para. 96.

⁴⁴⁴United States' appellee's submission, para. 97.

⁴⁴⁵Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 29, DSR 1996:1, 97, at 120. See also Appellate Body Report, *Korea – Alcoholic Beverages*, para. 149.

⁴⁴⁶Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 29, DSR 1996:1, 97, at 120.

⁴⁴⁷Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 29, DSR 1996:1, 97, at 120.

⁴⁴⁸Appellate Body Report, *Korea – Alcoholic Beverages*, para. 137.

⁴⁴⁹Philippines' appellant's submission, para. 128.

252. We do not find merit in the Philippines' argument in this respect. In our view, the question before the Panel at this stage of its analysis was whether the design, architecture, and structure of the excise tax indicates that such measure affords protection to the Philippine production of the "directly competitive or substitutable" distilled spirits at issue in this dispute. Ethyl alcohol, as such, does not fall within the category of the "directly competitive or substitutable" distilled spirits at issue, but, rather, is an input used in the production of these distilled spirits. Therefore, the fact that imported ethyl alcohol is subject to taxation similar to that imposed on domestic distilled spirits had no bearing on the Panel's assessment of whether the excise tax affords protection to domestic production of the directly competitive or substitutable distilled spirits at issue.

253. We now turn to the Philippines' claim that the Panel fell short of the required "case-by-case, comprehensive analysis" when it dismissed its argument that the excise tax could not afford protection to domestic production because of the competitive conditions in the Philippine market, where the majority of the population cannot afford imported distilled spirits.⁴⁵⁰

254. We agree with the Philippines that, read in isolation, the portion of the Panel's reasoning at which the Philippines' claim is directed was too cursory. Had the Panel found that the excise tax regime affords protection to domestic production solely by referring to the reasoning articulated by the Appellate Body in *Korea – Alcoholic Beverages*, it would have fallen short of a comprehensive and objective analysis of the case at hand.

255. However, the Panel's analysis of whether the measure at issue is applied so as to afford protection to Philippine production was not as limited as the Philippines suggests. Indeed, the Panel reviewed "the design, architecture and structure" of the measure in some detail and observed that, while "[a]ll designated raw materials are grown in the Philippines and all domestic distilled spirits are produced from designated raw materials", the vast majority of imported distilled spirits "are *not* made from designated raw materials".⁴⁵¹ It therefore concluded that, *de facto*, the application of the measure resulted in all domestic spirits enjoying the lower flat tax rate, while the vast majority of imported spirits are subject to higher taxes.⁴⁵² The Panel stressed further that the more burdensome tax treatment applied to imported spirits can be quantified in the order of "10 to 40 times that applicable to all domestic spirits", thus making the difference in taxation "nominally large".⁴⁵³ In our view, these findings by the Panel, taken as a whole, constitute an adequate analysis of the specific

⁴⁵⁰Philippines' appellant's submission, para. 135.

⁴⁵¹Panel Reports, para. 7.182. (original emphases)

⁴⁵²Panel Reports, para. 7.182.

⁴⁵³Panel Reports, para. 7.183.

facts of this dispute, as they relate to the European Union's and the United States' claims under Article III:2, second sentence, of the GATT 1994.

256. Having made the findings above, the Panel went on to dismiss the Philippines' argument regarding the lack of protective application on the basis of market segmentation. We agree with the Panel that the assessment of whether the excise tax could affect the competitive relationship between domestic and imported distilled spirits in the Philippine market pertains to the prong of analysis directed at determining whether the products are "directly competitive or substitutable". Having addressed—and rejected—the Philippines' arguments concerning pre-tax price differentials when determining whether the products at issue are "directly competitive or substitutable" in the Philippine market, it was not necessary for the Panel to revisit this argument in its assessment of whether the dissimilar taxation of such products afforded protection to domestic production. Moreover, the passage of the Appellate Body report in *Korea – Alcoholic Beverages* quoted by the Panel explained that a finding that a tax measure affords protection to domestic production does not depend upon showing "some identifiable trade effect".⁴⁵⁴ Thus, the question of whether or not the excise tax negatively impacts trade in imported distilled spirits is not determinative of the question of whether the measure affords protection to domestic production.

257. In light of the above, we do not consider that the Panel erred in its application of the term "so as to afford protection to domestic production" when it found, in paragraph 7.187 of the Panel Reports, that "the design, architecture, and structure of the measure, including the magnitude of the tax differential applicable to imported and domestic products, reveal the protective nature of the measure."⁴⁵⁵ Accordingly, we *uphold* the Panel's finding, in paragraph 7.187 of the Panel Reports, that dissimilar taxation imposed by the Philippine excise tax on imported distilled spirits and on directly competitive or substitutable domestic spirits is applied "so as to afford protection" to Philippine production of distilled spirits.

C. Conclusion

258. For all the foregoing reasons, we *uphold* the Panel's finding, in paragraph 7.188 of its Reports, that the Philippines has acted inconsistently with Article III:2, second sentence, of the GATT 1994 by applying dissimilar internal taxation to all imported distilled spirits made from non-designated raw materials and to all directly competitive or substitutable domestic distilled spirits

⁴⁵⁴Panel Reports, para. 7.185 (quoting Appellate Body Report, *Korea – Alcoholic Beverages*, para. 153).

⁴⁵⁵Panel Reports, para. 7.187.

made from designated raw materials, so as to afford protection to Philippine production of distilled spirits.

259. Consequently, we *uphold* the Panel's finding, in paragraphs 7.188 and 8.2(b) of the US Panel Report, that the Philippines has acted inconsistently with Article III:2, second sentence, of the GATT 1994 by applying dissimilar internal taxes to all imported spirits made from non-designated raw materials and to all directly competitive or substitutable domestic distilled spirits made from designated raw materials, so as to afford protection to Philippine production of distilled spirits.

260. Having *reversed* the Panel's finding at paragraph 8.3 of the EU Panel Report that the European Union's claim under the second sentence of Article III:2 was made in the "alternative" to its claim under the first sentence thereof, we complete the legal analysis on the basis of factual findings made by the Panel in the context of the complaints by the European Union and the United States, and on the basis of the legal findings that the Panel made under Article III:2, second sentence, in addressing the complaint by the United States, as upheld in this appeal. We consequently *find*, in relation to the European Union's claim, that the Philippines has acted inconsistently with Article III:2, second sentence, of the GATT 1994 by applying dissimilar internal taxation to all imported spirits made from non-designated raw materials and to all directly competitive or substitutable domestic distilled spirits made from designated raw materials, so as to afford protection to Philippine production of distilled spirits.

VII. Findings and Conclusions in the Appellate Body Report WT/DS396/AB/R

261. In the appeal of the Panel Report, *Philippines – Taxes on Distilled Spirits* (complaint by the European Union, WT/DS396/R) (the "EU Panel Report"), for the reasons set out in this Report, the Appellate Body:

- (a) with respect to Article III:2, first sentence, of the GATT 1994:
 - (i) upholds the Panel's finding, in paragraph 7.85 of the EU Panel Report, that each type of imported distilled spirit at issue in this dispute—gin, brandy, vodka, whisky, and tequila—made from non-designated raw materials is "like" the same type of domestic distilled spirit made from designated raw materials, within the meaning of Article III:2, first sentence, of the GATT 1994;
 - (ii) finds that the Panel did not act inconsistently with Article 11 of the DSU in its evaluations of the products' physical characteristics, of the Philippine market for distilled spirits, and of tariff classification;
 - (iii) upholds, as a consequence, the Panel's finding, in paragraphs 7.90 and 8.2 of the EU Panel Report, that the Philippines has acted inconsistently with Article III:2, first sentence, of the GATT 1994 by imposing on each type of imported distilled spirit at issue in this dispute—gin, brandy, rum, vodka, whisky, and tequila—internal taxes in excess of those applied to "like" domestic distilled spirits of the same type made from designated raw materials; and
 - (iv) reverses the Panel's finding, in paragraph 7.77 of the EU Panel Report, to the extent that it stands for the proposition that *all* distilled spirits at issue in this dispute are "like products", regardless of types, within the meaning of Article III:2, first sentence, of the GATT 1994;
- (b) with respect to Article III:2, second sentence, of the GATT 1994:
 - (i) reverses the Panel's findings, in paragraphs 7.1, 7.5, 7.17, 7.92, 7.93, 7.95, and 8.3 of the EU Panel Report, that the European Union's claim under Article III:2, second sentence, of the GATT 1994 was made in the "alternative" to its claim under the first sentence of that provision;

- (ii) finds that the Panel acted inconsistently with its duties under Article 11 of the DSU, in paragraph 8.3 of the EU Panel Report, by failing to examine, and abstaining from making findings in relation to, the European Union's separate and independent claim under Article III:2, second sentence, of the GATT 1994;
- (iii) upholds the Panel's finding, in paragraph 7.138 of the EU Panel Report, that all imported distilled spirits made from non-designated raw materials and all domestic distilled spirits made from designated raw materials at issue in this dispute are "directly competitive or substitutable" within the meaning of Article III:2, second sentence, of the GATT 1994, and finds that the Panel did not act inconsistently with Article 11 of the DSU in reaching this finding;
- (iv) upholds the Panel's finding, in paragraph 7.187 of the EU Panel Report, that dissimilar taxation imposed by the Philippine excise tax on imported distilled spirits and on directly competitive or substitutable domestic spirits is applied "so as to afford protection" to Philippine production of distilled spirits; and
- (v) on this basis, completes the legal analysis in relation to the European Union's separate and independent claim under Article III:2, second sentence, and finds that the Philippines has acted inconsistently with Article III:2, second sentence, of the GATT 1994, by applying dissimilar internal taxation to imported distilled spirits and to directly competitive or substitutable domestic distilled spirits, so as to afford protection to Philippine production of distilled spirits.

262. The Appellate Body recommends that the DSB request the Philippines to bring its measures, found in this Report and in the EU Panel Report, as modified by this Report, to be inconsistent with the GATT 1994, into conformity with its obligations under that Agreement.

Signed in the original in Geneva this 7th day of December 2011 by:

Peter Van den Bossche
Presiding Member

Jennifer Hillman
Member

Ricardo Ramirez-Hernández
Member

VII. Findings and Conclusions in the Appellate Body Report WT/DS403/AB/R

261. In the appeal of the Panel Report, *Philippines – Taxes on Distilled Spirits* (complaint by the United States, WT/DS403/R) (the "US Panel Report"), for the reasons set out in this Report, the Appellate Body:

- (a) with respect to Article III-2, first sentence, of the GATT 1994:
 - (i) upholds the Panel's finding, in paragraph 7.85 of the US Panel Report, that each type of imported distilled spirit at issue in this dispute—gin, brandy, vodka, whisky, and tequila—made from non-designated raw materials is "like" the same type of domestic distilled spirit made from designated raw materials, within the meaning of Article III-2, first sentence, of the GATT 1994;
 - (ii) finds that the Panel did not act inconsistently with Article 11 of the DSU in its evaluations of the products' physical characteristics, of the Philippine market for distilled spirits, and of tariff classification;
 - (iii) upholds, as a consequence, the Panel's finding, in paragraphs 7.90 and 8.2(a) of the US Panel Report, that the Philippines has acted inconsistently with Article III-2, first sentence, of the GATT 1994 by imposing on each type of imported distilled spirit at issue in this dispute—gin, brandy, rum, vodka, whisky, and tequila—internal taxes in excess of those applied to "like" domestic distilled spirits of the same type made from designated raw materials; and
 - (iv) reverses the Panel's finding, in paragraph 7.77 of the US Panel Report, to the extent that it stands for the proposition that *all* distilled spirits at issue in this dispute are "like products", regardless of types, within the meaning of Article III-2, first sentence, of the GATT 1994;

(b) with respect to Article III-2, second sentence, of the GATT 1994:

- (i) upholds the Panel's finding, in paragraph 7.138 of the US Panel Report, that all imported distilled spirits made from non-designated raw materials and all domestic distilled spirits made from designated raw materials are "directly competitive or substitutable" within the meaning of Article III-2,

second sentence, of the GATT 1994, and finds that the Panel did not act inconsistently with Article 11 of the DSU in reaching this finding;

- (ii) upholds the Panel's finding, in paragraph 7.187 of the US Panel Report, that dissimilar taxation imposed by the Philippine excise tax on imported distilled spirits and on directly competitive or substitutable domestic spirits is applied "so as to afford protection" to Philippine production of distilled spirits; and
- (iii) upholds, as a consequence, the Panel's finding in paragraphs 7.188 and 8.2(b) of the US Panel Report, that the Philippines has acted inconsistently with Article III-2, second sentence, of the GATT 1994 by applying dissimilar internal taxation to all imported distilled spirits made from non-designated raw materials and to all directly competitive or substitutable domestic distilled spirits made from designated raw materials, so as to afford protection to Philippine production of distilled spirits.

262. The Appellate Body recommends that the DSB request the Philippines to bring its measures, found in this Report and in the US Panel Report, as modified by this Report, to be inconsistent with the GATT 1994, into conformity with its obligations under that Agreement.

Signed in the original in Geneva this 7th day of December 2011 by:

ANNEX I

**WORLD TRADE
ORGANIZATION**

WT/DS396/7
WT/DS403/7
27 September 2011
(11-4674)

Original: English

Peter Van den Bossche
Presiding Member

PHILIPPINES – TAXES ON DISTILLED SPIRITS

Notification of an Appeal by the Philippines under Article 16.4 and Article 17 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), and under Rule 20(1) of the Working Procedures for Appellate Review

The following notification, dated 23 September 2011, from the Delegation of the Republic of the Philippines, is being circulated to Members.

Jennifer Hillman
Member

Ricardo Ramírez-Hernández
Member

1. Pursuant to Articles 16.4 and 17 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 20 of the *Working Procedures for Appellate Review* (WT/AB/WP/6, 16 August 2010), the Republic of the Philippines ("the Philippines") hereby notifies the Dispute Settlement Body ("DSB") of its decision to appeal certain issues of law and legal interpretations in *Philippines – Taxes on Distilled Spirits* (WT/DS396, WT/DS403) ("Panel Report"). As set out in this notice of appeal, and pursuant to Article 17.13 of the DSU, the Philippines requests that the Appellate Body reverse or modify various legal findings and conclusions of the Panel, that result from the errors identified below.

2. Pursuant to Rule 20(2)(d)(iii) of the *Working Procedures for Appellate Review*, this notice of appeal includes an indicative list of the paragraphs of the Panel Report containing the alleged errors, without prejudice to the Philippines' ability to refer to other paragraphs of the Panel Report in the context of its appeal.

I. APPEAL OF THE PANEL'S FINDINGS OF A VIOLATION OF ARTICLE III:2, FIRST SENTENCE OF THE GATT 1994

3. The Panel erred in its interpretation and application of the term "like products" under Article III:2, first sentence of the GATT 1994 and failed to apply the appropriate standard when assessing the products' physical characteristics, consumer tastes and habits, and the products' tariff classifications.

4. The Panel's errors of law and legal application include:

- (a) The Panel failed to apply the correct standard when examining the physical characteristics of the products in question, and the manner in which they compete in the Philippine market.
 - (b) The Panel failed to apply the correct standard when assessing consumers' tastes and habits in the Philippine market.
 - (c) The Panel failed to apply the appropriate standard when examining whether the tariff classification of non-sugar-based spirits and sugar-based spirits indicated "likeness."
5. As a result of these errors, the Philippines requests that the Appellate Body reverse the Panel's findings in paragraphs 7.39, 7.40, 7.42, 7.43, 7.45, 7.46, 7.47, 7.59, 7.60, 7.62, 7.63, 7.71, 7.74, 7.76, 7.77, 7.80, 7.82, 7.83, 7.85, 7.90, 8.2 (with respect to the claims of the European Union) and 8.2(a) (with respect to the claims of the United States) of the Panel Report.

II. APPEAL OF THE PANEL'S FINDINGS OF A VIOLATION OF ARTICLE III:2, SECOND SENTENCE OF THE GATT 1994

6. The Panel erred in its interpretation and application of the term "directly competitive or substitutable" within the meaning of Article III:2, second sentence of the GATT 1994, as well as the term "so as to afford protection". The Panel consequently also failed to apply the correct standard when assessing competition in the Philippine market.

7. The Panel's errors of law and legal application include:

- (a) The Panel failed to properly interpret and apply the term "directly" when it found that competition existed in the market due to the possibility that some consumer could purchase non-sugar-based spirits on "special occasions."
- (b) The Panel failed to apply the correct standard when it found that it was sufficient for a certain market segment to have access to both types of products.
- (c) The Panel failed to apply the correct standard when it found that potential competition existed in the Philippine market.
- (d) The Panel misinterpreted the application of the term "directly competitive or substitutable" by finding that some degree of substitutability in a non-representative sample of the market in question was sufficient to show direct competition.
- (e) The Panel erred in its interpretation of the treaty term "so as to afford protection to domestic production", and misapplied this provision in the instant case.

8. As a result of these errors, the Philippines requests that the Appellate Body reverse the Panel's findings in paragraphs 7.118, 7.119, 7.120, 7.121, 7.137, 7.138, 7.187, 7.188, and 8.2(b) (with respect to the claims of the United States) of the Panel Report.

III. APPEAL OF THE PANEL'S FAILURE TO MAKE AN OBJECTIVE ASSESSMENT OF THE MATTER AS REQUIRED BY ARTICLE II OF THE DSU

9. The Panel acted inconsistently with Article 11 of the DSU by failing to conduct an objective assessment of the matter when examining the evidence relating to physical characteristics of the products at issue, their tariff classification, the result of the econometric study and the Euromonitor International study and the segmentation of the market.

10. The Panel's errors of law and legal application under Article 11 include:

- (a) The Panel erroneously substituted its own judgment for that of the experts in relation to the organoleptic properties of the products and the congener results.
- (b) The Panel erred when it found that the evidence on tariff classification was inconclusive.
- (c) The Panel misinterpreted the results of the econometric study and the Euromonitor International survey, and substituted its own judgment for that of the experts in violation of Article 11.
- (d) The Panel erred when it found that the Philippine market is not segmented and that "many consumers may be able to purchase high-priced spirits" on "special occasions".
- (e) The Panel erred when it concluded that there is evidence that the products are capable of being directly competitive or substitutable in the near future.

11. As a result of these errors, the Philippines requests that the Appellate Body reverse the Panel's findings in paragraphs 7.39, 7.40, 7.42, 7.43, 7.45, 7.46, 7.56, 7.57, 7.59, 7.60, 7.62, 7.76, 7.77, 7.80, 7.82, 7.90, 7.113, 7.119, 7.121, 7.127, 7.137, 7.138, 7.188, 8.2 (with respect to the claims of the European Union) and 8.2(a) and (b) (with respect to the claims of the United States) of the Panel Report.

ANNEX II

**WORLD TRADE
ORGANIZATION**

WT/DS396/8
WT/DS403/8
30 September 2011
(11-4741)

Original: English

PHILIPPINES – TAXES ON DISTILLED SPIRITS

Notification of an Other Appeal by the European Union under Article 16.4 and Article 17 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), and under Rule 23(1) of the Working Procedures for Appellate Review

The following notification, dated 28 September 2011, from the Delegation of the European Union, is being circulated to Members.

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Pursuant to Articles 16.4 and 17 of the *DSU*, the European Union hereby notifies to the Dispute Settlement Body its decision to appeal to the Appellate Body certain issues of law covered and certain legal interpretations developed by the Panel in *Philippines – Taxes on Distilled Spirits* (WT/DS396, WT/DS403) ("Panel Report"). Pursuant to Rule 23(1) of the *Working Procedures for Appellate Review*, the European Union simultaneously files this Notice of Other Appeal with the Appellate Body Secretariat.

For the reasons further elaborated in its submissions to the Appellate Body, the European Union appeals, and requests the Appellate Body to reverse, modify or declare moot and of no legal effect the findings and conclusions of the Panel, with respect to the following errors of law and legal interpretations contained in the Panel Report, and to complete the analysis¹:

I. MISCHARACTERISATION OF THE EUROPEAN UNION CLAIM UNDER ARTICLE III:2, SECOND SENTENCE, OF THE GATT

The Panel erred in its interpretation and application of Article 7, paragraphs 1 and 2, of the *DSU*, and/or failed to make an objective assessment pursuant to Article 11 of the *DSU*, and/or falsely exercised judicial economy, thereby violating Articles 3.7 and 21.1 of the *DSU*, when it wrongly characterised the claim put forward by the European Union under Article III:2, second sentence, of the GATT as "alternative"², and consequently failed to make any findings in relation to it.³ The European Union requests the Appellate Body to complete the analysis.

¹Pursuant to Rule 20(2)(d)(iii) of the *Working Procedures for Appellate Review* this Notice of Appeal includes an indicative list of the paragraphs of the Panel Report containing the alleged errors, without prejudice to the ability of the European Union to refer to other paragraphs of the Panel Report in the context of its appeal.

²Panel Report, paras. 7.1, 7.5, 7.17, 7.92, 7.93, 7.95 and 8.3.

³Panel Report, paras. 7.95 and 8.3.

World Trade Organization

**China – Measures related to the Exportation of Various Raw
Materials**

Report of the Appellate Body, 30 January 2012

WORLD TRADE ORGANIZATION

WT/DS394/AB/R
WT/DS395/AB/R
WT/DS398/AB/R
30 January 2012

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CHINA – MEASURES RELATED TO THE EXPORTATION OF VARIOUS RAW MATERIALS

AB-2011-5

Reports of the Appellate Body

Note:

The Appellate Body is issuing these Reports in the form of a single document constituting three separate Appellate Body Reports: WT/DS394/AB/R; WT/DS395/AB/R; and WT/DS398/AB/R. The cover page, preliminary pages, Sections I through VIII and the Annexes are common to all three Reports. The page header throughout the document bears three document symbols, WT/DS394/AB/R, WT/DS395/AB/R, and WT/DS398/AB/R, with the following exceptions: Section IX on pages US-145 and US-146, which bears the document symbol for and contains the Appellate Body's findings and conclusions in the Appellate Body Report WT/DS394/AB/R; Section IX on pages EU-145 and EU-146, which bears the document symbol for and contains the Appellate Body's findings and conclusions in the Appellate Body Report WT/DS395/AB/R; and Section IX on pages MEX-145 and MEX-146, which bears the document symbol for and contains the Appellate Body's findings and conclusions in the Appellate Body Report WT/DS398/AB/R.

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US – Upland Cotton	Appellate Body Report, <i>United States – Subsidies on Upland Cotton</i> , WT/DS267/AB/R, adopted 21 March 2005, DSR 2005:I, 3
US – Wheat Gluten	Appellate Body Report, <i>United States – Definitive Safeguard Measures on Imports of Wheat Gluten from the European Communities</i> , WT/DS166/AB/R, adopted 19 January 2001, DSR 2001:II, 717
US – Wool Shirts and Blouses	Appellate Body Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/AB/R, adopted 23 May 1997, and Corr.1, DSR 1997:I, 323
US – Wool Shirts and Blouses	Panel Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/R, adopted 23 May 1997, upheld by Appellate Body Report WT/DS33/AB/R, DSR 1997:I, 343
US – Zeroing (EC) (Article 21.5 – EC)	Appellate Body Report, <i>United States – Laws, Regulations and Methodology for Calculating Dumping Margins ("Zeroing") – Recourse to Article 21.5 of the DSU by the European Communities</i> , WT/DS294/AB/RW and Corr.1, adopted 11 June 2009
US – Zeroing (Japan) (Article 21.5 – Japan)	Appellate Body Report, <i>United States – Measures Relating to Zeroing and Sunset Reviews – Recourse to Article 21.5 of the DSU by Japan</i> , WT/DS322/AB/RW, adopted 31 August 2009

Abbreviation	Definition
2008 Export Licence Administration Measures	Measures for the Administration of Licence for the Export of Goods, Order of the Ministry of Commerce (2008) No. 11, 1 July 2008 (Panel Exhibits CHN-342 and JE-74)
2008 Export Licensing Working Rules	Working Rules on Issuing Export Licences, Ministry of Commerce, Shangpeifa (2008) No. 398, 9 October 2008 (Panel Exhibits CHN-344 and JE-97)
2009 Announcement of Second Bidding Round for Talc and Silicon Carbide	Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009, Committee for the Invitation for bid for Export Commodity Quotas, 16 September 2009 (Panel Exhibit JE-132)
2009 Export Licensing Catalogue	Notice "2009 Export Licensing Management Commodities List", Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, 1 January 2009 (Panel Exhibits CHN-6 and JE-22)
2009 Export Quota Amounts	Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products, Ministry of Commerce, Notice (2008) No. 83, 1 January 2009 (Panel Exhibit JE-79)
2009 First Round Bauxite Bidding Procedures	Quotas of Bauxite of 2009, Committee for the Invitation for bid for Export Commodity Quotas, 10 December 2008 (Panel Exhibit JE-94)
2009 First Round Export Quota Bidding Announcement	Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009, Ministry of Commerce, Announcement (2008) No. 85, 30 October 2008 (Panel Exhibits CHN-309 and JE-90)
2009 Graded Export Licensing Entities Catalogue	Announcement of the Ministry of Commerce Issuing the "2009 Graded Licence-Issuing List of Commodities Subject to Export Licence Administration", Ministry of Commerce, Notice (2008) No. 124, 1 January 2009 (Panel Exhibit JE-96)
2009 Second Round Export Quota Bidding Announcement	Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009, Ministry of Commerce, Announcement (2009) No. 42, 8 June 2009 (Panel Exhibits CHN-310 and JE-91)
2009 Tariff Implementation Program	Notice Regarding the 2009 Tariff Implementation Program, State Council Tariff Policy Commission, Shuweiwhui (2008) No. 40, 1 January 2009 (Panel Exhibit JE-21)
2010 Tariff Implementation Plan	Circular of the State Council Tariff Commission on the 2010 Tariff Implementation Plan, Shui Wei Hui [2009] No. 28, promulgated by the Customs Tariff Commission of the State Council on 8 December 2009 (Panel Exhibit CHN-5)
CCCMC	Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters of the People's Republic of China
China's Accession Protocol	Protocol on the Accession of the People's Republic of China to the WTO, WT/L/432

Abbreviation	Definition
China's Accession Working Party Report	Report of the Working Party on the Accession of China, WT/ACC/CHN/49 and Corr.1
China's request for a preliminary ruling	Communication from China to the Panel: China's request for a preliminary ruling pursuant to Article 6.2 of the DSU, 30 March 2010
Complainants	United States, European Union, and Mexico
Complainants' response to China's request for a preliminary ruling	Joint Communication from the United States, the European Union, and Mexico to the Request for a Preliminary Ruling submitted by China, 21 April 2010
<i>Customs Law</i>	Customs Law of the People's Republic of China, adopted at the 19th Meeting of the Standing Committee of the Sixth National People's Congress on 22 January 1987, amended 8 July 2000 (Panel Exhibits CHN-14 and JE-68)
DSB	Dispute Settlement Body
DSU	<i>Understanding on Rules and Procedures Governing the Settlement of Disputes</i>
EU Panel Report	Panel Report, <i>China – Measures Related to the Exportation of Various Raw Materials</i> , complaint by the European Union (WT/DS395/R)
<i>Export Quota Administration Measures</i>	Measures for the Administration of Export Commodities Quotas, Order No. 12, promulgated by MOFTEC (now MOFCOM) on 20 December 2001 (Panel Exhibits CHN-312 and JE-76)
<i>Export Quota Bidding Implementation Rules</i>	Implementation Rules of Export Quota Bidding for Industrial Products, Ministry of Foreign Trade and Economic Cooperation, 8 November 2001 (Panel Exhibits CHN-305 and JE-78)
<i>Export Quota Bidding Measures</i>	Measures of Quota Bidding for Export Commodities, Decree of the Ministry of Foreign Trade and Economic Cooperation No. 11, adopted at the 9th ministerial office meeting of the Ministry of Foreign Trade and Economic Co-operation, 1 January 2002 (Panel Exhibits CHN-304 and JE-77)
GATS	<i>General Agreement on Trade in Services</i>
GATT 1994	<i>General Agreement on Tariffs and Trade 1994</i>
<i>Import Licensing Agreement</i>	<i>Agreement on Import Licensing Procedures</i>
MEP	minimum export price
Mexico Panel Report	Panel Report, <i>China – Measures Related to the Exportation of Various Raw Materials</i> , complaint by Mexico (WT/DS398/R)
MOFCOM	Ministry of Commerce of the People's Republic of China
MOFTEC	Ministry of Trade and Economic Cooperation of the People's Republic of China
Panel	Panel in <i>China – Measures Related to the Exportation of Various Raw Materials</i>

Abbreviation	Definition
Panel's preliminary ruling (first phase)	First phase of the Preliminary Ruling by the Panel dated 7 May 2010, Panel Reports, Annex F-1
Panel's preliminary ruling (second phase)	Second phase of the Preliminary Ruling by the Panel dated 1 October 2010, Panel Reports, Annex F-2
Panel Reports	Panel Reports, <i>China – Measures Related to the Exportation of Various Raw Materials</i> , WT/DS394/R/WT/DS395/R/WT/DS398
Raw materials	Certain forms of bauxite, coke, fluorspar, magnesium, manganese, silicon carbide, silicon metal, yellow phosphorous, and zinc
<i>Regulation on Import and Export Administration</i>	Regulation of the People's Republic of China on the Administration of the Import and Export of Goods, passed at the forty-sixth executive meeting of the State Council on 31 October 2001, 1 January 2002 (Panel Exhibits CHN-152 and JE-73)
<i>Regulations on Import and Export Duties</i>	Regulations of the People's Republic of China on Import and Export Duties, Order of the State Council (2003) No. 392, adopted at the 26th executive meeting of the State Council on 29 October 2003, 1 January 2004 (Panel Exhibits CHN-13 and JE-67)
SPS Agreement	<i>Agreement on the Application of Sanitary and Phytosanitary Measures</i>
TBT Agreement	<i>Agreement on Technical Barriers to Trade</i>
TRIMS Agreement	<i>Agreement on Trade-Related Investment Measures</i>
TRIPS Agreement	<i>Agreement on Trade-Related Aspects of Intellectual Property Rights</i>
US Panel Report	Panel Report, <i>China – Measures Related to the Exportation of Various Raw Materials</i> , complaint by the United States (WT/DS394/R)
<i>Vienna Convention</i>	<i>Vienna Convention on the Law of Treaties</i> , done at Vienna, 23 May 1969, 1155 UNTS 331; 8 International Legal Materials 679.
<i>Working Procedures</i>	<i>Working Procedures for Appellate Review</i> , WT/AB/WP/6, 16 August 2010
WTO	World Trade Organization
<i>WTO Agreement</i>	<i>Marrakesh Agreement Establishing the World Trade Organization</i>

WORLD TRADE ORGANIZATION
APPELLATE BODY

**China – Measures Related to the Exportation of
Various Raw Materials**

AB-2011-5

Present:

China, *Appellant, Appellee*
United States, *Other Appellant, Appellee*
European Union¹, *Other Appellants, Appellee*
Mexico, *Other Appellant, Appellee*

Ramirez-Hernández, Presiding Member
Hillman, Member
Oshima, Member

Argentina, *Third Participant*
Brazil, *Third Participant*
Canada, *Third Participant*
Chile, *Third Participant*
Colombia, *Third Participant*
Ecuador, *Third Participant*
India, *Third Participant*
Japan, *Third Participant*
Korea, *Third Participant*
Norway, *Third Participant*
Saudi Arabia, *Third Participant*
Separate Customs Territory of Taiwan, Penghu,
Kinmen and Matsu, *Third Participant*
Turkey, *Third Participant*

I. Introduction

1. China and the United States each appeals certain issues of law and legal interpretations developed in the Panel Report, *China – Measures Related to the Exportation of Various Raw Materials, Complaint by the United States* (WT/DS394/R) (the "US Panel Report"); China and the

¹This dispute began before the entry into force of the *Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community* (done at Lisbon, 13 December 2007) on 1 December 2009. On 29 November 2009, the World Trade Organization (the "WTO") received a Verbal Note (WT/L/779) from the Council of the European Union and the Commission of the European Communities stating that, by virtue of the *Treaty of Lisbon*, as of 1 December 2009, the "European Union" replaces and succeeds the "European Community". On 13 July 2010, the WTO received a second Verbal Note (WT/L/et/679) from the Council of the European Union confirming that, with effect from 1 December 2009, the European Union replaced the European Community and assumed all the rights and obligations of the European Community in respect of all Agreements for which the Director-General of the World Trade Organization is the depositary and to which the European Community is a signatory or a contracting party. We understand the reference in the Verbal Notes to the "European Community" to be a reference to the "European Communities". Thus, although the European Communities was a party in the Panel proceedings, it is the European Union that filed a Notice of Appeal in this dispute after the entry into force of the *Treaty of Lisbon*, and we will thus refer to the European Union in this Report in its capacity as appellee and other appellant.

European Union each appeals certain issues of law and legal interpretations developed in the Panel Report, *China – Measures Related to the Exportation of Various Raw Materials, Complaint by the European Union* (WT/DS395/R) (the "EU Panel Report"); and China and Mexico each appeals certain issues of law and legal interpretations developed in the Panel Report, *China – Measures Related to the Exportation of Various Raw Materials, Complaint by Mexico* (WT/DS398/R) (the "Mexico Panel Report") (collectively, the "Panel Reports").² The Panel was established to consider complaints by the United States³, the European Union⁴, and Mexico⁵ (the "complainants") regarding the consistency of certain measures imposed by China on the exportation of certain forms of bauxite, coke, fluorspar, magnesium, manganese, silicon carbide, silicon metal, yellow phosphorous, and zinc⁶ (the "raw materials") with the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994"), the Protocol on the Accession of the People's Republic of China⁷ ("China's Accession Protocol"), and the Report of the Working Party on the Accession of China⁸ ("China's Accession Working Party Report").

2. Before the Panel, the complainants challenged four types of restraints imposed by China on the exportation of the raw materials: (i) export duties; (ii) export quotas; (iii) export licensing; and (iv) minimum export price requirements.⁹ The complainants also challenged certain aspects of China's allocation and administration of export quotas, export licences, and minimum export prices, as well as the alleged non-publication of certain export measures.¹⁰ The complainants alleged that these export restraints were inconsistent with China's commitments under China's Accession Protocol and China's Accession Working Party Report, and with Articles VIII:1(a), VIII:4, X:1, X:3(a), and XI:1 of the GATT 1994.

²WT/DS394/R; WT/DS395/R; WT/DS398/R, 5 July 2011 (collectively, the "Panel Reports"). At its meeting on 21 December 2009, the Dispute Settlement Body (the "DSB") established a single Panel for all three complaints in accordance with Article 9.1 of the DSU (WT/DSB/M/277). Pursuant to a joint request by the United States and Mexico, the Panel issued its findings in the form of a single document containing three separate reports, with common descriptive and analytical sections, but separate conclusions and recommendations for each complaining party, each of which bears only the document symbol for that report. (Panel Reports, paras. 6.74 and 8.1) In our Reports, when referring to more than one of the complainants, we mostly refer to the United States first, then to the European Union, and then to Mexico, in keeping with the chronology of the DS numbers assigned to these disputes.

³Request for the Establishment of a Panel by the United States, WT/DS394/7.

⁴Request for the Establishment of a Panel by the European Communities, WT/DS395/7.

⁵Request for the Establishment of a Panel by Mexico, WT/DS398/6.

⁶Further details regarding the products at issue in this dispute are provided in paragraph 2.2 of the Panel Reports.

⁷WT/L/432.

⁸WT/ACC/CHN/49 and Corr. 1.

⁹Panel Reports, para. 2.1.

¹⁰Panel Reports, para. 2.1.

3. On 30 March 2010, China requested a preliminary ruling by the Panel regarding the consistency of the complainants' panel requests¹¹ with the requirements of Article 6.2 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"). In particular, China alleged that the complainants' panel requests: (i) did not clearly and specifically identify which measures were being challenged and for which raw materials; and (ii) failed to provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly, because the measures identified in Section III of each of the panel requests were not plainly connected to the list of treaty provisions that the complainants claimed were being infringed. The Panel issued its preliminary ruling in two phases.¹² With the exception of one claim by the European Union, the Panel found the complainants' panel requests sufficient to comply with Article 6.2 of the DSU.¹³

4. As regards the substantive claims raised by the complainants, the Panel addressed each of the four types of export restraints imposed by China, as well as aspects of the administration and application of certain export measures. The Panel first considered whether the export duties imposed by China on certain forms of bauxite, coke, fluorspar, magnesium, manganese, silicon metal, yellow phosphorous, and zinc were inconsistent with Paragraph 11.3 of China's Accession Protocol. Paragraph 11.3 requires the elimination of all taxes and charges applied to exports, except as specifically provided for in Annex 6 to the Protocol or as applied in conformity with Article VIII of the GATT 1994. The Panel found that, with the exception of yellow phosphorous, none of the raw materials at issue is listed in Annex 6, and thus the materials are not exempt from the requirement to eliminate export duties. With respect to yellow phosphorous, the Panel found that the 50-per cent duty imposed on exports of yellow phosphorous, challenged by the complainants, had been removed prior to the establishment of the Panel, and therefore did not make findings with regard to that duty.¹⁴

5. In its defence, China contended that the export duties on certain forms of coke, fluorspar, magnesium, manganese, and zinc were justified under Article XX(b) and (g) of the GATT 1994 because these raw materials were exhaustible natural resources, or because the duties were applied in

¹¹See *supra*, footnotes 3-5.

¹²The first phase of the preliminary ruling was issued to the parties on 7 May 2010 and circulated to WTO Members on 18 May 2010 as document WT/DS394/9, WT/DS395/9, WT/DS396/8 ("Panel's preliminary ruling (first phase)"). The second phase of the preliminary ruling was issued to the parties on 1 October 2010 and, at the request of the United States and Mexico, circulated only to the third parties ("Panel's preliminary ruling (second phase)"). The first and second phases of the preliminary ruling were attached as Annexes F-1 and F-2 to the Panel Reports. (See Panel Reports, paras. 1.12 and 1.13)

¹³Panel Reports, paras. 7.1-7.3.

¹⁴Panel Reports, sections VII.B.1-VII.B.4.

order to reduce pollution and to protect human health.¹⁵ However, the Panel found that China could not invoke exceptions under Article XX to justify measures found to be inconsistent with Paragraph 11.3 of China's Accession Protocol, because these exceptions apply only to violations of the GATT 1994, unless specifically incorporated into a non-GATT provision or instrument. The Panel found that Paragraph 11.3 of China's Accession Protocol does not contain any language or reference that would allow recourse to Article XX of the GATT 1994 for justifying China's export duties found to be inconsistent with Paragraph 11.3.¹⁶ Even assuming, *arguendo*, that the exceptions under Article XX(b) and (g) were available to China under Paragraph 11.3 of its Accession Protocol, the Panel found that China had failed to satisfy the requirements of those provisions for the raw materials at issue.¹⁷

6. With regard to export quotas, the Panel found that the quotas imposed on certain forms of bauxite, coke, fluorspar, silicon carbide, and zinc are inconsistent with Article XI:1 of the GATT 1994. In addressing China's defence that the export quota applied to one form of bauxite known as "refractory-grade bauxite"¹⁸ is justified under Article XI:2(a) of the GATT 1994, the Panel found that the export quota had not been "temporarily applied" in order to "prevent or relieve a critical shortage" of refractory-grade bauxite within the meaning of Article XI:2(a).¹⁹ The Panel also found that China had not demonstrated that its export quotas on refractory-grade bauxite, coke, and silicon carbide were justified under Article XX(b) or (g) of the GATT 1994.²⁰

7. Next, the Panel addressed certain aspects of China's administration and allocation of its export quotas. The Panel found that the export performance and minimum registered capital requirements imposed by China on the allocation of certain export quotas are inconsistent with China's "trading

¹⁵China did not seek to justify under Article XX the export duties imposed on bauxite, other forms of manganese, or silicon metal.

¹⁶Panel Reports, section VII.B.5.

¹⁷Panel Reports, sections VII.D.2-VII.D.4.

¹⁸We note that the complainants and the Panel sometimes referred to this form of bauxite as "high alumina clay". We will refer to this material throughout these Reports as "refractory-grade bauxite".

¹⁹Panel Reports, section VII.D.1.

²⁰Panel Reports, sections VII.D.2-VII.D.4. The Panel found that China had not demonstrated that its export quotas on coke and silicon carbide are necessary within the meaning of Article XX(b) of the GATT 1994. (*Ibid.*, para. 7.615) The Panel also found that China had not demonstrated that its export quota on refractory-grade bauxite relates to the conservation of exhaustible natural resources and was made effective in conjunction with restrictions on domestic production or consumption pursuant to Article XX(g) of the GATT 1994. (*Ibid.*, para. 7.613) China does not appeal these findings by the Panel. We also note that, before the Panel, China did not seek to justify under Article XX the quotas imposed on other forms of bauxite, fluorspar, or zinc.

rights" obligations under its Accession Protocol and Accession Working Party Report.²¹ The Panel, however, rejected the claim that China's prior export performance requirement operates to the detriment and exclusion of foreign enterprises.²² Furthermore, the Panel found that China's allocation of export quotas through the use of an "operation capacity" criterion contained in Article 19 of China's Measures for the Administration of Export Commodities Quotas²³ ("*Export Quota Administration Measures*") is inconsistent with Article X:3(a) of the GATT 1994, because the lack of any definition, guidelines, or standards on how to apply this criterion necessarily results in unreasonable and non-uniform administration.²⁴ The Panel also found that China has acted inconsistently with Article X:1 of the GATT 1994 because it failed to publish promptly the total amount and procedure for the allocation of export quotas for zinc.²⁵ The Panel rejected the claim by the United States and Mexico that China's administration of its export quotas through the involvement of China's Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters (the "CCCMC") results in partial or unreasonable administration inconsistent with Article X:3(a) of the GATT 1994.²⁶ The Panel also rejected the claims by the United States and Mexico that China's allocation of export quotas for certain forms of bauxite, fluorspar, and silicon carbide through a quota-bidding process, based on a "bid-winning price", is inconsistent with Article VIII:1(a) of the GATT 1994 and Paragraph 11.3 of China's Accession Protocol.²⁷

8. Regarding China's export licensing system for certain forms of bauxite, coke, fluorspar, manganese, silicon carbide, and zinc, the Panel found that the system is not *per se* inconsistent with China's obligations under Article XI:1 of the GATT 1994.²⁸ However, the Panel found that China's export licensing authorities had the discretion to request undefined "other" documents or materials from enterprises applying for such licences, and that this creates uncertainty and constitutes an export restriction prohibited under Article XI:1.²⁹ The Panel declined to make findings on other claims

²¹Specifically, the Panel found China's prior export performance and minimum registered capital requirements to be inconsistent with Paragraphs 1.2 and 5.1 of China's Accession Protocol, read with Paragraphs 83(a), 83(b), 83(d), 84(a), and 84(b) of China's Accession Working Party Report. (Panel Reports, paras. 7.657-7.670)

²²The Panel concluded that China's prior export performance requirement is not inconsistent with Paragraph 5.2 of China's Accession Protocol, read with Paragraphs 84(a) and 84(b) of China's Accession Working Party Report. (Panel Reports, paras. 7.671-7.677)

²³Measures for the Administration of Export Commodities Quotas, Order No. 12, promulgated by MOFTEC (now MOFCOM) on 20 December 2001 (Panel Exhibits CHN-312 and JE-76).

²⁴Panel Reports, paras. 7.746 and 7.752.

²⁵Panel Reports, para. 7.807.

²⁶Panel Reports, paras. 7.787 and 7.796.

²⁷Panel Reports, paras. 7.851 and 7.860.

²⁸Panel Reports, para. 7.938.

²⁹Panel Reports, para. 7.948.

regarding China's export licensing system.³⁰ In addition, the Panel found that China imposes a requirement to export at a coordinated minimum export price ("MEP") certain forms of bauxite, coke, fluorspar, magnesium, silicon carbide, yellow phosphorous, and zinc that also constitutes a prohibited export restriction under Article XI:1. The Panel also found that, by failing to publish promptly measures through which it administers its MEP requirement, China has acted inconsistently with its obligations under Article X:1 of the GATT 1994.³¹ The Panel, however, declined to make a finding on whether China's administration of the MEP requirement alleged to apply to yellow phosphorous is inconsistent with its obligations under Article X:3(a) of the GATT 1994.³²

9. On 31 August 2011, China notified the Dispute Settlement Body (the "DSB") of its intention to appeal certain issues of law covered in the Panel Reports and certain legal interpretations developed by the Panel, pursuant to Articles 16.4 and 17 of the DSU, and filed a Notice of Appeal³³ and an appellant's submission pursuant to Rules 20 and 21, respectively, of the *Working Procedures for Appellate Review*³⁴ (the "*Working Procedures*").

10. On 1 September 2011, the United States, the European Union, and Mexico requested the Appellate Body Division hearing these appeals to extend certain time periods for filing submissions. In their joint request, the complainants referred to Rule 16(2) of the *Working Procedures* and the extensive nature of China's appeal. The complainants also indicated that they wished to coordinate their efforts and submissions to the greatest extent possible. On the same day, the Division invited China and the third participants to comment on the complainants' request. Written comments were received from China, Japan, and Saudi Arabia on 2 September 2011.³⁵ On the same day, the Division informed the participants and third participants that it had decided to extend the deadline for the filing

³⁰The Panel declined to make a finding on whether China's export licensing system for certain forms of bauxite, coke, fluorspar, manganese, silicon carbide, and zinc is inconsistent with Paragraphs 162 and 165 of China's Accession Working Party Report and Paragraph 1.2 of China's Accession Protocol. (Panel Reports, paras. 7.960-7.973) The Panel also declined to make a finding regarding the inconsistency of China's export licensing system for certain forms of bauxite, coke, fluorspar, manganese, silicon carbide, and zinc with Paragraphs 83 and 84 of China's Accession Working Party Report and Paragraphs 1.2 and 5.1 of China's Accession Protocol. (*Ibid.*, paras. 7.974-7.983)

³¹Panel Reports, paras. 7.1088-7.1102.

³²Panel Reports, paras. 7.1083-7.1087.

³³WT/DS394/11, WT/DS395/11, WT/DS398/10 (attached as Annex IV to these Reports).

³⁴WT/AB/W/P/6, 16 August 2010.

³⁵China informed the Division that it opposed the complainants' request. China argued, *inter alia*, that the length of its appeal did not justify a departure from the deadlines contained in the *Working Procedures* for the filing of other appellants' or appellees' submissions. Japan and Saudi Arabia indicated that they had no objection to the extension of time-limits requested by the complainants. They asked, however, that additional time also be granted to third participants for the filing of their submissions, in the event that the Division were to decide to grant additional time to the participants. No other third participants submitted comments to the Division.

of any Notice of Other Appeal and other appellant's submission until 6 September 2011; the deadline for the filing of the complainants' appellees' submissions until 22 September 2011; the deadline for the filing of China's appellee's submission until 26 September 2011; and the deadline for the filing of third participants' submissions and notifications until 29 September 2011.

11. On 6 September 2011, the United States, the European Union, and Mexico each notified the DSB of its intention to appeal certain issues of law and certain legal interpretations developed by the Panel in Panel Reports WT/DS394/R, WT/DS395/R, and WT/DS398/R, respectively, pursuant to Articles 16.4 and 17 of the DSU, and filed a Notice of Other Appeal³⁶ and an other appellant's submission pursuant to Rules 23(1) and (3) and 26(2) of the *Working Procedures*. On 22 September 2011, the United States and Mexico filed a joint appellees' submission³⁷ and the European Union filed an appellee's submission.³⁸ On 26 September 2011, China filed an appellee's submission.³⁹

12. On 28 September 2011, Colombia filed a third participant's submission.⁴⁰ On the same day, Ecuador notified its intention to appear at the oral hearing as a third participant.⁴¹ On 29 September 2011, Brazil, Canada, Japan, Korea, Saudi Arabia, and Turkey each filed a third participant's submission.⁴² On the same day, Argentina, Chile, India, and Norway each notified its intention to appear at the oral hearing as a third participant.⁴³ On 2 November 2011, the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu also notified the Secretariat of its intention to appear at the oral hearing as a third participant.⁴⁴

13. On 29 October 2011, the Chair of the Appellate Body informed the Chair of the DSB that, due to the significant size, scope, and timing of this appeal and the demands that it, along with the two other appeals under review, placed on the Appellate Body and translation services, the

³⁶WT/DS394/12; WT/DS395/12; WT/DS398/11 (attached as Annexes V, VI, and VII to these Reports, respectively).

³⁷Pursuant to Rules 22, 23(4), and 26(2) of the *Working Procedures*.

³⁸Pursuant to Rules 22, 23(4), and 26(2) of the *Working Procedures*.

³⁹Pursuant to Rules 22, 23(4), and 26(2) of the *Working Procedures*.

⁴⁰Pursuant to Rules 24(1) and 26(2) of the *Working Procedures*.

⁴¹Pursuant to Rules 24(2) and 26(2) of the *Working Procedures*.

⁴²Pursuant to Rules 24(1) and 26(2) of the *Working Procedures*.

⁴³Pursuant to Rules 24(2) and 26(2) of the *Working Procedures*.

⁴⁴On 2 November 2011, the Separate Customs Territory of Taiwan, Penghu, Kinmen and Matsu submitted its delegation list for the oral hearing to the Appellate Body Secretariat and the participants and third participants in this dispute. For the purpose of this appeal, we have interpreted this action as a notification expressing its intention to attend the oral hearing pursuant to Rule 24(4) of the *Working Procedures*.

Appellate Body Report in this appeal would be circulated to WTO Members no later than 31 January 2012.⁴⁵

14. On 1 November 2011, China requested an extension of the time allocated for its opening statement at the oral hearing. On the same day, the Division invited the other participants and the third participants to comment on China's request. Written comments were submitted by the United States, the European Union, and Mexico on 2 November 2011.⁴⁶ By letter of 3 November 2011, the Division informed the participants and third participants that it considered the time allocated for opening statements to reflect an appropriate balance in the light of the high number of participants and third participants in the dispute and the time required in order to provide the participants and third participants with a full opportunity to respond to questions that would be posed by the Division at the oral hearing. Consequently, the Division decided not to adjust the amount of time it had allocated to the participants for their opening statements at the oral hearing.

15. The oral hearing in this appeal was held on 7-9 November 2011. The participants and 11 of the third participants—Brazil, Canada, Chile, Colombia, Ecuador, India, Japan, Korea, Norway, Saudi Arabia, and Turkey—made oral statements. The participants and third participants responded to questions posed by the Members of the Appellate Body Division hearing the appeal.

II. Arguments of the Participants and the Third Participants

A. *Claims of Error by China – Appellant*

1. Article 6.2 of the DSU

16. China requests the Appellate Body to reverse the Panel's finding that Section III of each of the complainants' panel requests, entitled "Additional Restraints Imposed on Exportation", complies with the requirements of Article 6.2 of the DSU, and to find, instead, that Section III of the panel requests does not comply with Article 6.2, with the exception of the complainants' claims regarding the non-publication of export measures concerning zinc.⁴⁷ Consequently, China requests the

⁴⁵WT/DS394/13, WT/DS395/13, WT/DS398/12.

⁴⁶The United States, the European Union, and Mexico opposed China's request for additional time. They submitted that the time allocated to China was greater than in other appeals involving multiple complainants, and was also already proportionally greater than that given to other participants in situations comparable to that of China in this dispute.

⁴⁷China's appellant's submission, para. 5 (referring to Panel's preliminary ruling (second phase), Panel Reports, Annex F-2, para. 77; and Panel Reports, para. 7.3(b)).

Appellate Body to reverse the Panel's findings made pursuant to other claims allegedly contained in Section III of the panel requests.⁴⁸

17. China contends that the Panel correctly concluded that the panel requests set out subsets of claims concerning subsets of measures, rather than raising all claims listed in Section III of the panel requests in relation to all measures listed in that section of the panel requests. However, the panel requests fail to identify which claims were made with respect to which measures. For China, in order to comply with Article 6.2 of the DSU, the complainants were required plainly to connect the 37 listed measures with the 13 listed treaty provisions with sufficient precision to identify the specific combination of measure(s) and claim(s) at issue.

18. China explains that subsequent submissions by the complainants reveal substantial differences between the United States and Mexico, on the one hand, and the European Union, on the other hand, with respect to the specific combination of measures and claims at issue. Therefore, while the panel requests are nearly identical, the "problems" presented in the three panel requests are considerably different, thus giving the misleading impression that the three complainants referred the same matter to the DSB, when in reality the matters are different.

19. Furthermore, China alleges that the Panel found that the panel requests comply with Article 6.2 not on the basis of the panel requests themselves, but, rather, on additional information contained in subsequent submissions by the parties. China submits that this amounts to legal error, because, as found by the Appellate Body in *EC and certain member States – Large Civil Aircraft*, Article 6.2 requires that a panel request, as it existed at the time of filing, comply with Article 6.2, and that a party's submissions during a panel proceeding cannot cure a defect in a panel request.⁴⁹ China alleges that the Panel, rather than respecting these findings, instead encouraged the complainants to correct defects in the panel requests in subsequent submissions.⁵⁰

20. China contends that the Panel observed defects in Section III of the panel requests, and points to several features of the Panel's reasoning that, in China's view, demonstrate that the Panel itself recognized that the panel requests did not provide the necessary connection between the 37 listed measures and the 13 listed treaty provisions. First, the Panel did not accept the complainants'

⁴⁸Referring specifically to the findings in the Panel Reports in paragraphs 7.669, 7.670, 7.678, 7.756, 7.807, 7.958, 7.1082, 7.1102, 7.1103, 8.4(a)-(b), 8.5(b), 8.6(a)-(b), 8.11(a), (c), (e), and (f), 8.12(b), 8.13(a)-(b), 8.18(a)-(b), 8.19(b), and 8.20(a)-(b).

⁴⁹China's appellant's submission, para. 65 (referring to Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 642).

⁵⁰China's appellant's submission, para. 66.

argument that there was no need to establish any connection between the measures and the claims. Second, in the first phase of its preliminary ruling, the Panel requested the complainants to clarify which of the listed measures were alleged to be inconsistent with which specific WTO obligation. Third, the Panel requested again, after the first Panel meeting with the parties, that the complainants clarify which specific WTO provision(s) each of the measures was allegedly violating. Finally, the Panel pointed to no language in the panel requests that indicated that the complainants had in fact established the connection, but instead relied on the complainants' subsequent submissions as the basis for its finding that the panel requests comply with Article 6.2.

21. China further argues that, although the Panel stated that the complainants' first written submissions provided "sufficient connections" between the measures and the claims at issue, the complainants in fact provided the connections only in their response to Panel Question 2 following the first Panel meeting. The Panel expressly acknowledged this fact when it noted that, in their first written submissions, the complainants failed to "directly address" the connections between the measures and claims at issue.⁵¹ Instead, submits China, all three examples listed by the Panel to illustrate that the complainants had in fact connected the measures and claims at issue are taken from the complainants' response to Panel Question 2 after the first Panel meeting, and not from the panel requests or the first written submissions.

22. Finally, China claims that the Panel frustrated China's due process rights under Article 6.2 of the DSU, in particular, China's right to begin preparing its defence on the basis of the panel requests and its right to have the scope of the dispute unaltered during the course of the proceedings. China argues that, with respect to the claims listed in Section III of the panel requests, it was impossible for China to begin preparing its defence when the panel requests were filed, because the measures implicated by the different narrative paragraphs, and the claims made regarding those measures, could not be identified.

2. The Panel's Recommendations

23. On appeal, China seeks review of the Panel's recommendations concerning export duties and export quotas "to the extent that [these] recommendations apply to annual replacement measures" adopted after the establishment of the Panel on 21 December 2009.⁵² China argues that the complainants had excluded such measures from the scope of the dispute and hence, by making

⁵¹China's appellant's submission, para. 74 (referring to Panel's preliminary ruling (second phase), Panel Reports, Annex F-2, para. 32).

⁵²China's appellant's submission, paras. 99 and 136.

recommendations extending to such measures, the Panel acted inconsistently with its obligations under Article 7.1 of the DSU; failed to make an objective assessment of the matter under Article 11 of the DSU; and made recommendations on measures that were not part of the matter before it, inconsistently with Article 19.1 of the DSU.

24. China highlights that, under Article 7.1 of the DSU, a panel must respect the mandate conferred upon it through its terms of reference. This conclusion has been "consistently repeated" by panels and the Appellate Body⁵³, and it is well established that "panels 'cannot assume jurisdiction that [they] do not have'."⁵⁴ Although, typically, a panel's terms of reference are established by a panel request, a complainant can limit the panel's terms of reference in several ways—for example, by withdrawing a claim regarding a measure or by abandoning a complaint entirely. In the present dispute, the complainants' decision to abandon certain of their claims meant that the Panel could not make recommendations regarding such claims. In China's view, the Panel acted inconsistently with Article 7.1 of the DSU by permitting the complainants to "evade" the consequences of their own decision to withdraw annual replacement measures from the scope of the dispute.⁵⁵

25. China further submits that, by making recommendations regarding annual replacement measures, the Panel failed to make an objective assessment of the matter before it as required under Article 11 of the DSU. When a panel makes recommendations regarding measures that are not a part of the "matter" before it, it confers an "advantage" on the complainant, in that it benefits from recommendations regarding measures that it did not challenge, and places the respondent at a "disadvantage", by subjecting it to implementation obligations regarding measures that were not within the scope of the dispute.⁵⁶ China asserts that such an approach lacks the "objectivity" required under Article 11.⁵⁷

26. China further argues that, in making recommendations regarding the "series of measures" with a prospective life extended through annual replacement measures, the Panel acted inconsistently with Article 19.1 of the DSU.⁵⁸ In China's view, there is a textual link between a panel's terms of

⁵³China's appellant's submission, para. 137 (referring to Appellate Body Report, *Chile – Price Band System*, para. 168; Appellate Body Report, *India – Patents (US)*, para. 92; Appellate Body Report, *US – Carbon Steel*, paras. 172-174; Panel Report, *US – Continued Zeroing*, para. 7.63; and Appellate Body Report, *US – Gambling*, para. 281).

⁵⁴China's appellant's submission, para. 137 (referring to Appellate Body Report, *India – Patents (US)*, para. 92).

⁵⁵China's appellant's submission, paras. 141-143. (emphasis omitted)

⁵⁶China's appellant's submission, paras. 145 and 146.

⁵⁷China's appellant's submission, para. 146.

⁵⁸China's appellant's submission, para. 153.

reference under Article 7.1, its duty to make an objective assessment under Article 11, and its authority to make recommendations under Article 19.1. Specifically, the measures that may be the subject of recommendations under Article 19.1 are the same measures to which Articles 7.1 and 11 refer, that is, the measures included in the panel's terms of reference. China highlights that the Panel made recommendations regarding a "so-called 'series of measures'", attributing to this concept an "ongoing legal character stretching into the future", despite the fact that the complainants had argued that no recommendations could or should be made regarding annual replacement measures. China also notes that the complainants never argued that the export duty and export quota measures at issue in this dispute have prospective application through annual replacement measures.⁵⁹

27. China also takes issue with the Panel's conclusion that it could make recommendations extending to annual replacement measures in order to "ensure that the dispute settlement system functions efficiently in resolving disputes".⁶⁰ Referring to Articles 3.4 and 3.7 of the DSU, the Panel was "concerned" that, if it did not address annual replacement measures, it would not effectively resolve the dispute.⁶¹ However, since the complainants had decided to exclude annual replacement measures from the dispute, there was no dispute to resolve regarding annual replacement measures. Past disputes, including *US – Continued Zeroing*, show that the WTO dispute settlement system is "perfectly effective" in resolving disputes regarding measures with general and prospective application.⁶² China asserts that there is a crucial difference between such disputes and the present one, in which the complainants "actively decided to exclude" annual replacement measures from the dispute.⁶³ Since the complainants were "well aware" that they could pursue a claim against annual replacement measures, but chose not to, the complainants must bear the consequences of their decision.⁶⁴

3. Applicability of Article XX of the GATT 1994

28. China alleges various errors in the Panel's analysis and requests the Appellate Body to reverse the Panel's finding that China may not seek to justify export duties found to be inconsistent with Paragraph 11.3 of China's Accession Protocol pursuant to Article XX of the GATT 1994. Specifically, China contends that the Panel erred in determining that there is "no textual basis" in China's Accession Protocol for its right to invoke Article XX in defence of a claim under

⁵⁹China's appellant's submission, para. 152.

⁶⁰China's appellant's submission, para. 160 (quoting Panel Reports, para. 7.30).

⁶¹China's appellant's submission, para. 161.

⁶²China's appellant's submission, para. 164.

⁶³China's appellant's submission, para. 165. (emphasis omitted)

⁶⁴China's appellant's submission, para. 166.

Paragraph 11.3.⁶⁵ According to China, the Panel's finding that Paragraph 11.3 excludes recourse to Article XX of the GATT 1994 was based on the Panel's erroneous assumption that the absence of language expressly granting the right to regulate trade in a manner consistent with Article XX means that China and other Members intended to deprive China of that right.

(a) Paragraph 11.3 of China's Accession Protocol

29. China observes that Paragraph 11.3 of its Accession Protocol requires that it eliminate export taxes and charges, unless they are specifically provided for in Annex 6 thereto or applied consistently with Article VIII of the GATT 1994. As such, the obligation under Paragraph 11.3 is first "qualified" by Annex 6 of China's Accession Protocol, which provides a schedule of the maximum export duty rates applicable to 84 products, along with a Note that "sets forth an exception to China's obligations regarding export duties".⁶⁶ At the Panel stage, the European Union claimed that China had violated its obligations under Annex 6 "by failing to consult with affected Members prior to the imposition of export duties on particular forms of bauxite, coke, fluorspar, magnesium, manganese, silicon metal and zinc, none of which is among the 84 listed products in Annex 6".⁶⁷ China further emphasizes that the Panel ruled in favour of the European Union, concluding that China has acted inconsistently with its obligations under Annex 6 because it failed to consult with other affected WTO Members prior to imposing export duties on these products.⁶⁸ Highlighting that none of the products subject to the European Union's claim is included in the Annex 6 schedule, China argues that the European Union's claim and the Panel's ruling necessarily mean that "the exception in Annex 6 permits China to impose export duties on all products, provided there are 'exceptional circumstances', and that China consults with affected Members."⁶⁹

30. China argues that the reference to "exceptional circumstances" in the Note to Annex 6 demonstrates a "substantive overlap" between the scopes of the exceptions set forth in Annex 6 to China's Accession Protocol and Article XX of the GATT 1994, respectively.⁷⁰ Although the Note does not prescribe the specific circumstances in which the Annex 6 exception would apply, the ordinary meaning of "exceptional" establishes that these circumstances "must be unusual and

⁶⁵China's appellant's submission, para. 190.

⁶⁶China's appellant's submission, para. 212.

⁶⁷China's appellant's submission, para. 213 (referring to European Union's first written submission to the Panel, paras. 254, 258, 262, 266, 270, 274, 278, 282, 286, 290, 294, 298, 302, 306, and 310).

⁶⁸China's appellant's submission, para. 214.

⁶⁹China's appellant's submission, para. 215.

⁷⁰China's appellant's submission, para. 216.

special".⁷¹ China asserts that the circumstances provided in the various subparagraphs of Article XX are "exceptional" within the meaning of the Note to Annex 6 because they allow a Member to depart from an "affirmative obligation", and because the circumstances enumerated in Article XX "are both unusual and special".⁷² This demonstrates that the obligation to eliminate export duties is "not absolute" and "unqualified", and that China has "retained its inherent right to regulate trade using export duties to promote non-trade interests in 'exceptional circumstances'".⁷³ China adds that, by allowing China to adopt otherwise WTO-inconsistent export duties in "exceptional circumstances", the Note to Annex 6 demonstrates China's and other WTO Members' shared intent that China may have recourse to the "exceptional circumstances" set out in Article XX to justify export duties. China also argues that the Panel's finding that a "provision-specific" exception in Paragraph 11.3 of China's Accession Protocol precludes the applicability of Article XX is erroneous, because it is not "uncommon" to find provision-specific exceptions coupled with a right of recourse to more general exceptions, as in Article XI:2 of the GATT 1994.⁷⁴

31. China claims that the reference to Article VIII of the GATT 1994 in Paragraph 11.3 of its Accession Protocol confirms the applicability of Article XX of the GATT 1994. China reasons that Paragraph 11.3 requires that export taxes and charges be applied in conformity with the provisions of Article VIII of the GATT 1994. According to China, "[i]f they are not, the measure violates both Paragraph 11.3 and Article VIII."⁷⁵ For China, "[i]n the event that a measure violates Article VIII of the GATT 1994, it may, of course, be justified under Article XX of the GATT 1994", such that "[China] is not deprived of its right to justify a measure that violates Article VIII through recourse to Article XX simply because a complainant chooses to bring a claim under Paragraph 11.3" of China's Accession Protocol.⁷⁶ In China's view, the fact that Article VIII applies to certain export charges and fees covered by Paragraph 11.3, and not specifically to export duties, does not render the reference to Article VIII irrelevant, as the reference shows that the obligations under Paragraph 11.3 are not absolute and unqualified, and that China did not agree to abandon its right to resort to Article XX.

(b) Context from the *WTO Agreement*

32. China asserts that, by virtue of Paragraph 342 of China's Accession Working Party Report and Paragraph 1.2 of its Accession Protocol, Paragraph 170 of the Accession Working Party Report

⁷¹China's appellant's submission, para. 216.

⁷²China's appellant's submission, para. 218.

⁷³China's appellant's submission, para. 219. (emphasis omitted)

⁷⁴China's appellant's submission, para. 222.

⁷⁵China's appellant's submission, para. 224.

⁷⁶China's appellant's submission, paras. 224 and 225.

and Paragraph 11.3 of China's Accession Protocol are on an "equal legal footing", and are "integral parts" of the same accession agreement, as well as the *WTO Agreement*.⁷⁷ In China's view, the fact that the title of the subsection of China's Accession Working Party Report under which Paragraph 170 falls and the title of the provision that includes Paragraph 11.3 of its Accession Protocol are "exactly the same" provides a "powerful textual indication" that the subject matter of Paragraph 11.3 and Paragraph 170 overlap.⁷⁸ Since both provisions apply to "'taxes' and 'charges' on 'exports'", the use of identical language suggests that there is a "very considerable overlap" between the measures to which the provisions apply and that they impose "cumulative obligations" with respect to "taxes and charges".⁷⁹

33. Referring to the ordinary meaning of the terms "taxes" and "charges", and the substantive overlap between Paragraph 11.3 and Paragraph 170, China disagrees with the Panel's conclusion that Paragraph 170 does not apply to export duties, whereas Paragraph 11.3 does. In so finding, the Panel erred in relying on Paragraph 155 and Paragraph 156 of China's Accession Working Party Report, which, the Panel found, deal with export duties and do not incorporate Article XX of the GATT 1994. Unlike Paragraph 170, Paragraphs 155 and 156 are not incorporated into China's Accession Protocol and are, therefore, of "secondary importance" in interpreting the scope of China's obligations.⁸⁰

34. China also takes issue with the Panel's reasoning that Paragraph 170 does not apply to export duties because it applies to domestic taxes. China argues that, similar to Paragraph 11.3, Paragraph 170 refers to "'taxes' and 'charges' in relation to 'exports'", and that neither provision refers to "domestic" or "internal" taxes and charges.⁸¹ Although section IV.D of China's Accession Working Party Report, of which Paragraph 170 is a part, deals with "internal policies", the heading of the subsection under which Paragraph 170 falls (IV.D.1) is "Taxes and Charges Levied on Imports and Exports".⁸² Finally, China argues that Paragraph 171, dealing with subsidies contingent on exportation, shows that this subsection "may deal with" export duties.⁸³

35. China disagrees with the Panel's finding that Paragraph 170 essentially repeats the commitments existing under certain GATT 1994 rules. The text of Paragraph 170 indicates that its commitments therein extend to all of its "WTO obligations", including, but not limited to, those

⁷⁷China's appellant's submission, para. 230.

⁷⁸China's appellant's submission, para. 232. (emphasis omitted)

⁷⁹China's appellant's submission, para. 233. (emphasis omitted)

⁸⁰China's appellant's submission, para. 237.

⁸¹China's appellant's submission, para. 239. (original emphasis)

⁸²China's appellant's submission, para. 239. (emphasis omitted)

⁸³China's appellant's submission, para. 239.

imposed by the GATT 1994.⁸⁴ The phrase "WTO obligations" in Paragraph 170 includes obligations under Paragraph 11.3 of China's Accession Protocol. If export duties are inconsistent with its obligations under Paragraph 11.3, they are also inconsistent with Paragraph 170. Based on this observation, China argues that "any flexibilities that Paragraph 170 affords to China to adopt otherwise WTO-inconsistent export 'taxes' and 'charges' must extend equally to Paragraph 11.3."⁸⁵

36. China highlights that the Panel appeared "to agree that the language in Paragraph 170 permits recourse to Article XX", at least in the context of Paragraphs 11.1 and 11.2 of China's Accession Protocol.⁸⁶ Specifically, the Panel's findings that the inclusion of the phrase "shall be in conformity with the GATT 1994" in Paragraphs 11.1 and 11.2, and its "deliberate exclusion" in Paragraph 11.3, "reflected 'agreement'" that Article XX does not apply to Paragraph 11.3, are significant since they "demonstrate the Panel's acceptance" that such language incorporates Article XX.⁸⁷ However, in China's view, if such language can incorporate Article XX into Paragraphs 11.1 and 11.2, "the same language" in Paragraph 170 must also be "sufficient" to incorporate Article XX.⁸⁸ China asserts that a harmonious interpretation of Paragraph 11.3 and Paragraph 170 "dictates" that, if an export duty is in full conformity with China's obligations under Article XX pursuant to Paragraph 170, it "must also be in full conformity" with China's obligations under Paragraph 11.3.⁸⁹

37. China takes issue with the Panel's reasoning under which "China must eliminate export duties pursuant to Paragraph 11.3, even if these duties serve legitimate public health or conservation goals."⁹⁰ China argues that the Panel's approach is contrary to the text, context, and object and purpose of the *WTO Agreement* and "leads to an absurd outcome".⁹¹ Interpreting Paragraph 11.3 of China's Accession Protocol "to mean that China has abandoned the right to impose export duties in a manner consistent with Article XX of the GATT 1994, as the Panel did, is irreconcilable with the fact that", under Article XI:1, China can impose export quotas in a manner consistent with Article XX.⁹² China adds that, "[i]f the Panel's interpretation were accepted, China could not impose, for example, an export duty in a manner consistent with Article XX of the GATT 1994, whereas it could justify under Article XX an export quota on the same goods, and with equivalent trade restrictive and welfare

⁸⁴China's appellant's submission, para. 244.

⁸⁵China's appellant's submission, para. 246.

⁸⁶China's appellant's submission, para. 255. (emphasis omitted)

⁸⁷China's appellant's submission, paras. 256 and 257. (emphasis omitted)

⁸⁸China's appellant's submission, para. 257.

⁸⁹China's appellant's submission, para. 259.

⁹⁰China's appellant's submission, para. 268.

⁹¹China's appellant's submission, paras. 268 and 269.

⁹²China's appellant's submission, para. 269.

effects."⁹³ Further, the preamble of the *WTO Agreement* confirms that obligations in the covered agreements, such as Paragraph 11.3 of China's Accession Protocol, do not impose absolute prohibitions on the right to regulate trade. China considers that Members are entitled to regulate trade, for example, "through export duties, for the purpose of pursuing the objectives set forth in the Preamble, provided they do so in conformity with the requirements in Article XX of the GATT 1994".⁹⁴

(c) The Inherent Right to Regulate Trade

38. China argues that, "like any other State", it enjoys the right to regulate trade.⁹⁵ Referring to the Appellate Body report in *China – Publications and Audiovisual Products*, China asserts that such a right to regulate trade is an "inherent right" vested in States, and "not a right bestowed by international treaties such as the *WTO Agreement*".⁹⁶ China further argues that the preamble of the *WTO Agreement* recognizes that the WTO covered agreements, including China's Accession Protocol, "preserve the basic disciplines underlying the multilateral trading system, which includes respect for the inherent right to regulate trade".⁹⁷ In acceding to the WTO, Members agree to exercise their inherent right in conformity with disciplines set out in the covered agreements, either by complying with affirmative obligations or with the "obligations attaching to an exception, such as those included in Article XX".⁹⁸ China also refers to the texts of the first recital of the preamble of the *Agreement on the Application of Sanitary and Phytosanitary Measures* (the "*SPS Agreement*"), the sixth recital of the preamble of the *Agreement on Technical Barriers to Trade* (the "*TBT Agreement*"), the preamble of the *Agreement on Import Licensing Procedures* (the "*Import Licensing Agreement*"), the fourth recital of the preamble of the *General Agreement on Trade in Services* (the "*GATS*"), and the preamble and Article 8.1 of the *Agreement on Trade-Related Aspects of Intellectual Property Rights* (the "*TRIPS Agreement*") to argue that, by acceding to the WTO, Members preserve their right to regulate trade to achieve legitimate objectives.⁹⁹

39. In China's view, the appropriate interpretative question is whether Paragraph 11.3 of China's Accession Protocol explicitly excludes this right and not whether the language explicitly reaffirms this

⁹³China's appellant's submission, para. 269.

⁹⁴China's appellant's submission, para. 270.

⁹⁵China's appellant's submission, para. 275.

⁹⁶China's appellant's submission, para. 275 (quoting Appellate Body Report, *China – Publications and Audiovisual Products*, para. 222; and referring to Panel Report, *Argentina – Hides and Leather*, para. 11.98).

⁹⁷China's appellant's submission, para. 276.

⁹⁸China's appellant's submission, para. 278.

⁹⁹China's appellant's submission, para. 281.

right. China's Accession Protocol and Accession Working Party Report contain no language showing that China "abandon[ed]" its inherent right to regulate trade to promote fundamental non-trade objectives. Instead, its accession commitments "indicate" that it retains this right.¹⁰⁰ China emphasizes that its interpretation of Paragraph 11.3 does not mean that China can evade its WTO obligations, as it still must demonstrate compliance with the "conditions and limitations" of Article XX of the GATT 1994.¹⁰¹ According to China, the "suggestion" that an "inherent power" can be denied "unless expressly re-affirmed" is contrary to the "harmonious interpretation" of the covered agreements required by the Appellate Body.¹⁰² Moreover, "[a]ny such suggestion turns *inherent* rights into *acquired* rights, autonomy into *heteronomy*, and the *single* undertaking into a series of *detached* agreements".¹⁰³ China further alleges that the Panel's interpretation distorts the balance of rights and obligations that were established when China acceded to the WTO.

4. Article XI:2(a) of the GATT 1994

40. China requests the Appellate Body to reverse the Panel's interpretation and application of Article XI:2(a) of the GATT 1994 reached as part of the Panel's finding that China had not demonstrated that its export quota on refractory-grade bauxite is temporarily applied to prevent or relieve a critical shortage.¹⁰⁴ In particular, China alleges that the Panel erred in its interpretation and application of the term "temporarily" and in its interpretation of the term "critical shortages", because it effectively excluded from the scope of the provision export restrictions on non-renewable, exhaustible natural resources. In addition, China alleges that the Panel failed to make an objective assessment of the matter as required by Article 11 of the DSU.

41. First, with respect to the Panel's interpretation of the term "temporarily", China agrees with the Panel's finding that the word "temporarily" "suggest[s] a fixed time-limit for the application of a measure".¹⁰⁵ The Panel, however, subsequently "adjusted" its interpretation of the term "temporarily" to exclude the "long-term" application of export restrictions, by stating that Article XI:2(a) could not be interpreted "to permit the long-term application of ... export restrictions" or to "permit long-term

¹⁰⁰China's appellant's submission, para. 286.

¹⁰¹China's appellant's submission, para. 288.

¹⁰²China's appellant's submission, para. 291 (referring to Appellate Body Report, *Argentina – Footwear (EC)*, para. 81; Appellate Body Report, *India – Patents (US)*, para. 45; Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 12, DSR 1996:1, 97, at 106; Appellate Body Report, *Korea – Dairy*, para. 81; and Appellate Body Report, *US – Gasoline*, p. 25, DSR 1996:1, 3, at 23).

¹⁰³China's appellant's submission, para. 291. (original emphasis)

¹⁰⁴In particular, China refers to paragraphs 7.257, 7.258, 7.297-7.302, 7.305, 7.306, 7.346, 7.349, 7.351, 7.354, and 7.355 of the Panel Reports. (China's appellant's submission, paras. 299 and 388)

¹⁰⁵China's appellant's submission, para. 335 (quoting Panel Reports, para. 7.255).

measures to be imposed".¹⁰⁶ The Panel's approach suggests that Article XI:2(a) imposes an absolute limit on the length of time an export restriction may be imposed. China, however, maintains that the words "to prevent or relieve" in Article XI:2(a) suggest that the term "temporarily" does not mark a "bright line" moment in time after which an export restriction has necessarily been maintained for too long.¹⁰⁷ Instead, whether an export restriction is applied "temporarily" depends on the period of time required to prevent or relieve the critical shortage. China also argues that the Panel erred in finding that Article XI:2(a) and Article XX(g) are mutually exclusive, and contends that this finding was the basis for the Panel's erroneous interpretation of the term "temporarily" in Article XI:2(a). China submits that the two provisions are not mutually exclusive, but apply cumulatively.

42. Second, with regard to the Panel's application of the term "temporarily", China alleges that the Panel failed to take into consideration the fact that China's export restrictions on refractory-grade bauxite are subject to annual review. China faults the Panel for "simply assum[ing]" that China's restriction on exports of refractory-grade bauxite will be maintained indefinitely.¹⁰⁸ China submits that, at the close of each year, the factual circumstances are assessed in the light of the legal standard set forth in Article XI:2(a) to establish whether the export restriction should be maintained.

43. Third, China maintains that the Panel erred in its interpretation of the term "critical shortages" as excluding shortages caused by the "finite" nature or "limited reserve[s]" of a product.¹⁰⁹ China agrees with the Panel's interpretation of the term "critical shortages" as meaning a deficiency in quantity "involving suspense or grave fear", of "decisive importance".¹¹⁰ China alleges, however, that the Panel erred in excluding from the scope of Article XI:2(a) shortages caused by the limited, finite, or exhaustible nature of the product. China maintains that, had the drafters intended to limit the applicability of Article XI:2(a) to renewable resources, such as "foodstuffs", they would have indicated that by employing the term "other renewable products", instead of "other products", or by explicitly excluding "exhaustible natural resources" from the scope of Article XI:2(a).¹¹¹ For China, the Panel's interpretation leads to "absurd" distinctions, because Article XI:2(a) cannot be used to justify export restrictions on exhaustible natural resources, such as bauxite, but it could be used to

¹⁰⁶China's appellant's submission, para. 336 (quoting Panel Reports, paras. 7.298 and 7.305; and referring to para. 7.349).

¹⁰⁷China's appellant's submission, para. 340.

¹⁰⁸China's appellant's submission, para. 349 (quoting the Panel's statement at paragraph 7.350 of its Reports that there is "every indication that [China's restriction on exports of refractory-grade bauxite] will remain in place until the reserves have been depleted").

¹⁰⁹China's appellant's submission, para. 356 (quoting Panel Reports, paras. 7.297 and 7.305).

¹¹⁰China's appellant's submission, para. 357 (quoting *Oxford English Dictionary Online*, 2nd edn (Oxford University Press, 1989) (Panel Exhibit CHN-189)).

¹¹¹China's appellant's submission, paras. 361 and 362. (emphasis omitted)

justify restrictions concerning natural resources that can be renewed, such as wheat.¹¹² In China's view, the fact that a product cannot be renewed may exacerbate the consequences of a shortage, thus making it particularly important to impose a restriction that will alleviate the shortage.

44. China alleges that the Panel committed an additional error in its interpretation of "critical shortage" by assuming that there is no possibility for an existing shortage of an exhaustible natural resource ever to cease to exist, and that, therefore, it would never be possible to "relieve or prevent" the shortage through an export restriction applied on a temporary basis.¹¹³ China submits that a shortage of an exhaustible natural resource could cease to exist independently from depletion, for instance, where additional reserves or new extraction methods are discovered, or where substitutes or new technologies replace the product. China adds that, elsewhere in its analysis, the Panel recognized that shortages of exhaustible natural resources are not inevitable, and that advances in reserve detection or extraction techniques could alleviate or eliminate a shortage of an exhaustible natural resource.

45. Finally, China advances two separate claims that the Panel failed to make an objective assessment of the matter pursuant to Article 11 of the DSU. First, the Panel failed to assess properly evidence that China's export restriction on refractory-grade bauxite is annually reviewed and renewed. China submits that evidence relating to China's annual review procedure demonstrates that the export restriction will be maintained only as long as justified to prevent or relieve the critical shortage of refractory-grade bauxite. For China, this evidence shows that the Panel erred in assuming that the restriction "will remain in place until the reserves have been depleted".¹¹⁴ Second, China asserts that the Panel employed internally inconsistent or incoherent reasoning in stating, on the one hand, that "there is no possibility for an existing shortage [of an exhaustible natural resource] ever to cease to exist" such that "it will not be possible to relieve or prevent" it through an export restriction applied on a temporary basis,¹¹⁵ and acknowledging, on the other hand, that "advances in reserve detection or extraction techniques", or the availability of "additional capacity", could "alleviate or eliminate" a shortage of an exhaustible natural resource, or that "new technology or conditions" might "lessen demand" for the resource.¹¹⁶

¹¹²China's appellant's submission, para. 363.

¹¹³China's appellant's submission, para. 366 (quoting Panel Reports, para. 7.297).

¹¹⁴China's appellant's submission, para. 355 (quoting Panel Reports, para. 7.350).

¹¹⁵China's appellant's submission, para. 373 (referring to Panel Reports, para. 7.297). (emphasis added by China omitted)

¹¹⁶China's appellant's submission, para. 373 (referring to Panel Reports, paras. 7.348 and 7.351).

5. Article XX(g) of the GATT 1994

46. China had also contended before the Panel that, even if its quotas on refractory-grade bauxite did not fall within the exception of Article XI:2(a), the quotas could be justified under Article XX(g) of the GATT 1994. However, the Panel found that China had not demonstrated that its quotas met the requirements of Article XX(g). China requests the Appellate Body to find that the Panel erred in interpreting the phrase "made effective in conjunction with" in Article XX(g) of the GATT 1994 to mean that, in order to be justified under Article XX(g), a challenged measure must satisfy two cumulative conditions: first, it must "be applied jointly with" restrictions on domestic production or consumption; and, second, the "purpose" of the challenged measure must be to make effective restrictions on domestic production or consumption.¹¹⁷ China argues that the second element of the Panel's interpretation is inconsistent with the ordinary meaning of the phrase "made effective in conjunction with". China, however, does not appeal the Panel's ultimate conclusion that China has not demonstrated that its export quota on refractory-grade bauxite is justified pursuant to Article XX(g).

47. China submits that the Appellate Body's interpretation of the term "in conjunction with" in *US – Gasoline* corresponds to the first element of the Panel's interpretation of that phrase, namely that the challenged measures "be applied jointly with" restrictions on domestic production or consumption.¹¹⁸ However, nothing in the phrase "made effective in conjunction with" suggests that the "purpose" of a challenged measure must be to ensure the effectiveness of domestic restrictions.¹¹⁹ Instead, China contends that a measure restricting international trade must operate together with restrictions on domestic production or consumption, with both sets of restrictions forming part of a policy relating to the conservation of the resource in question.

6. Prior Export Performance and Minimum Capital Requirements

48. China appeals the Panel's finding that Paragraphs 1.2 and 5.1 of China's Accession Protocol, read in combination with Paragraphs 83(a), 83(b), 83(d), 84(a), and 84(b) of China's Accession Working Party Report, require China to eliminate any examination and approval system for WTO-consistent export quotas operated after 11 December 2004, including prior export performance and minimum registered capital requirements. China alleges various errors in the Panel's analysis.

¹¹⁷China's appellant's submission, para. 390 (quoting Panel Reports, para. 7.397).

¹¹⁸China's appellant's submission, paras. 404–406 (referring to Appellate Body Report, *US – Gasoline*, pp. 22–23, DSR 1996:1, 3, at 20–21).

¹¹⁹China's appellant's submission, para. 407.

49. Referring to the Appellate Body report in *China – Publications and Audiovisual Products*, China argues that the introductory phrase to Paragraph 5.1 means that China's trading rights obligations cannot "affect, encroach upon, or impair" its right to regulate trade in a WTO-consistent manner.¹²⁰ In particular, Paragraph 5.1 entitles it to adopt export quotas that are contrary to Article XI:1 of the GATT 1994, as long as they are justified under an exception such as Article XI:2 or XX of the GATT 1994. Paragraph 5.1 also entitles China to administer export quotas through an examination and approval system, including quota allocating criteria, provided that the system complies with the relevant WTO disciplines. China emphasizes that it "is not obliged by its accession commitments to abandon its WTO-consistent regulation of its export trade in order to confer upon traders an unfettered right to export".¹²¹

50. China further observes "that the authority of WTO Members to use prior export performance as a criterion in allocating import and export quotas is supported by the text of the covered agreements".¹²² In particular, Article 3.5(j) of the *Import Licensing Agreement* "not only affirms the right of a Member to take account of prior import performance in allocating import licenses, it expressly requires that such performance be considered".¹²³ Paragraph 130(a)(ii) of China's Accession Working Party Report also explicitly refers to "historical performance" as a criterion for quota allocation.¹²⁴ Further, Article XIII:2(d) of the GATT 1994 describes the circumstance in which quotas may be allocated among Members "based upon the proportions, supplied by such Members during a previous representative period, of the total quantity or value of imports of the product".¹²⁵ The Appellate Body has stated that this provision allows quota allocation by supplying countries "in accordance with the proportions supplied by those Members during a previous representative period, taking due account of 'special factors'".¹²⁶ According to China, Article XIII:2(d), "therefore, also supports the view that past trading performance is a relevant consideration in deciding to whom to allocate shares of a quota".¹²⁷

¹²⁰China's appellant's submission, para. 441 (quoting Appellate Body Report, *China – Publications and Audiovisual Products*, para. 219).

¹²¹China's appellant's submission, para. 456. (original emphasis)

¹²²China's appellant's submission, para. 463.

¹²³China's appellant's submission, para. 464. (original emphasis)

¹²⁴China's appellant's submission, para. 464. Paragraph 130(a)(ii) of China's Accession Working Party Report is included in China's Accession Protocol and is an integral part of the *WTO Agreement* by virtue of Paragraph 342 of China's Accession Working Party Report and Paragraph 1.2 of China's Accession Protocol.

¹²⁵China's appellant's submission, para. 465.

¹²⁶China's appellant's submission, para. 465 (quoting Appellate Body Reports, *EC – Bananas III (Article 21.5 – Ecuador II)/EC – Bananas III (Article 21.5 – US)*, para. 338).

¹²⁷China's appellant's submission, para. 465.

51. In China's view, minimum registered capital and prior export performance requirements serve important purposes, such as, ensuring that exporters are financially sound and have the necessary means to engage in export trade. China recognizes that, in the "ordinary course" of trade, it is required to grant the right to trade to all enterprises; however, "in the exceptional event" that it can maintain an export quota for a particular product, China submits that it may establish quota allocation rules that restrict the right to trade, provided that such rules are not inconsistent with the WTO disciplines applicable to such measures.¹²⁸

52. China further argues that the Panel misinterpreted the text of Paragraph 83(b) of China's Accession Working Party Report in finding that it "directs China to eliminate *any* 'examination and approval system' within three years of accession, including specifically the elimination of minimum registered capital requirements".¹²⁹ China reasons that the final sentence of Paragraph 83(b) applies to the particular examination and approval process for Chinese-invested enterprises that is described in the first sentence of Paragraph 83(b), and that the Panel erroneously gave Paragraph 83(b) such a broad scope of application as to prohibit any examination and approval system.

7. China's "Operation Capacity" Criterion and Article X:3(a) of the GATT 1994

53. China requests the Appellate Body to reverse the Panel's findings concerning the inconsistency of Article 19 of China's *Export Quota Administration Measures* and the "operation capacity" criterion for quota allocation with Article X:3(a) of the GATT 1994. China submits that, in reaching these findings, the Panel erred in its interpretation and application of Article X:3(a) of the GATT 1994 and acted inconsistently with Article 11 of the DSU.

54. According to China, the Panel erred in interpreting the term "administer" in Article X:3(a) to mean that WTO-inconsistent administration arises if a measure does not necessarily lead to, but merely poses, a "very real risk of" such administration. For a claim under Article X:3(a) to succeed, the Appellate Body has required that the complainant prove that such legal instruments or the features of such administrative processes "necessarily lead to a lack of uniform, impartial, or reasonable administration".¹³⁰ However, under the Panel's standard, a violation would also be found "if the complaining party shows that the features of an administrative process pose a very real risk to the

¹²⁸China's appellant's submission, para. 468.

¹²⁹China's appellant's submission, para. 469 (quoting Panel Reports, para. 7.655). (emphasis added by China)

¹³⁰China's appellant's submission, para. 639 (referring to Appellate Body Report, *EC – Selected Customs Matters*, paras. 201 and 226; and referring to Panel Report, *Thailand – Cigarettes (Philippines)*, paras. 7.873, 7.909, and 7.929).

interests of the relevant parties".¹³¹ For China, there is a significant difference between the two standards, given that an administrative process that creates a risk to a trader's interests does not "necessarily lead to" WTO-inconsistent administration. China emphasizes that a theoretical risk, possibility, or danger of a WTO Member choosing a WTO-inconsistent course of action that is not mandated by the measure is not sufficient to support a finding that the measure "as such" is inconsistent with Article X:3(a), absent evidence that the measure has been interpreted and applied in a WTO-inconsistent manner. Yet, several of the Panel's statements demonstrate that the Panel "based its findings on the mere risk or possibility that China might administer the 'operation capacity' criterion in a manner that violates Article X:3(a)".¹³² China adds that the Panel did not find that the "operation capacity" criterion "necessarily leads to" WTO-inconsistent administration. Nor did it have before it evidence demonstrating the WTO-inconsistent application of the measure. Consequently, there was no basis for the Panel to find that, where Chinese authorities exercise their discretion to interpret and apply the "operation capacity" criterion, they will do so in a manner that is inconsistent with Article X:3(a).

55. China further asserts that the Panel acted inconsistently with Article 11 of the DSU by finding, without a sufficient evidentiary basis, that the "operation capacity" criterion is "as such" inconsistent with Article X:3(a) of the GATT 1994. China points out that the Panel itself found that the term "operation capacity" was "vague" and "undefined", and that the European Union provided no evidence of the WTO-inconsistent application by China of the criterion.¹³³ Further, the Panel had no other evidence as to the operation of the measure, such as pronouncements of domestic courts on the meaning of such laws, or the opinions of legal experts. China asserts that every WTO Member is entitled to the presumption that its authorities will act in accordance with its WTO obligations. China alleges that the Panel reversed this presumption by assuming that the Chinese authorities would interpret and apply the "operation capacity" requirement in a WTO-inconsistent manner.

8. China's Export Licensing Requirements and Article XI:1 of the GATT 1994

56. China requests the Appellate Body to reverse the Panel's finding that Article 11(7) of China's Measures for the Administration of Licence for the Export of Goods¹³⁴ (the "2008 *Export Licence*

¹³¹China's appellant's submission, para. 640 (quoting Panel Reports, para. 7.708 (original emphasis omitted)).

¹³²China's appellant's submission, para. 669. (emphasis omitted)

¹³³China's appellant's submission, para. 680 (quoting Panel Reports, para. 7.710 and footnote 1059 thereto).

¹³⁴Measures for the Administration of Licence for the Export of Goods, Order of the Ministry of Commerce (2008) No. 11, 1 July 2008 (Panel Exhibits CHN-342 and JE-74).

Administration Measures"), and Articles 5(5) and 8(4) of China's Working Rules on Issuing Export Licences¹³⁵ (the "2008 Export Licensing Working Rules"), as applicable to export licences granted to applicants to export bauxite, coke, fluorspar, manganese, silicon carbide, and zinc, are inconsistent with Article XI:1 of the GATT 1994.¹³⁶

57. China submits that the Panel erred in interpreting the term "restriction" in Article XI:1 of the GATT 1994 to prohibit a measure "as such", based on the theoretical possibility that an export restriction might arise from the interpretation and application of undefined terms in the measure, absent evidence that the measure has been applied in a WTO-inconsistent manner. Referring to the dictionary meaning of the word "restriction", China argues that not all regulation of imports and exports constitutes a "restriction". To China, the use of the term "quantitative restriction" in the title of Article XI suggests that Article XI covers only those restrictions that have a "limiting effect" or impose a "limiting condition" on the quantity of exports.¹³⁷ China submits that such a limiting effect on the quantity of exports cannot be assumed from the mere regulation of exports. Rather, a panel must examine the design, structure, and operation of the measure in order to assess whether it does indeed limit the quantity of exports.

58. In the case of licensing requirements, China argues that the *Import Licensing Agreement* provides context to assist in identifying the dividing line between permissible and impermissible regulation under Article XI:1 of the GATT 1994. The fact that the *Import Licensing Agreement* imposes disciplines on licensing, without prohibiting it, underscores that licensing requirements are not *a priori* impermissible. China agrees with the Panel that the determination of whether a documentary requirement constitutes a restriction turns on the "nature" of the document required, and whether that documentary requirement has a limiting effect.¹³⁸

59. China maintains that the object and purpose underlying Article XI:1 is to protect competitive opportunities rather than trade flows, and that panels and the Appellate Body have ensured this protection by permitting a challenge to a measure "as such", independent of its application. China contends that the factual uncertainty surrounding the "expected operation" of a measure does not alter the interpretation of the term "restriction" or the requirement for a complainant to demonstrate that a challenged measure gives rise to a "restriction". Therefore, China argues, a complaining Member

¹³⁵Working Rules on Issuing Export Licences, Ministry of Commerce, Shangpeifa (2008) No. 398, 9 October 2008 (Panel Exhibits CHN-344 and JE-97).

¹³⁶China's appellant's submission, para. 603 (referring to Panel Reports, paras. 7.921, 7.946, 7.948, 7.958, 8.5(b), 8.8, 8.12(b), 8.15, 8.19(b), and 8.22).

¹³⁷China's appellant's submission, para. 539. (original emphasis)

¹³⁸China's appellant's submission, para. 543 (referring to Panel Reports, para. 7.917).

must establish that the action reasonably foreseen or anticipated under the measure will, at least in defined circumstances, give rise to a limiting effect or condition on the quantity of exports, and that the mere possibility that action to be taken under the measure might be WTO-inconsistent is not enough. China submits that a measure that mandates and, therefore, necessarily leads to WTO-inconsistent conduct is "as such" WTO-inconsistent even if the measure affords an authority the discretion to apply, or not to apply, the measure. China, however, distinguishes such measures from measures with uncertain meaning in domestic law that can always be interpreted and applied in a WTO-consistent manner. The theoretical possibility that the authority could exercise its discretion by choosing a WTO-inconsistent meaning does not render the measure "as such" WTO-inconsistent.

60. Turning to the application of Article XI:1 of the GATT 1994 to Article 11(7) of the 2008 *Export Licence Administration Measures* and Articles 5(5) and 8(4) of the 2008 *Export Licensing Working Rules*, China maintains that it was not sufficient for the Panel to rely on the theoretical possibility for a Chinese license-issuing authority to exercise "open-ended discretion" by interpreting and applying the measures in such a way as to impose a restriction on exports.¹³⁹ In China's view, its authorities could always choose a WTO-consistent course of action by requiring documents that do not entail a "restriction" on exportation. Where an authority enjoys "discretion" to interpret and apply the licensing measures, in all instances, in such a way that the required documents do not have a "limiting effect" or impose a "limiting condition" on exports, the theoretical possibility that an authority might exercise that discretion in a WTO-inconsistent manner does not constitute a "restriction" under Article XI:1, absent evidence that the measure has been applied in a WTO-inconsistent manner.¹⁴⁰

61. China further submits that the Panel erred under Article 11 of the DSU because it had no evidentiary basis to find that the discretion to request additional documents would constitute a prohibited "restriction" under Article XI:1.¹⁴¹ In particular, China contends that there is no evidence of any instance in which Chinese authorities "requested the provision of an unspecified document that

¹³⁹China's appellant's submission, para. 568.

¹⁴⁰China's appellant's submission, para. 533.

¹⁴¹China's appellant's submission, p. 161, heading VIII.D.4. China includes a ground of appeal under Article 11 of the DSU based on the Appellate Body's recognition "that it is often difficult to distinguish clearly between issues that are purely legal or purely factual, or are mixed issues of law and fact", and that "a failure to make a claim under Article 11 of the DSU on an issue that the Appellate Body determines to concern a factual assessment may have serious consequences for the appellant". (China's appellant's submission, p. 161, footnote 676 to heading VIII.D.4. (quoting Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 872))

restricted exports".¹⁴² China refers to evidence showing that export licences have always been granted on the production of documents specified in China's licensing measures.

B. *Arguments of the United States and Mexico – Joint Appellees*

1. Article 6.2 of the DSU

62. The United States and Mexico contend that the Panel correctly found that Section III of the complainants' panel requests complies with the requirements of Article 6.2 of the DSU. The United States and Mexico request the Appellate Body to uphold the Panel's finding in the Panel's preliminary ruling (second phase) and in the Panel Reports that Section III of the panel requests comply with Article 6.2 of the DSU, and to uphold all consequent findings of inconsistency.¹⁴³

63. The United States and Mexico disagree with China's contention that the Panel observed defects in Section III of the panel requests. Rather, the fact that the Panel, in the preliminary ruling (first phase), reserved its decision on China's objections under Article 6.2 of the DSU demonstrates that the Panel provisionally considered Section III of the panel requests to be sufficient to comply with Article 6.2. The United States and Mexico find support for their contention in paragraphs 34 and 35 of the Panel's preliminary ruling (first phase); in particular, the Panel's statement that the "narrative paragraphs aim at explaining succinctly how and why some of the challenged measures at issue are inconsistent with some of the WTO principles".¹⁴⁴ Furthermore, the Panel's statement in paragraph 46 of the Panel's preliminary ruling (first phase), where the Panel stated that it "reserves its decision" on China's objections under Article 6.2 of the DSU, supports the proposition that the Panel provisionally accepted that Section III of the panel requests comply with Article 6.2 of the DSU.

64. For the United States and Mexico, the only additional information the Panel needed in order to make a definitive finding under Article 6.2 was to determine, from the parties' first written submissions, whether China had suffered any prejudice in its ability to defend itself. In addition, the United States and Mexico take issue with China's contention that the Panel used the complainants' later submissions to cure defects in Section III of the panel requests. The Panel questions following the first and second Panel meetings requesting the complainants to list all measures and the specific

¹⁴²China's appellant's submission, para. 597.

¹⁴³In particular, paras. 7.669, 7.670, 7.678, 7.756, 7.807, 7.958, 7.1082, 7.1102, 7.1103, 8.4(a)-(b), 8.5(b), 8.6(a)-(b), 8.11 (a), (c), (e), and (f), 8.12(b), 8.13(a)-(b), 8.18(a)-(b), 8.19(b), and 8.20(a)-(b) of the Panel Reports. (See joint appellees' submission of the United States and Mexico, para. 59)

¹⁴⁴Joint appellees' submission of the United States and Mexico, para. 45 (quoting Panel's preliminary ruling (first phase), Panel Reports, Annex F-1, para. 35). (emphasis added by the United States and Mexico omitted)

WTO provisions each of the measures allegedly violate were not posed with any specific intentions regarding Section III of the panel requests, but rather in order to clarify what recommendations the complainants were seeking with respect to all the claims at issue in the dispute. Thus, the Panel looked at the tables submitted by the complainants in order to confirm that China had not been prejudiced in the preparation of its defence.

65. The United States and Mexico submit that China mistakenly relies on the Appellate Body's statement in *US – Oil Country Tubular Goods Sunset Reviews* that, in order to "present the problem clearly", a complainant must "plainly connect" the challenged measures with the provisions of the covered agreements claimed to have been infringed.¹⁴⁵ In that dispute, the Appellate Body found that Argentina's panel request satisfied the requirements of Article 6.2, even though the link between the measures and the WTO obligations at issue was far less clear than in the panel requests at issue in the current dispute. The United States and Mexico recall that they had identified before the Panel 37 panel requests from previous disputes that follow the structure of Section III of the panel requests at issue in this dispute, and in none of those cases was the panel request found not to satisfy Article 6.2 of the DSU. This demonstrates that China is advocating a "dramatically new approach to the interpretation of Article 6.2".¹⁴⁶

66. Finally, the United States and Mexico maintain that the Panel respected the due process requirements contained in Article 6.2 of the DSU. The Panel "took pains to assess whether the argumentation advanced by the [c]omplainants resulted in any prejudice to China's ability to defend itself".¹⁴⁷ Yet, China's argument that the complainants intended to advance "subsets of claims regarding subsets of measures", as well as the argument that the total combination of measures and legal provisions resulted in a large number of possible claims, demonstrate that China was more than "adequately notified", and was in fact "well aware", of the claims the complainants could advance.¹⁴⁸ The United States and Mexico add that Article 6.2 of the DSU does not require that every claim identified in a panel request be advanced.

2. The Panel's Recommendations

67. The United States and Mexico emphasize the limited scope of China's appeal, noting that China appeals only the Panel's recommendations "to the extent that [the] recommendation[s] apply to

¹⁴⁵Joint appellees' submission of the United States and Mexico, para. 48 (quoting Appellate Body Report, *US – Oil Country Tubular Goods Sunset Reviews*, para. 162).

¹⁴⁶Joint appellees' submission of the United States and Mexico, para. 54.

¹⁴⁷Joint appellees' submission of the United States and Mexico, para. 55.

¹⁴⁸Joint appellees' submission of the United States and Mexico, para. 57.

annual replacement measures", which China argues are outside the Panel's terms of reference.¹⁴⁹ The Panel did not make recommendations on measures on which it had not made findings, and it did not make a recommendation on annual replacement measures adopted after the establishment of the Panel. Instead, the Panel made findings and recommendations on the series of measures "in force at the date of panel establishment".¹⁵⁰ According to the United States and Mexico, China's appeal could therefore "be dismissed on this basis alone".¹⁵¹

68. The United States and Mexico further disagree with China's apparent position that the only way for them to challenge the future life of the export duties and quotas at issue is by challenging China's replacement measures. The United States and Mexico submit, however, that they do not have to challenge and obtain findings and recommendations against "replacement measures" in order for "future" measures to come within the scope of China's implementation obligation once the challenged measures have been found to be WTO-inconsistent.¹⁵² China's approach would "frustrate the aims of the dispute settlement system", as it would create the "moving target situation" against which the Appellate Body has cautioned.¹⁵³ If no recommendations could be made in relation to an annual measure once it had been superseded, then trade measures imposed through annually recurring legal instruments could never be successfully challenged in WTO dispute settlement. In the present case, the implication of China's position is that the DSB would be precluded from making any recommendations because the 2010 replacement measures will have ceased to exist before the DSB could adopt the Panel's recommendations and rulings.

69. The United States and Mexico also fault China for confusing the distinction between the basis on which a recommendation is made and the application or effect of the recommendation once it has been made. Contrary to China's assertion, they have not abandoned their right to obtain meaningful recommendations from this dispute settlement proceeding. Instead, the United States and Mexico assert that they have consistently sought recommendations on the measures found to be inconsistent as of the date of Panel establishment.

¹⁴⁹Joint appellees' submission of the United States and Mexico, para. 80 (quoting China's appellant's submission, para. 99).

¹⁵⁰Joint appellees' submission of the United States and Mexico, para. 83 (quoting Panel Reports, para. 7.33(e)).

¹⁵¹Joint appellees' submission of the United States and Mexico, para. 83.

¹⁵²Joint appellees' submission of the United States and Mexico, para. 86.

¹⁵³Joint appellees' submission of the United States and Mexico, para. 87.

3. Applicability of Article XX of the GATT 1994

70. The United States and Mexico request the Appellate Body to uphold the Panel's finding that China may not rely upon the exceptions contained in Article XX of the GATT 1994 to justify an inconsistency with its export duty commitments contained in Paragraph 11.3 of China's Accession Protocol. Specifically, the Panel "correctly interpreted and applied" China's Accession Protocol based on the text of Paragraph 11.3 and Article XX and the relevant context, in conformity with a "key principle of treaty interpretation" contained in Article 31(1) of the *Vienna Convention on the Law of Treaties*¹⁵⁴ (the "*Vienna Convention*").¹⁵⁵ Additionally, the Panel properly rejected China's arguments that an inherent right to regulate trade "applies above and beyond the exceptions provided for in Paragraph 11.3".¹⁵⁶

(a) Paragraph 11.3 of China's Accession Protocol

71. The United States and Mexico request the Appellate Body to uphold the Panel's interpretation of the "plain meaning" of Paragraph 11.3 of China's Accession Protocol.¹⁵⁷ China's argument that the two exceptions in Paragraph 11.3—for Annex 6 to the Protocol, and for taxes and charges applied in conformity with Article VIII of the GATT 1994—"somehow authorize" China to justify its export duties in excess of the maximum levels contained in Annex 6, as well as export duties on products not listed in Annex 6, "misconstrue[s] the relevance" of these two exceptions.¹⁵⁸

72. Regarding China's argument that reference to "exceptional circumstances" in the Note to Annex 6 to China's Accession Protocol allows China to justify under Article XX of the GATT 1994 export duties found to be inconsistent with Paragraph 11.3 of the Protocol, the United States and Mexico assert that there is "no textual basis" for such a conclusion.¹⁵⁹ The first sentence of the Note makes clear that China committed not to impose export duties on the 84 products listed in Annex 6 above the maximum rates set out therein. The second and third sentences of the Note also impose an additional obligation upon China that, in the event that the applied rate for any of the 84 products listed in Annex 6 is less than the maximum rate, China cannot raise the applied rate except in "exceptional circumstances", and only after consulting with the affected Members. In the light of China's acceptance of this additional obligation, the Note cannot be read as providing a basis for

¹⁵⁴Done at Vienna, 23 May 1969, 1155 UNITS 331; 8 International Legal Materials 679.

¹⁵⁵Joint appellees' submission of the United States and Mexico, para. 96.

¹⁵⁶Joint appellees' submission of the United States and Mexico, para. 97.

¹⁵⁷Joint appellees' submission of the United States and Mexico, para. 111.

¹⁵⁸Joint appellees' submission of the United States and Mexico, para. 111.

¹⁵⁹Joint appellees' submission of the United States and Mexico, para. 113.

China to impose export duties on the 84 products above the maximum rates specified in Annex 6. The United States and Mexico further reject China's argument that, because of the reference to "exceptional circumstances" in the Note to Annex 6, there is a "substantive overlap" between the Note and Article XX of the GATT 1994.¹⁶⁰ Instead, Annex 6 and Article XX only "overlap" to the extent that each establishes "potential exceptions" to the commitments contained in Annex 6 regarding the applied rates for the 84 products listed, and in the GATT 1994, respectively.¹⁶¹

73. The United States and Mexico further submit that the fact that Paragraph 11.3 of China's Accession Protocol expressly refers to Article VIII of the GATT 1994, but leaves out reference to other provisions of the GATT 1994, indicates that WTO Members and China did not intend Article XX to be available as an exception to justify a violation of Paragraph 11.3. They disagree with China's assumption that, if a tax or charge that would otherwise be inconsistent with Article VIII met the conditions of Article XX, then it would be consistent with Article VIII. Instead, they consider that conformity with the conditions of Article XX only means that Article VIII would not "prevent the application" of that measure.¹⁶²

(b) Context from the *WTO Agreement*

74. The United States and Mexico argue that the Panel did not rely solely on the inclusion of the two specific exceptions in Paragraph 11.3 of China's Accession Protocol to reach the conclusion that Article XX of the GATT 1994 is not available in cases of violation of the obligations contained in Paragraph 11.3. Instead, the Panel also considered other provisions of China's Accession Protocol and China's Accession Working Party Report, noting that, unlike Paragraph 11.3, such provisions include general references to the *WTO Agreement* and the GATT 1994.

75. The United States and Mexico further argue that Paragraphs 5.1, 11.1, and 11.2 of China's Accession Protocol, Paragraphs 155 and 156 of China's Accession Working Party Report, and Article XX of the GATT 1994 support the Panel's finding that Article XX is not applicable in cases of findings of inconsistency with the commitments contained in Paragraph 11.3 of China's Accession Protocol. The Panel relied on *China – Publications and Audiovisual Products*, where the Appellate Body interpreted the introductory clause of Paragraph 5.1 of China's Accession Protocol as including a reference to Article XX of the GATT 1994; however, the "specific and circumscribed" language of Paragraph 11.3 is "in sharp contrast" to that of Paragraph 5.1, because it "sets forth

¹⁶⁰Joint appellees' submission of the United States and Mexico, para. 114.

¹⁶¹Joint appellees' submission of the United States and Mexico, para. 114.

¹⁶²Joint appellees' submission of the United States and Mexico, para. 117.

particular commitments" and the two exceptions to those commitments, and includes no reference to the GATT 1994, or to WTO obligations more generally.¹⁶³ The United States and Mexico argue that China's interpretation of Paragraph 11.3 would render the introductory language in Paragraph 5.1 "superfluous" and would therefore be "disfavoured under a key tenet" of the customary rules of treaty interpretation that meaning and effect be given to all the terms of a treaty.¹⁶⁴

76. According to the United States and Mexico, the Panel was also "appropriately struck" by the difference between the language of Paragraph 11.3 and that of Paragraphs 11.1 and 11.2 of China's Accession Protocol.¹⁶⁵ Whereas Paragraphs 11.1 and 11.2 affirm China's obligation to apply or administer certain measures "in conformity with the GATT 1994", Paragraph 11.3 establishes an obligation with regard to export duties that is absent in the GATT 1994, and sets forth the specific exceptions that apply to that obligation.¹⁶⁶ Similarly, the Panel properly found support for its interpretation of Paragraph 11.3 in Paragraphs 155 and 156 of China's Accession Working Party Report. While the Panel acknowledged that Paragraphs 155 and 156 are not a part of the "explicit commitments" made by China, the Panel also properly viewed these paragraphs as providing relevant context because, in those paragraphs, WTO Members expressed concerns over taxes and charges that China applied to exports, and expressed the view that such taxes and charges should be eliminated unless applied in conformity with Article VIII of the GATT 1994 or Annex 6 of the Draft Protocol.¹⁶⁷

77. The United States and Mexico recall the Panel's reliance upon the text of Article XX of the GATT 1994 as indicating that the Article XX exceptions relate only to the GATT 1994, and the Panel's observation that Article XX has been incorporated by reference into some other covered agreements. No such reference is contained in Paragraph 11.3 of China's Accession Protocol, and China does not address the meaning of the phrase "this Agreement" in Article XX on appeal. In concluding that Article XX does not apply to violations of the commitments contained in Paragraph 11.3, the Panel correctly interpreted Paragraph 11.3 and the relevant provisions of the

¹⁶³Joint appellees' submission of the United States and Mexico, para. 121.

¹⁶⁴Joint appellees' submission of the United States and Mexico, para. 121 (referring to Appellate Body Report, *US – Gasoline*, p. 25, DSR 1996:1.3, at 23).

¹⁶⁵Joint appellees' submission of the United States and Mexico, para. 122.

¹⁶⁶Joint appellees' submission of the United States and Mexico, para. 123 (quoting Panel Reports, para. 7.138).

¹⁶⁷Joint appellees' submission of the United States and Mexico, para. 124 (referring to Panel Reports, para. 7.145).

GATT 1994, China's Accession Protocol, and China's Accession Working Party Report "in a harmonious manner", giving effect to the text of each provision.¹⁶⁸

78. Next, the United States and Mexico assert that China's argument that the Panel erred in "failing to conclude" that Paragraph 170 of China's Accession Working Party Report means that the exceptions under Article XX apply to violations of China's export duty commitments under Paragraph 11.3 of its Accession Protocol is "without merit".¹⁶⁹ Paragraph 169 of the Accession Working Party Report shows that some Members were concerned about internal policies, especially those of sub-national governments, imposing discriminatory taxes and other charges that would affect trade in goods. In Paragraph 170, China responded to this concern by confirming that its laws relating to all fees, charges, or taxes levied on imports and exports would be in full conformity with WTO obligations. The United States and Mexico argue that it is "untenable to believe" that Paragraph 170 reflects the negotiators' intent to apply Article XX to Paragraph 11.3 of China's Accession Protocol.¹⁷⁰ They submit that China's arguments ignore the text of Paragraph 11.3, the context supplied by Paragraphs 155, 156, and 159 of China's Accession Working Party Report, and Article XX of the GATT 1994, and "misconstrue"¹⁷¹ the Panel's analysis of Paragraph 170. The Panel did not "simply conclude" that Paragraph 170 applies to domestic taxes, and not export duties; instead, it correctly found that "Paragraph 170 does not refer to China's *specific obligations on export duties*".¹⁷²

79. Finally, in response to China's argument that the Panel failed to interpret Paragraph 11.3 in the light of the preamble of the *WTO Agreement*, the United States and Mexico assert that the preamble does not provide "a textual basis" for concluding that Article XX applies to violations of Paragraph 11.3, nor does it negate the text and context demonstrating that Members intended Article XX not to apply.¹⁷³

(c) The Inherent Right to Regulate Trade

80. According to the United States and Mexico, China's arguments asserting that its inherent right to regulate trade permits recourse to Article XX of the GATT 1994 for violations of Paragraph 11.3 of

¹⁶⁸Joint appellees' submission of the United States and Mexico, para. 127.

¹⁶⁹Joint appellees' submission of the United States and Mexico, para. 128.

¹⁷⁰Joint appellees' submission of the United States and Mexico, para. 130.

¹⁷¹Joint appellees' submission of the United States and Mexico, para. 132.

¹⁷²Joint appellees' submission of the United States and Mexico, para. 132 (quoting Panel Reports, para. 7.141). (emphasis added by the United States and Mexico)

¹⁷³Joint appellees' submission of the United States and Mexico, para. 136.

China's Accession Protocol "are flawed in several respects, and should be rejected".¹⁷⁴ They begin by highlighting that, contrary to China's claims, the Panel "nowhere suggested" that the *WTO Agreement* confers an inherent right to regulate trade, or that Members "abandoned" their right to regulate trade upon "entering" the WTO.¹⁷⁵

81. The United States and Mexico argue that the Panel's conclusion that China agreed to "specific textual disciplines" on its ability to impose export duties is consistent with the text of Paragraph 11.3 and the "understanding" reflected in previous Appellate Body reports that, by joining the WTO, Members agreed to disciplines on their right to regulate trade, as contained in the covered agreements.¹⁷⁶ The Appellate Body report in *China – Publications and Audiovisual Products* recognized that, because WTO Members have an inherent right to regulate trade, it was necessary to agree on rules that constrain that right. The United States and Mexico also rely on the Appellate Body report in *Japan – Alcoholic Beverages II* to argue that China's obligation to eliminate export duties contained in Paragraph 11.3 of China's Accession Protocol is a "commitment" that conditions the exercise of China's sovereignty in exchange for the benefits it derives as a Member of the WTO.¹⁷⁷

82. Recalling China's argument that it is entitled to invoke Article XX exceptions for violations of Paragraph 11.3 in the absence of "specific treaty language", the United States and Mexico assert that China's approach would render the introductory clause in Paragraph 5.1, and the language in Paragraphs 11.1 and 11.2, "superfluous".¹⁷⁸ In fact, the Appellate Body's finding in *China – Publications and Audiovisual Products* that Article XX is available for violations of Paragraph 5.1 of China's Accession Protocol was "grounded" in the language of the provision and not a right to regulate trade "in the abstract".¹⁷⁹ The language in Paragraph 11.3 is "in contrast" to the language in the accession documents of other WTO Members with respect to their obligations on export duties.¹⁸⁰ China's "citation" to language in other agreements related to WTO Members' ability to regulate is "similarly unavailing".¹⁸¹ Specifically, the agreements cited by China do not address the applicability of Article XX exceptions to China's obligations under Paragraph 11.3, nor do they "inform an

¹⁷⁴Joint appellees' submission of the United States and Mexico, para. 139.

¹⁷⁵Joint appellees' submission of the United States and Mexico, para. 140.

¹⁷⁶Joint appellees' submission of the United States and Mexico, para. 140.

¹⁷⁷Joint appellees' submission of the United States and Mexico, paras. 143 and 144 (referring to Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 15, DSR 1996:1, 97, at 108).

¹⁷⁸Joint appellees' submission of the United States and Mexico, para. 145.

¹⁷⁹Joint appellees' submission of the United States and Mexico, para. 145 (referring to Appellate Body Report, *China – Publications and Audiovisual Products*, paras. 219-228).

¹⁸⁰Joint appellees' submission of the United States and Mexico, para. 145 (referring to, as example, Report of the Working Party on the Accession of Ukraine to the World Trade Organization, WT/ACC/UKR/152, paras. 512 and 540).

¹⁸¹Joint appellees' submission of the United States and Mexico, para. 146.

interpretation" of the text of Paragraph 11.3.¹⁸² The United States and Mexico also highlight the Panel's observation that the *Agreement on Trade-Related Investment Measures* (the "TRIMs Agreement"), the *TBT Agreement*, the *TRIPS Agreement*, the GATS, and the *SPS Agreement* either expressly incorporate the right to invoke Article XX exceptions or include their own exceptions and flexibilities.

83. According to the United States and Mexico, China's insistence that it is not advocating for the right to ignore its WTO commitments because it still must comply with the requirements of Article XX "does not address the relevant issue in this dispute".¹⁸³ China's arguments wrongly assume that the exceptions in Article XX are the starting point for an analysis of WTO-consistency. Instead, the United States and Mexico argue that the starting point of the analysis is whether a measure is consistent with a Member's WTO obligations, and if not, whether any applicable exceptions apply. Moreover, China's argument that it is entitled to invoke Article XX in the case of Paragraph 11.3 violations because it is the only WTO Member with export duty commitments "lacks a textual basis".¹⁸⁴ The fact that a WTO Member has undertaken a specific commitment that not all WTO Members have made is not a proper basis for finding that an exception is applicable to that commitment.

84. The United States and Mexico assert that China's right to promote non-trade interests is not "at risk" in this dispute.¹⁸⁵ Paragraph 11.3 does not prevent China from undertaking measures other than export duties to promote legitimate public health or conservation objectives, and China has a number of "tools at its disposal" to pursue these ends.¹⁸⁶ Paragraph 11.3 of China's Accession Protocol, however, contains specific commitments with respect to export duties and provides only two "applicable" exceptions. "Neither an abstract right to regulate trade nor Article XX of the GATT 1994 changes that fact."¹⁸⁷

4. Article XI:2(a) of the GATT 1994

85. The United States and Mexico request the Appellate Body to uphold the Panel's finding that China had not demonstrated that its export quota on refractory-grade bauxite is "temporarily" applied to prevent or relieve a "critical shortage" within the meaning of Article XI:2(a) of the GATT 1994,

¹⁸²Joint appellees' submission of the United States and Mexico, para. 146.

¹⁸³Joint appellees' submission of the United States and Mexico, para. 147.

¹⁸⁴Joint appellees' submission of the United States and Mexico, para. 148.

¹⁸⁵Joint appellees' submission of the United States and Mexico, para. 149.

¹⁸⁶Joint appellees' submission of the United States and Mexico, para. 150.

¹⁸⁷Joint appellees' submission of the United States and Mexico, para. 150.

and to reject China's claim that the Panel failed to conduct an objective assessment of the matter, as required under Article 11 of the DSU.

86. With respect to China's arguments relating to the interpretation of the term "temporarily", the United States and Mexico disagree with China's allegation that the Panel excluded from the scope of Article XI:2(a) any "long-term" application of export restrictions. However, the Panel did not interpret the term "temporarily" so as to impose an "absolute limit" on the time period in which an export restraint may be imposed under Article XI:2(a). In the United States and Mexico's view, the Panel was appropriately sensitive to the contextual relationship between the terms "temporarily applied" and "critical shortages" when it found that Article XI:2(a) cannot be interpreted to permit the long-term application of measures in the nature of China's export restrictions on refractory-grade bauxite.

87. In response to China's allegation that the Panel erred in finding that Articles XI:2(a) and XX(g) of the GATT 1994 are mutually exclusive, the United States and Mexico submit that China misunderstands the Panel's analysis. The Panel did not find that Articles XI:2(a) and XX(g) can never apply to the same measure. Rather, the Panel found that, under China's interpretation of Article XI:2(a), pursuant to which a Member could impose an export restriction for the purpose of addressing limited reserves of a natural resource, Articles XI:2(a) and XX(g) would be duplicative.

88. Regarding China's argument that the Panel erred in its interpretation of the term "critical shortages", the United States and Mexico disagree that the Panel erred in interpreting Article XI:2(a) "to exclude shortages caused, in part, by the exhaustibility of the product subject to the export restriction".¹⁸⁸ They submit that the existence of a limited amount of reserves constitutes only a degree of shortage, and a mere degree of shortage does not constitute a "critical" shortage, which is one rising to the level of a crisis. They also refer to a discussion in the negotiating history of Article XI:2(a), during which, in response to a proposal to omit the word "critical" in Article XI:2(a), the representative from the United Kingdom stated that, "if you take out the word 'critical', almost any product which is essential will be alleged to have a degree of shortage and could be brought within the scope of this paragraph".¹⁸⁹ This suggests that a showing of finite availability is not sufficient to

¹⁸⁸Joint appellees' submission of the United States and Mexico, para. 173 (quoting China's appellant's submission, paras. 356, 363, and 367).

¹⁸⁹Joint appellees' submission of the United States and Mexico, para. 176 (quoting United Nations Economic and Social Council, Second Session of the Preparatory Committee of the United Nations Conference of Trade and Employment, Verbatim Report, Fortieth Meeting of Commission "A" (1) (Articles 25 & 27, 26, 28 & 29), UN document E/PC/T/A/PV/40(1), 15 August 1947 (Panel Exhibit CHN-181), p. 6).

demonstrate a critical shortage. In addition, the United States and Mexico maintain that the Panel properly reasoned that the concept of "temporarily" informs the concept of a "critical shortage".

89. The United States and Mexico disagree with China's contention that the Panel's finding that an export restriction applied to address the exhaustibility of a resource cannot be temporarily applied is contradictory to other findings by the Panel. In their view, irrespective of whether a measure is applied until the remaining reserves of the product are exhausted, or until technological advancements slow the rate of exhaustion, the application of the export restriction is not "temporary", as, in either case, it is not connected to the time period necessary to address the critical shortage, but rather to the depletion of reserves. Additionally, the "hypothetical situation" in which technological advancements may allow for a slower rate of exhaustion does not "negate" the evidence on record showing that China intends to maintain its export quota to guarantee a supply for its domestic industry until the reserves are depleted.¹⁹⁰

90. As regards China's allegations, first, that the Panel acted inconsistently with Article 11 of the DSU, the United States and Mexico submit that the Panel fully engaged with China's arguments regarding annual review. However, the Panel also had before it evidence that China has imposed an export quota on refractory-grade bauxite since at least 2000, as well as indications that China intended to maintain the restrictions until the exhaustion of the remaining reserves. Therefore, irrespective of China's arguments relating to the annual review of those measures, the Panel's finding that the restriction is not applied "temporarily" is, in the United States and Mexico's view, "well-founded".¹⁹¹ Second, China alleges that the Panel employed internally inconsistent or incoherent reasoning when it found that an export restriction imposed to address the exhaustibility of a natural resource could not be temporarily applied, because, in China's view, that finding is inconsistent with other Panel findings with respect to technological developments. The United States and Mexico contend that there is no inconsistency in the Panel's finding. Whether a measure is applied until remaining reserves are exhausted or until technological developments slow the rate of exhaustion, the application of the export quota is not temporary. In either case, it is tied not to the time period needed to address a "critical shortage", but rather to the depletion of finite reserves.

¹⁹⁰ Joint appellees' submission of the United States and Mexico, para. 190 (referring to China's opening statement at second Panel meeting, paras. 143, 144, and 146-148; and Panel Reports, para. 7.344).

¹⁹¹ Joint appellees' submission of the United States and Mexico, para. 185.

5. Article XX(g) of the GATT 1994

91. The United States and Mexico request the Appellate Body to uphold the Panel's interpretation of the phrase "made effective in conjunction with" in Article XX(g) of the GATT 1994 as requiring that the purpose of a challenged export restriction must be to ensure the effectiveness of restrictions imposed on domestic production or consumption. In their view, the Panel's interpretation is in accordance with the ordinary meaning of the terms in Article XX(g) in their context and in the light of the object and purpose of the GATT 1994. They distinguish from the present case the Appellate Body reports in *US – Gasoline* and *US – Shrimp* on the basis that neither of those cases involved the question of how the operation of the challenged measure should be conjoined with the operation of the domestic restrictions. In *US – Gasoline*, this was because the challenged measure affecting imports was the same measure establishing the restrictions on domestic production or consumption. In *US – Shrimp*, the conjunction of the operation of the challenged measure with the domestic regulation was found to "satisfy easily" the requirement of Article XX(g).¹⁹²

92. According to the United States and Mexico, the only other time a respondent has asserted an Article XX(g) defence where the challenged trade measure was distinct from the restrictions on domestic production or consumption was in the GATT dispute in *Canada – Herring and Salmon*. The United States and Mexico agree with the GATT panel that an export restriction can only be considered to be made effective "in conjunction with" domestic restrictions "if it was primarily aimed at rendering effective these restrictions".¹⁹³ In the present case, the Panel appropriately drew on that GATT panel report to conclude that, in order to qualify as a conservation measure justified under Article XX(g), China's export quota must not only be applied jointly with restrictions on domestic production or consumption, but must also ensure the effectiveness of those domestic restrictions.

6. Prior Export Performance and Minimum Capital Requirements

93. The United States and Mexico argue that the Panel correctly found that the imposition of prior export performance and minimum registered capital requirements is inconsistent with China's trading rights commitments under Paragraphs 83 and 84 of China's Accession Working Party Report. First, they assert that Paragraphs 83 and 84 include specific commitments to eliminate China's examination

¹⁹² Joint appellees' submission of the United States and Mexico, para. 215 (referring to Appellate Body Report, *US – Gasoline*, pp. 3-5, DSR 1996:1, 3, at 4-6; and Appellate Body Report, *US – Shrimp*, paras. 143-145).

¹⁹³ Joint appellees' submission of the United States and Mexico, para. 217 (quoting Panel Reports, para. 7.395, in turn quoting GATT Panel Report, *Canada – Herring and Salmon*, para. 4.6 (original emphasis omitted)).

and approval process, including prior export performance and minimum capital requirements that are not found elsewhere in the *WTO Agreement*. Second, China's suggestion that the complainants need to demonstrate the WTO-inconsistency of China's prior export performance and minimum capital requirements under other provisions of the *WTO Agreement* is without merit. The United States and Mexico insist that China has obligations with respect to such requirements pursuant to Paragraph 5.1 of China's Accession Protocol and Paragraphs 83 and 84 of China's Accession Working Party Report, and that the requirements currently imposed with respect to export quota allocation are inconsistent with China's obligations under these provisions.

94. The United States and Mexico also refute China's argument that the *Import Licensing Agreement* and Article XIII of the GATT 1994 contemplate the use of historical performance in allocating quotas. They insist that neither provision can be read as overriding China's trading rights obligations.

95. Finally, the United States and Mexico challenge China's position that China is allowed to maintain a minimum capital requirement for foreign-invested companies. They note that China did not present this argument to the Panel. Paragraphs 83(b), 83(d), 84(a), and 84(b) of China's Accession Working Party Report show that there is no basis for concluding that China is permitted to maintain an examination and approval system that applies only to foreign-invested enterprises; in fact, these provisions provide the opposite.

7. China's Export Licensing Requirements and Article XI:1 of the GATT 1994

96. The United States and Mexico request the Appellate Body to uphold the Panel's finding that Article 11(7) of China's *2008 Export Licence Administration Measures*, and Articles 5(5) and 8(4) of the *2008 Export Licensing Working Rules*, are inconsistent with Article XI:1 of the GATT 1994.¹⁹⁴ The United States and Mexico also request the Appellate Body to reject China's claim that the Panel erred under Article 11 of the DSU by finding that China's measures are inconsistent with Article XI:1 without a sufficient evidentiary basis. The Panel correctly interpreted and applied Article XI:1 of the GATT 1994, and correctly found that the uncertainty and unpredictability inherent in China's export licensing system constitute a restriction under that provision. The United States and Mexico thus reject China's contention that, where an authority enjoys the discretion always to interpret and apply a challenged measure in a WTO-consistent manner, an examination of the design, structure, and

¹⁹⁴Joint appellees' submission of the United States and Mexico, para. 255 (referring to Panel Reports, paras. 7.921, 7.946, 7.948, 7.958, 8.5(b), 8.8, 8.12(b), 8.15, 8.19(b), and 8.22).

expected operation of the measure does not permit a panel to conclude that the measure mandates and, if applied, necessarily leads to WTO-inconsistent conduct.

97. The United States and Mexico argue that the Panel's interpretation is consistent with the ordinary meaning of the term "restriction", as interpreted by WTO panels. They refer to a statement by the panel in *Colombia – Ports of Entry* that the term "restrictions" under Article XI:1 is "broad in scope" and "can cover measures that negatively affect competitive opportunities", including "measures that create uncertainties and affect investment plans, restrict market access for imports, or make importation prohibitively costly".¹⁹⁵ For the United States and Mexico, an interpretation of the term "restriction" as including the lack of certainty and predictability arising from a discretionary export licensing system is also supported by the Appellate Body's interpretation in *Chile – Price Band System* of the term "import restrictions" in the context of Article 4 and footnote 1 of the *Agreement on Agriculture*.

98. Moreover, the United States and Mexico argue that China itself recognizes that "[t]he object and purpose underlying Article XI:1 is to protect competitive opportunities for exports, rather than trade flows."¹⁹⁶ This assertion is at odds with China's argument that its export licensing system can be considered inconsistent with Article XI:1 only if it restricts trade flows through the denial of export licences. According to the United States and Mexico, the uncertainty and unpredictability inherent in the discretion of Chinese authorities to require undefined or unspecified documents entails a restriction on competitive opportunities even without the occurrence of actual denials of export licences, and is therefore inconsistent with Article XI:1 of the GATT 1994.

99. The United States and Mexico request the Appellate Body to reject China's claim that the Panel acted inconsistently with Article 11 of the DSU in making findings regarding China's export licensing system without an evidentiary basis. The United States and Mexico argue that, while China alleges that the Panel lacked a sufficient evidentiary basis for its finding, it acknowledges at the same time that "it is not necessary to provide evidence of the application of a measure in support of an *as such* challenge".¹⁹⁷

¹⁹⁵Joint appellees' submission of the United States and Mexico, para. 270 (quoting Panel Report, *Colombia – Ports of Entry*, para. 7.240; and referring to Panel Reports, para. 7.894).

¹⁹⁶Joint appellees' submission of the United States and Mexico, para. 275 (quoting China's appellant's submission, para. 548).

¹⁹⁷Joint appellees' submission of the United States and Mexico, para. 281 (quoting China's appellant's submission, para. 596 (original emphasis)).

C. *Arguments of the European Union – Appellee*

1. Article 6.2 of the DSU

100. The European Union requests the Appellate Body to uphold the Panel's findings in paragraph 77 of its preliminary ruling (second phase), and in paragraph 7.3(b) of the Panel Reports, that Section III of the panel requests complies with Article 6.2 of the DSU, and to uphold all of the Panel's consequent findings of inconsistency.¹⁹⁸ The European Union contends that the Panel did not err under Article 6.2 of the DSU by finding that Section III of the panel requests presents the problem clearly.

101. In response to China's contention that the Panel observed defects in Section III of the panel requests, the European Union asserts that the Panel never found that the complainants' panel requests were defective. The European Union submits that, although the Panel observed that the complainants had not directly addressed in their submissions or in their subsequent oral statements the question of whether Section III of the panel requests was consistent with the requirements of Article 6.2 of the DSU, it "was not pointing to a 'defective' Panel Request".¹⁹⁹

102. The European Union also disagrees with China's contention that the Panel found that the complainants' responses to Panel Question 2 following the second Panel meeting corrected the defects in the panel requests. For the European Union, the replies given by the complainants to Panel Question 2 were merely a summary of the claims that had already been presented in more detail in the complainants' first written submissions.

103. The European Union further contends that its first written submission was sufficiently clear as to which Chinese measures were in violation of which WTO obligations. In the European Union's view, the scope of this dispute was therefore established early on in the proceedings.

104. Furthermore, in response to China's submission that it attaches great importance to the paramount principle that deficiencies in a panel request cannot be cured by a party's subsequent submissions, the European Union argues that this statement would only be relevant if the panel

¹⁹⁸In particular, the findings in paragraphs 7.669, 7.670, 7.678, 7.756, 7.807, 7.958, 7.1082, 7.1102, 7.1103, 8.4(a)-(b), 8.5(b), 8.6(a)-(b), 8.11 (a), (b), (c) and (f), 8.12(b), 8.13(a)-(b), 8.18(a)-(b), 8.19(b), and 8.20(a)-(b) of the Panel Reports. (See European Union's appellee's submission, para. 4)

¹⁹⁹European Union's appellee's submission, para. 15.

requests were in fact "defective", which, according to the European Union is not the case in the present dispute.²⁰⁰

105. Finally, in response to China's assertion that the Panel erred by frustrating China's due process rights under Article 6.2 of the DSU, the European Union contends that the fact that China defended, already in its first written submission, all the claims made by the complainants demonstrates that China had the opportunity to prepare exhaustively its defence in the earliest stages of the Panel proceedings. Finally, the European Union also disagrees with China that the Panel had allowed the complainants a "'long à la carte menu' from which they could choose in subsequent submissions ... the 'specific combination of measures and claims'".²⁰¹ The European Union asserts that, contrary to what China suggests, the European Union had "no choice at all" as regards the specific combinations of measures and claims at issue.²⁰²

2. The Panel's Recommendations

106. With regard to China's appeal of the Panel's recommendations, the European Union points out that the Panel made recommendations "on the 'series of measures', which comprise the 'relevant framework legislation, the implementing regulation(s), other applicable laws and the specific measure imposing export duties or export quotas in force at the date of the Panel's establishment'".²⁰³ The European Union recalls that the Panel was established on 21 December 2009 and, on that date, the 2010 "replacement measures" to which China refers in its appeal were not "*in force*": they entered into force on 1 January 2010.²⁰⁴ The European Union considers, therefore, that the Panel did not make recommendations that apply to 2010 replacement measures and China's appeal should be rejected "as baseless".²⁰⁵

107. Referring to China's concern that the Panel's recommendations may "require China to take action to revise" its "annual replacement measures"²⁰⁶, the European Union argues that the Appellate Body is not the "proper forum" to determine actions China should take to comply with its

²⁰⁰European Union's appellee's submission, para. 22.

²⁰¹European Union's appellee's submission, para. 26 (quoting China's appellant's submission, para. 96) (emphasis added by the European Union omitted)

²⁰²European Union's appellee's submission, para. 27.

²⁰³European Union's appellee's submission, para. 40 (quoting Panel Reports, para. 7.33(e)). (emphasis added by the European Union)

²⁰⁴European Union's appellee's submission, para. 40 (referring to Panel Reports, para. 7.32). (emphasis added by the European Union)

²⁰⁵European Union's appellee's submission, para. 41.

²⁰⁶European Union's appellee's submission, para. 43 (referring to China's appellant's submission, para. 100).

WTO obligations. Instead, Article 21 of the DSU provides the proper procedure that China should follow in order to identify these actions. For the European Union, this is another reason why China's appeal of the Panel's recommendations should be rejected.

3. Applicability of Article XX of the GATT 1994

108. The European Union requests the Appellate Body to uphold the Panel's findings and conclusions that China cannot invoke the defence of Article XX of the GATT 1994 for violations of the obligations contained in Paragraph 11.3 of China's Accession Protocol. While WTO Members can "incorporate" Article XX of the GATT 1994 into another agreement if they so wish, the legal basis for "applying" Article XX to another agreement would be the "very text of incorporation", and not Article XX itself, as Article XX is limited by its "express terms" to the GATT 1994.²⁰⁷ The European Union also asserts that the Panel was correct in finding that "China had 'exercised its inherent and sovereign right to regulate trade in negotiating, among other actions, the terms of its accession into the WTO'", and that the inherent right to regulate trade does not permit recourse to Article XX.²⁰⁸

(a) Paragraph 11.3 of China's Accession Protocol

109. The European Union disagrees with China's assertion that "the exception to [P]aragraph 11.3 in Annex 6 to China's Accession Protocol establishes a connection with Article XX of the GATT 1994".²⁰⁹ The "fundamental flaw" with this argument is that it is based on the premise that the use of the term "exceptional circumstances" in the text of the Note to Annex 6 establishes a "substantive overlap" with Article XX, which is entitled "General Exceptions".²¹⁰ Specifically, China's argument is flawed because it compares the term "exceptional circumstances" to "exceptions". The European Union notes that there is no "agreed definition or interpretation" of the phrase "exceptional circumstances" in the Note to Annex 6 of China's Accession Protocol, and highlights the fact that the word "exceptional" in the Note to Annex 6 is used as an adjective and not as a noun as in Article XX.²¹¹ Since an "exceptional circumstance" does not have the same meaning as an "exception" within the meaning of Article XX, China's argument takes the word "exceptional" out of context.²¹² The European Union faults China for searching "for similar words or phrases in other

²⁰⁷European Union's appellee's submission, para. 54.

²⁰⁸European Union's appellee's submission, para. 55 (referring to Panel Reports, paras. 7.155-7.157).

²⁰⁹European Union's appellee's submission, paras. 59.

²¹⁰European Union's appellee's submission, para. 62.

²¹¹European Union's appellee's submission, para. 62.

²¹²European Union's appellee's submission, para. 63.

WTO agreements" in order to make them applicable to Paragraph 11.3 of China's Accession Protocol.²¹³

110. The European Union further submits that China disregards the Panel's reasoning regarding the "fundamental difference"²¹⁴ between Paragraph 11.3 and Paragraph 5.1 of China's Accession Protocol, violations of which the Appellate Body has found can be justified under Article XX. That is, Paragraph 11.3 does not contain the introductory phrase "[w]ithout prejudice to China's rights to regulate trade in a manner consistent with the WTO Agreement" found in Paragraph 5.1.

111. The European Union also rejects China's argument that the reference to Article VIII of the GATT 1994 in Paragraph 11.3 of China's Accession Protocol confirms the "common intent"²¹⁵ of WTO Members to make Article XX applicable to Paragraph 11.3 as "pure conjecture".²¹⁶ To the contrary, the fact that there is a specific reference to Article VIII, but not to Article XX, indicates a common intent to exclude the applicability of Article XX. The European Union adds that it is "obscure from a systemic point of view" how the "express reference" to Article VIII could include a "tacit reference" to the availability of Article XX of the GATT 1994.²¹⁷

(b) Context from the *WTO Agreement*

112. In response to China's argument that Paragraph 170 of China's Accession Working Party Report justifies recourse to the exceptions contained in Article XX of the GATT 1994, although the European Union agrees that Paragraph 170 is integrated into China's Accession Protocol, it asserts that this fact does not make Article XX applicable to Paragraph 11.3 of China's Accession Protocol. Recalling China's argument that Paragraph 11.3 and Paragraph 170 overlap in terms of their subject matter, the European Union asserts that the Panel correctly identified the differences between Paragraph 170 and Paragraph 11.3. Regarding China's argument that the Panel erred in "assum[ing]" that Paragraph 170 does not apply to export duties because Paragraphs 155 and 156 of China's Accession Working Party Report apply to export duties, the European Union notes that the Panel recognized the importance of Paragraphs 155 and 156 as providing the context for interpreting Paragraph 170 of the Accession Working Party Report.²¹⁸ The European Union also highlights that

²¹³European Union's appellee's submission, para. 64.

²¹⁴European Union's appellee's submission, para. 70.

²¹⁵European Union's appellee's submission, para. 75 (referring to China's appellant's submission, para. 226).

²¹⁶European Union's appellee's submission, para. 77.

²¹⁷European Union's appellee's submission, para. 78.

²¹⁸European Union's appellee's submission, para. 85 (referring to Panel Reports, para. 7.145).

the Panel noted that Paragraphs 155 and 156 fall under section C of China's Accession Working Party Report entitled "Export Regulations", whereas Paragraph 170 falls under section D, entitled "Internal Policies Affecting Foreign Trade in Goods".

113. According to the European Union, China's argument that "the Panel appeared to consider that Paragraph 170 imposes obligations solely under the GATT 1994"²¹⁹ attempts to "distort" what the Panel had "actually stated"²²⁰; that Paragraph 11.3 of China's Accession Protocol includes an obligation to eliminate export duties that is not found in the GATT 1994, whereas "Paragraph 170 essentially repeats the commitments existing under certain GATT rules".²²¹

114. In response to China's argument that context from the *WTO Agreement* confirms the applicability of Article XX of the GATT 1994 as a justification for inconsistencies with Paragraph 11.3 of China's Accession Protocol, the European Union begins by noting that, under Article 31(1) of the *Vienna Convention*, context can only confirm the ordinary meaning given to the terms of the agreement, and since China has failed to show that the ordinary meaning establishes the applicability of Article XX to Paragraph 11.3, context alone cannot serve as the "constitutive element".²²² The European Union asserts that, although the preamble of the *WTO Agreement* contains elements such as general principles underlying the creation of the WTO, objectives of the multilateral trading system, and common expectations of Members, which may be relevant when assessing Article XX of the GATT 1994, the preamble cannot make Article XX applicable to specific obligations in a WTO legal instrument in the absence of a reference to Article XX in that instrument.

(c) The Inherent Right to Regulate Trade

115. The European Union disagrees with China that the Panel erred in its interpretation of Paragraph 11.3 of China's Accession Protocol by not recognizing China's inherent right to regulate trade. The European Union points out that the Panel recognized that this sovereign and inherent right is held by all WTO Members and reasoned that China had exercised this right when negotiating its accession to the WTO. The European Union agrees with the Panel that the provisions of the covered

²¹⁹European Union's appellee's submission, para. 87 (quoting China's appellant's submission, para. 242).

²²⁰European Union's appellee's submission, para. 88.

²²¹European Union's appellee's submission, para. 87 (quoting Panel Reports, para. 7.141).

²²²European Union's appellee's submission, para. 97.

agreements and China's Accession Protocol therefore "delineate" China's exercise of its inherent and sovereign right to regulate trade.²²³

4. Article XI:2(a) of the GATT 1994

116. The European Union requests the Appellate Body to reject China's appeal and also to reject China's claims that the Panel failed to conduct an objective assessment of the matter, as required under Article 11 of the DSU. With respect to the Panel's interpretation of the term "temporarily" in Article XI:2(a) of the GATT 1994, China misunderstands the Panel's statements that Article XI:2(a) should not be interpreted to permit the "long-term application of conservation measures", or "long-term measures related to conservation purposes".²²⁴ For the European Union, these statements do not mean that the Panel found that Article XI:2(a) does not cover any "long-term" export restrictions, but rather that Article XI:2(a) does not cover any "long-term conservation measures".²²⁵

117. Further, the European Union takes issue with China's assertion that the annual renewal of China's export restrictions means that the restrictions have a relatively short duration of one year and that their duration is defined in relation to the time required to prevent or relieve the critical shortage. In the European Union's view, the annual renewal of China's measures implies that, at the beginning of each year, China expects that the shortage of refractory-grade bauxite will cease by the end of the year, but at year-end, China realizes that this expectation was incorrect and adapts its expectation that the shortage will cease one year later, and so on, until final depletion of the reserves. For the European Union, this indicates that China's annual renewal of export restrictions does not have any impact on whether the restrictions are applied "temporarily".

118. The European Union also takes issue with China's contention that the Panel found that Article XI:2(a) and Article XX(g) of the GATT 1994 are mutually exclusive. The European Union maintains that the Panel did not make such a finding, but instead used a comparison between the two Articles only to draw additional support for its interpretation. On the basis of that analysis, the Panel rightly concluded that Article XX(g) is confined to conservation measures, while Article XI:2(a) covers "exceptional measures" that address situations of crisis.²²⁶

119. With respect to the Panel's interpretation of the term "critical shortages", the European Union submits that the Panel found that Article XI:2(a) does not cover all types of critical shortages, but

²²³European Union's appellee's submission, para. 109.

²²⁴European Union's appellee's submission, para. 174 (quoting Panel Reports, para. 7.349).

²²⁵European Union's appellee's submission, para. 175. (original emphasis)

²²⁶European Union's appellee's submission, para. 165 (quoting Panel Reports, para. 7.301).

deals only with a subset, namely those critical shortages that are "capable of being 'prevented or relieved' through the 'temporary application' of export restrictions".²²⁷ Thus, a "critical shortage" is capable of being prevented or relieved through an export restriction that is "temporarily applied", only if the critical shortage itself is "temporary".

120. The European Union takes issue with China's allegation that the Panel found that "conservation measures" can never fall within the scope of Article XI:2(a) and contends that, rather, the Panel found that China's export quota on refractory-grade bauxite is not covered by Article XI:2(a). The European Union submits that the purpose of the export quota, as acknowledged by China, was not to "prevent" or "relieve" a critical shortage, but to "extend the reserves" for "current and future generations".²²⁸ The limited life span of the reserves of a good, however, is not sufficient for a finding of a "critical shortage" in the sense of Article XI:2(a). In the European Union's view, Article XI:2(a) covers export restrictions that act as a "bridge" until a crisis is resolved and normality returns. In that sense, the gradual depletion of natural resources may well create a shortage in the availability of a good, however, such shortage does not fall within the scope of Article XI:2(a), because it is not "temporary".²²⁹ Absent extraordinary circumstances, such as an unexpected discovery of new reserves, there is no point in time where it could reasonably be expected that the shortage would cease to exist and the availability of the good would return to normal conditions. The European Union submits that "a shortage caused by the limited natural reserves of the good is *the normal condition* for the availability of the good".²³⁰

121. For the European Union, a shortage caused by the depletion of natural resources is different from the "critical shortage" occurring in situations of crisis. The former can be addressed by conservation measures seeking to extend the duration of the resources. The latter can be addressed by temporary measures seeking to prevent or relieve the effects of a crisis. For the European Union, the text of Article XI:2(a) covers only the latter situation. This does not mean that Article XI:2(a) can never cover goods with a limited reserve. The European Union gives the example of a mining accident, which would cause a severe decrease in the quantity of refractory-grade bauxite in China. The ensuing shortage of the good could fall within the scope of Article XI:2(a) because it would be

²²⁷European Union's appellee's submission, para. 135.

²²⁸European Union's appellee's submission, para. 147.

²²⁹European Union's appellee's submission, para. 150.

²³⁰European Union's appellee's submission, para. 150. (original emphasis)

capable of being relieved through measures applied for the time needed to bring the mine back to operation, and the market conditions back to their "normal", gradually depleting situation".²³¹

122. Finally, in response to China's allegation that the Panel erred under Article 11 of the DSU because it failed to assess properly evidence that China's export restrictions are annually reviewed and renewed, the European Union contends that the above considerations relating to China's review and renewal mechanism support the Panel's finding that a withdrawal of the restrictions is not to be expected until the depletion of the reserves, and that this finding was based on accurate findings of fact. The European Union also objects to China's allegation that the Panel found that there was no possibility for an existing shortage of an exhaustible natural resource to cease to exist, and that the Panel thereby acted inconsistently with Article 11 of the DSU. The European Union contends that the Panel did not make such a finding. Instead, the Panel relied on the fact that the restriction had been in place "for at least a decade" and that there was no indication that it would be lifted.

5. Article XX(g) of the GATT 1994

123. The European Union requests the Appellate Body to uphold the Panel's interpretation of the phrase "made effective in conjunction with" in Article XX(g) of the GATT 1994. The European Union takes issue with China's allegation that the Panel found that a restriction on international trade must pursue a dual purpose of conserving a natural resource and of seeking to ensure the effectiveness of domestic restrictions on that resource. For the European Union, the Panel referred only to one and the same purpose, namely the conservation of a natural resource, for both the restriction on international trade and the restrictions on domestic production or consumption.

124. Furthermore, the European Union argues that the word "purpose" in paragraph 7.397 of the Panel Reports closely reflects the language used in paragraph 4.6 of the GATT panel report in *Canada – Herring and Salmon*, which rightly stated that a measure "can only be made [effective] in conjunction" with domestic restrictions on production, if it is primarily aimed at rendering effective these restrictions".²³² The European Union further submits that the domestic restrictions on production or consumption must, by their very nature, have the purpose or aim of conserving natural resources. It would be difficult to imagine a situation in which a domestic restriction on the

²³¹European Union's appellee's submission, para. 154.

²³²European Union's appellee's submission, para. 195 (quoting GATT Panel Report, *Canada – Herring and Salmon*, para. 4.6). (emphasis added by the European Union omitted)

production or consumption of a natural resource would have a "purpose" other than conservation of the same natural resource.²³³

6. Prior Export Performance and Minimum Capital Requirements

125. As a preliminary matter, the European Union argues that China's appeal concerning examination and approval systems for WTO-consistent export quotas is "ineffective" since China has not appealed the Panel's finding that the export quotas are inconsistent with the GATT 1994.²³⁴ The European Union, therefore, questions whether the Appellate Body should rule on China's appeal regarding China's prior export performance and minimum capital requirements.²³⁵

126. In any event, the European Union considers that the Panel correctly found that China's prior export performance and minimum capital requirements imposed on exporters of bauxite, coke, fluorspar, and silicon carbide are inconsistent with China's obligations under Paragraph 5.1 of its Accession Protocol and Paragraphs 83 and 84 of China's Accession Working Party Report. The European Union submits that these provisions require that China: (i) eliminate its system of examination and approval of trading rights; (ii) grant the right to trade to all Chinese enterprises (both Chinese-invested and foreign-invested) and to all foreign enterprises and individuals; and (iii) eliminate the "minimum capital" and the "prior experience" requirements for foreign enterprises, after the end of the phase-in period.²³⁶

127. The European Union further notes that China seeks to justify the continued use of its prior export performance and minimum capital requirements on the basis of its alleged right to adopt WTO-consistent "quota allocating criteria", its need to "allocate the quota through criteria that restrict the volume of exports to quota volume"²³⁷, its right to "maintain quota allocation rules"²³⁸, and its right to "establish quota allocation rules".²³⁹ Yet, China's prior export performance and minimum capital requirements are not "export quota allocation criteria" or part of an "export quota allocation system". Rather, China uses these requirements only at the stage of prior examination and approval. The

²³³European Union's appellee's submission, para. 201.

²³⁴European Union's appellee's submission, para. 214.

²³⁵European Union's appellee's submission, para. 216.

²³⁶European Union's appellee's submission, para. 224.

²³⁷European Union's appellee's submission, para. 231 (referring to China's appellant's submission, para. 443).

²³⁸European Union's appellee's submission, para. 231 (referring to China's appellant's submission, para. 444).

²³⁹European Union's appellee's submission, para. 231 (referring to China's appellant's submission, para. 568).

European Union considers that this is an additional reason for which this aspect of China's appeal should be dismissed.

128. The European Union further argues that allowing China to treat Chinese-invested enterprises differently from foreign-invested enterprises would be contrary to the general structure of the obligations undertaken by China in Paragraphs 83 and 84 of its Accession Working Party Report.

7. China's "Operation Capacity" Criterion and Article X:3(a) of the GATT 1994

129. The European Union requests the Appellate Body to uphold the Panel's finding that China's allocation of export quotas through the use of the "operation capacity" criterion is inconsistent with Article X:3(a) of the GATT 1994, and to reject China's claim that the Panel acted inconsistently with Article 11 of the DSU. The European Union disagrees with China's contention that, in the light of the absence of evidence demonstrating WTO-inconsistent application, China was entitled to the presumption that it would act in accordance with its WTO obligations. The European Union contends that the Panel found that there are 32 different local departments in China interpreting and applying the "operation capacity" criterion, and that Chinese legislation does not define the notion of "operation capacity" or offer any standard on the basis of which the local departments should assess that criterion. For the European Union, it is therefore difficult to see how China's 32 local departments can always interpret and apply the "operation capacity" criterion in the same way, as a result of their own choice. Rather, the logical conclusion would seem to be that, if the 32 local departments ever interpret and apply this in the same way, this would be sheer coincidence.

130. The European Union also takes issue with China's argument that, where an authority is faced with a domestic measure of uncertain meaning, the theoretical risk that the authority might choose a WTO-inconsistent meaning does not render the measure "as such" WTO-inconsistent. The Panel did not find that the "operation capacity" criterion was "as such" WTO-inconsistent. Rather, it found that China's administration of its direct allocation of export quotas is inconsistent with Article X:3(a).

131. In the European Union's view, China attempts to draw an artificial distinction between types of certainty so as to distinguish the facts of the present case from the facts in *Argentina – Hides and Leather*. Yet, just as the facts in the present case create a "very real risk" of administration inconsistent with Article X:3(a)²⁴⁰, the panel in *Argentina – Hides and Leather* found that the risk that information might be improperly used was sufficient to lead to a finding of unreasonable and partial

²⁴⁰European Union's appellee's submission, para. 319.

administration.²⁴¹ The European Union argues therefore that the analysis and findings by the panel in *Argentina – Hides and Leather* support the Panel's analysis and findings in this case.

132. The European Union stresses that the Panel correctly found China's administration of its direct allocation of export quotas to be inconsistent with Article X:3(a) on the basis that the "operation capacity" criterion could not be applied "consistently in the same manner, both over time and in different places" and 'in respect of all traders'²⁴², and that the Panel did not find that the "operation capacity" criterion was *per se* inconsistent.²⁴³ In other words, contrary to what China asserts, the Panel did not find that a theoretical risk that the Chinese authorities may exercise their discretion to adopt a WTO-inconsistent meaning for the term "operation capacity" thereby renders the measure "as such" WTO-inconsistent.²⁴⁴

133. The European Union also disagrees with China's assertion that there is no evidence to support the Panel's assessment regarding the likelihood of the risk of inconsistent administration as being "very real".²⁴⁵ The Panel's findings that the risk is "very real" were supported by the "undisputed fact[]" that there is "no definition, standard or guidelines" for the 32 local departments charged with interpreting and applying the "operation capacity" criterion.²⁴⁶ The European Union therefore requests that the Appellate Body reject China's assertion that the Panel acted inconsistently with Article 11 of the DSU in its analysis of this issue.

8. China's Export Licensing Requirements and Article XI:1 of the GATT 1994

134. The European Union requests the Appellate Body to uphold the Panel's finding that Article 11(7) of the *2008 Export Licence Administration Measures*, and Articles 5(5) and 8(4) of the *2008 Export Licensing Working Rules* are inconsistent with Article XI:1 of the GATT 1994.²⁴⁷ The European Union also requests the Appellate Body to reject China's claim that the Panel erred under Article 11 of the DSU by making this finding without a sufficient evidentiary basis. The European Union disagrees with China's argument that allowing export licensing agencies the

"discretion" to grant or refuse export licences is not inconsistent with Article XI:1 of the GATT 1994.²⁴⁸

135. The European Union takes issue with China's distinction between discretion to apply or not a domestic legal provision that mandates WTO-inconsistent action, and discretion to apply an ambiguous provision in a WTO-consistent manner. The European Union argues that such a distinction makes little difference to individual economic operators and other WTO Members. China's interpretation would contradict the purpose of Article XI:1, which is "to protect traders and create the *predictability* needed to plan future trade".²⁴⁹ The European Union contends that both types of "discretion" create uncertainty which, in turn, "leads to increased transaction costs and has negative economic impact".²⁵⁰

136. The European Union submits that China's position is inconsistent with the interpretation of Article XI:1 of the GATT 1994 given by WTO panels. The discretion accorded to Chinese licensing authorities in this case to require undefined documents resembles the discretion enjoyed by the Indian licensing authorities when granting licences on the basis of unspecified "merits", which the panel in *India – Quantitative Restrictions* found to be inconsistent with Article XI:1.²⁵¹

137. The European Union further disagrees with China's assertion that, where there is an "ambiguous" domestic measure that can always be interpreted and applied in a WTO-consistent manner, it must be presumed that the respondent will abide by its WTO obligations in applying such measure. The "ambiguous" domestic measure could also always be interpreted and applied in a WTO-inconsistent manner. For the European Union, Article XI:1 protects the rights of traders and other WTO Members and "does not create 'presumptions of WTO consistency'" for responding parties.²⁵²

138. The European Union also rejects China's assertion that the Panel acted inconsistently with Article 11 of the DSU by making findings under Article XI:1 of the GATT 1994 without a sufficient evidentiary basis. Contrary to what China argues, the Panel did not simply presume "that Chinese license-issuing authorities will one day choose to request additional documents of such a nature so as

²⁴¹European Union's appellee's submission, para. 318 (referring to Panel Report, *Argentina – Hides and Leather*, para. 11.92).

²⁴²European Union's appellee's submission, para. 309 (quoting Panel Reports, para. 7.749).

²⁴³European Union's appellee's submission, para. 309.

²⁴⁴European Union's appellee's submission, para. 307.

²⁴⁵European Union's appellee's submission, para. 326.

²⁴⁶European Union's appellee's submission, para. 327.

²⁴⁷European Union's appellee's submission, para. 285.

²⁴⁸European Union's appellee's submission, para. 253 (referring to China's appellant's submission, paras. 569, 580, and 582).

²⁴⁹European Union's appellee's submission, para. 260 (referring to Panel Report, *US – Section 301 Trade Act*, para. 7.84) (emphasis added by the European Union)

²⁵⁰European Union's appellee's submission, para. 260 (referring to Panel Report, *US – Section 301 Trade Act*, para. 7.84).

²⁵¹European Union's appellee's submission, para. 263 (referring to Panel Reports, para. 7.920).
²⁵²European Union's appellee's submission, para. 266.

to impose a 'restriction' on export[s]".²⁵³ Instead, based on its understanding of the relevant legal provisions, the Panel found that the very existence of China's authorities' discretion to require undefined and unspecific documents "created uncertainty as to an applicant's ability to obtain an export licence", and was therefore inconsistent with Article XI-1 of the GATT 1994.²⁵⁴ The European Union argues that the text of China's relevant measures "was the proper 'evidentiary basis' for the Panel's finding, and that China's assertion that its authorities had never rejected any export license application relating to manganese and zinc was not relevant for the Panel's analysis."²⁵⁵

D. *Claims of Error by the United States – Other Appellant*

1. Conditional Appeal regarding the Panel's Recommendations

139. The United States and Mexico assert that the outcome of the Panel's approach to making findings and recommendations in this dispute is consistent with the covered agreements and supported by the record in this dispute. Specifically, the Panel properly concluded that it would make findings and recommendations on the measures operating together (the "series of measures") to impose export duties or export quotas on the raw materials at issue.²⁵⁶ The United States and Mexico request the Appellate Body to review the Panel's recommendations on the export quota and export duty measures only in the event that, pursuant to China's appeal, the Appellate Body reverses the Panel's recommendations in paragraphs 8.8, 8.15, and 8.22 of the Panel Reports and finds that no recommendation should have been made by the Panel on the "series of measures" as they existed when the Panel was established.

140. The United States and Mexico submit that the complainants challenged a number of export restraints in a "logical way" that reflected the structure of the legal instruments that give effect to the challenged export duties and export quotas.²⁵⁷ In addition to seeking findings that the measures at issue were inconsistent with WTO rules, the complainants sought recommendations with respect to these measures that would ensure that the export duties and quotas at issue would be within the scope of any future compliance proceedings under Article 21.5 of the DSU. According to the United States

²⁵³European Union's appellee's submission, para. 280 (quoting China's appellant's submission, para. 599).

²⁵⁴European Union's appellee's submission, para. 281 (quoting Panel Reports, para. 7.948).

²⁵⁵European Union's appellee's submission, para. 283. The European Union further contends that China's assertion in this respect was not proved during the Panel proceedings, because the complainants did not have access to the relevant information in order to corroborate or challenge it.

²⁵⁶United States' other appellant's submission, para. 38 (referring to Panel Reports, paras. 7.17, 7.33, 7.60-7.68, 7.76, 7.80, 7.83, 7.86, 7.89, 7.94, 7.97, and 7.218-7.224).

²⁵⁷United States' other appellant's submission, para. 41.

and Mexico, the adoption of a recommendation by the DSB was a "critical objective" in achieving a "positive solution to the dispute", in terms of Article 3.7 of the DSU.²⁵⁸

141. The United States and Mexico highlight that, during the Panel proceedings, China tried to avoid responsibility for the challenged trade barriers by asking the Panel to "shift the focus" of its review from the measures as they existed at the time of the establishment of the Panel to later points in time.²⁵⁹ By contrast, the complainants asked the Panel to focus its review on the challenged measures in effect at the time of its establishment, because focusing on the legal situation at a later time would be tantamount to permitting China to "move the target" and "shield important parts of the export restraint regimes" from scrutiny.²⁶⁰ The United States and Mexico request the Appellate Body to make a recommendation that "clearly is aimed at securing a positive resolution to this ongoing dispute", as only such a resolution would prevent an "endless loop of WTO dispute settlement proceedings".²⁶¹

142. In the event that the Appellate Body finds that no recommendation should have been made by the Panel on the "series of measures" as they existed at the time of Panel establishment, and reverses the Panel's recommendations with respect to the replacement measures, the United States and Mexico assert that the Panel erred under Articles 6.2, 7.1, 11, and 19.1 of the DSU in not making recommendations on the 2009 export duty and export quota measures that were annually recurring and in effect on the date of Panel establishment. The United States and Mexico note that it is "undisputed" that the Panel correctly found that these measures, which were annually recurring and in existence at the time the Panel was established but were subsequently superseded by other legal instruments, were inconsistent with China's obligations under Article XI:1 of the GATT 1994 and Paragraph 11.3 of China's Accession Protocol. However, in the light of Article 19.1 of the DSU and the circumstances of this dispute where recurrence of a violation is likely, the Panel erred in not making a recommendation on the basis of its finding that, on the date the Panel was established, those measures were inconsistent with China's WTO obligations. According to the United States and

²⁵⁸United States' other appellant's submission, para. 42.

²⁵⁹United States' other appellant's submission, para. 44 (referring to China's first written submission to the Panel, paras. 63-67; China's second written submission to the Panel, paras. 6-18; and China's opening statement at the second Panel meeting, paras. 3-11).

²⁶⁰United States' other appellant's submission, para. 44 (referring to the complainants' joint oral statement at the first Panel meeting, paras. 45 and 51; United States' second written submission to the Panel, paras. 341 and 342; United States' opening statement at the second Panel meeting, paras. 109-111; Mexico's second written submission to the Panel, paras. 346-348; and Mexico's opening statement at the second Panel meeting, paras. 6-9).

²⁶¹United States' other appellant's submission, para. 45.

Mexico, the Panel "misconstrued" its terms of reference and the "relevant point in time" for its analysis of these annually recurring measures.²⁶²

143. The United States and Mexico seek to distinguish the present case from *US – Certain EC Products*, where the Appellate Body found that the panel had erred in making a recommendation on an expired measure. First, unlike *US – Certain EC Products*, where the measure at issue had ceased to exist prior to the establishment of the panel, in the present dispute, the annual export duty and quota measures were in effect on the date the Panel was established. Second, the measure at issue in *US – Certain EC Products* was not one that was "maintained over time through the annual recurrence of legal instruments"; whereas, in the present dispute, even though the impugned legal instruments have been superseded, these measures nonetheless maintain legal effect through the recurrence of the following year's legal instrument.²⁶³

144. The United States and Mexico recall that, throughout the Panel proceedings, China introduced, amended, and repealed a number of legal instruments, decreasing the burden of export restraints imposed on bauxite and fluorspar, with a view to justifying the imposition of the export restraints on these products under Article XX of the GATT 1994. This could have effectively prevented the complainants from getting recommendations on the challenged measures found to be inconsistent as of the date the Panel was established. According to the United States and Mexico, a "correct and reasonable interpretation from a systemic point of view" avoids creating a "loophole" in the system whereby complainants could find themselves "taking aim" at "appearing and disappearing targets", and whereby WTO Members could evade a panel's scrutiny by removing measures during panel proceedings and reinstating them in the future without any consequences.²⁶⁴

2. Article VIII:1(a) of the GATT 1994 and Paragraph 11.3 of China's Accession Protocol

145. The United States requests the Appellate Body to reverse the Panel's conclusion that China's requirement for enterprises to pay a bid-winning fee in order to export bauxite, fluorspar, and silicon carbide under its export quota regime is not inconsistent with Article VIII:1(a) of the GATT 1994 and Paragraph 11.3 of China's Accession Protocol.

146. First, the United States alleges that the Panel incorrectly found that China's bid-winning fee is not a fee or charge "imposed on or in connection with ... exportation" in the sense of

²⁶²United States' other appellant's submission, para. 56.

²⁶³United States' other appellant's submission, paras. 60 and 61.

²⁶⁴United States' other appellant's submission, paras. 70 and 71.

Article VIII:1(a), notwithstanding the fact that payment of the fee is a legal prerequisite for exportation, and is a requirement imposed in relation to the administration of a quantitative restriction. The Panel properly recognized that the phrase "on or in connection with ... exportation" has a "broad temporal view", and explained that Article VIII:1(a) refers to fees or charges that are applied not only "at the moment in time of exportation" but also "in association with exportation".²⁶⁵ However, the United States contends that the Panel erred by adding an additional test, namely that fees and charges in connection with exportation would "typically" be limited to "specific fees, charges, formalities or requirements, associated with customs-related documentation, certification and inspection, and statistical matters".²⁶⁶ This is also inconsistent with the context provided by Article VIII:4 of the GATT 1994, because China's bid-winning fee falls within the examples of items (b) "quantitative restrictions" and (c) "licensing" of the list set out in that provision. In addition, the United States argues that the Panel's reliance on the GATT panel report in *US – Customs User Fee* does not support the conclusion that the bid-winning fee is not a fee imposed on or in connection with exportation, because the part of that GATT panel's reasoning cited by the Panel in the present case relates to the meaning of the term "services rendered" and not to the meaning of "on or in connection with ... exportation".

147. Second, the United States alleges that the Panel erred in concluding that Article VIII of the GATT 1994 is not applicable to China's bid-winning fee because it does not relate to any service rendered. The Panel correctly concluded that the bid-winning fee is not related to the approximate cost of a service rendered, but, for the United States, this conclusion weighs in favour of a finding that the fee is inconsistent with Article VIII:1(a), and not of a finding that the fee falls outside the scope of Article VIII altogether. The latter finding would turn Article VIII on its head, allowing a Member to impose any fee at any level, even where there was no service rendered.

148. The United States also takes issue with the Panel's statement that, because bid-winning fees would necessarily be "variable", such fees could not be related to any service rendered.²⁶⁷ The mere fact of "variability" does not mean that a fee is necessarily disconnected from services rendered. In addition, a finding that a certain type of fee might always be inconsistent with Article VIII:1(a) does not mean that the fee, for that reason alone, falls outside the scope of Article VIII. Instead, in the United States' view, if it does not meet the requirement of being limited to the approximate cost of services rendered, then such a fee is inconsistent with Article VIII:1(a).

²⁶⁵United States' other appellant's submission, para. 19 (quoting Panel Reports, para. 7.823).

²⁶⁶United States' other appellant's submission, para. 20 (quoting Panel Reports, para. 7.832).

²⁶⁷United States' other appellant's submission, para. 35 (referring to Panel Reports, para. 7.850).

149. Finally, the United States submits that the Panel erred in finding that China's imposition of a bid-winning fee is not inconsistent with Paragraph 11.3 of China's Accession Protocol. The Panel's analysis of the bid-winning fee under Paragraph 11.3 of the Accession Protocol flowed from its Article VIII:1(a) analysis, and was therefore similarly flawed.

E. *Claims of Error by Mexico – Other Appellant*

1. Conditional Appeal regarding the Panel's Recommendations

150. Mexico incorporates by reference into its other appellant's submission the arguments concerning the Panel's recommendations on annual export quota and export duty measures set out in section IV of the United States' other appellant's submission.²⁶⁸

2. Involvement of the CCCMC in the Allocation of Export Quotas and Article X:3(a) of the GATT 1994

151. Mexico requests the Appellate Body to reverse the Panel's findings that the involvement of the CCCMC in China's administration of its export quota regime is consistent with Article X:3(a) of the GATT 1994, including the Panel's findings concerning the interpretation and application of Article X:3(a).²⁶⁹ Mexico contends that the Panel erred in its interpretation of Article X:3(a) by requiring complainants bringing "as such" claims to demonstrate that a challenged measure necessarily leads to partial and/or unreasonable administration. Since Mexico's claims relate to the structure rather than the application of China's quota allocation system, no evidence of actual partial or unreasonable administration was required, nor was it necessary to show that partial or unreasonable application would inevitably result. To require evidence of partiality or unreasonableness would "ignore[] the realities of the social and political context in which the trade association's activities take place".²⁷⁰

152. The Panel does not explain the legal basis for its "very real risk" standard, which is not reflected in the text of Article X:3(a).²⁷¹ However, since the CCCMC is made up of competitors, regardless of its administrative function, Mexico contends that "it must be assumed that a significant

²⁶⁸Mexico's other appellant's submission, para. 16 (referring to United States' other appellant's submission, section IV).
²⁶⁹Mexico's other appellant's submission, para. 61.
²⁷⁰Mexico's other appellant's submission, para. 31.
²⁷¹Mexico's other appellant's submission, para. 36.

possibility exists" that the CCCMC's decisions will lack objectivity and "be distorted in some degree", and that applicants' confidential information "may be leaked" to competitors.²⁷²

153. Mexico suggests that the involvement of the CCCMC in the quota allocation process "lead[s] to an inherent conflict of interest" that "results in partial or unreasonable" administration contrary to Article X:3(a).²⁷³ A risk of inconsistent administration exists whenever a private party "responsible for assisting in the administration ... has commercial interests" adverse to those of the applicants.²⁷⁴ This risk increases when the private party "exercises discretionary authority over applicants", and becomes even more problematic when the private party "is granted access to the confidential business information" of the applicants.²⁷⁵

154. Specifically, in the context of partial administration, Mexico contends that the Panel's finding that the CCCMC played a purely "administrative/clerical function" in the quota administration process is factually incorrect.²⁷⁶ Even assuming *arguendo* that the CCCMC's role is merely administrative, it may still present a "very real risk" of partial administration.²⁷⁷ The panel in *Argentina – Hides and Leather* found partial administration where a private party association with conflicting commercial interests played an observatory role in the customs classification process, but was, according to Mexico, not in a position to influence the result of the process. While the Panel in this dispute "purported to agree with [this] approach", it then "effectively disregarded" it by finding that an inherent conflict of interest can be remedied if the party with the adverse interest does not have "influence in the process".²⁷⁸ Mexico suggests that the fact that China's export quota regime "inherently contains the possibility of disclosure of confidential business data to commercial competitors" means that its administration is unreasonable, even if the confidential information submitted by quota applicants is required and relevant to the CCCMC's task.²⁷⁹

155. Finally, Mexico contends that the Panel failed to make an objective assessment of the facts as required by Article 11 of the DSU. Rather than evaluating the evidence on record in its totality, the Panel only considered isolated aspects of China's regime and ignored other evidence regarding the CCCMC's responsibilities. If the Panel had made an objective assessment, it would have found that

²⁷²Mexico's other appellant's submission, para. 58.
²⁷³Mexico's other appellant's submission, para. 39.
²⁷⁴Mexico's other appellant's submission, para. 39.
²⁷⁵Mexico's other appellant's submission, para. 39.
²⁷⁶Mexico's other appellant's submission, para. 43.
²⁷⁷Mexico's other appellant's submission, para. 42.
²⁷⁸Mexico's other appellant's submission, para. 42 (referring to Panel Reports, para. 7.77).
²⁷⁹Mexico's other appellant's submission, para. 46.

the CCCMC's role is not purely administrative, and that the CCCMC has "a significant amount of discretion" regarding which applicants receive export quotas.²⁸⁰ For example, in the context of the direct quota allocation system for coke, the CCCMC is the "sole administrative division" that "reviews, evaluates, and recommends which applicants qualify for consideration by MOFCOM".²⁸¹ In the context of the quota bidding system, the CCCMC not only plays a significant role in the composition of the Bidding Offices, but also "evaluates, verifies, and recommends applicants" with respect to certain raw materials. In addition, while the CCCMC does not make final determinations, its verification of applicants' qualifications for consideration without any "real oversight" has "obvious implications" for the final outcomes.²⁸² In Mexico's view, had the Panel made an objective assessment of this matter, it would have found that the requirement to provide confidential business information to the CCCMC "created an inherent conflict of interest that result[ed] in a partial and unreasonable administration".²⁸³

F. *Claims of Error by the European Union – Other Appellant*

1. Conditional Appeal regarding the Panel's Recommendations

156. The European Union submits a conditional appeal in the event the Appellate Body were to accept the relevant ground of appeal raised by China *and* reject the relevant other appeals submitted by the United States and Mexico. In that case, the European Union would argue that the Panel erred when it found that the European Union "requested the Panel not to make findings or recommendations on the legal instruments taking effect on 1 January 2010" and that the European Union "narrowed the Panel's terms of reference during the course of the proceedings".²⁸⁴ The European Union submits several arguments in support of its assertion.

157. First, the European Union observes that the Panel relied on the European Union's statement that it "agrees with the views expressed by the United States and Mexico in their opening statement".²⁸⁵ The European Union submits that it "never explicitly or implicitly stated that it withdraws its claims on replacement measures, or that it narrows the Panel's terms of reference".²⁸⁶

²⁸⁰Mexico's other appellant's submission, para. 53.

²⁸¹Mexico's other appellant's submission, para. 53. (original emphasis)

²⁸²Mexico's other appellant's submission, para. 56.

²⁸³Mexico's other appellant's submission, para. 60.

²⁸⁴European Union's other appellant's submission, para. 3 (referring to Panel Reports, paras. 7.21 and 7.22).

²⁸⁵European Union's other appellant's submission, para. 21 (referring to Panel Reports, para. 7.21 and footnote 62 thereto).

²⁸⁶European Union's other appellant's submission, para. 25.

The European Union argues that "[a] simple statement that a party generally agrees with the views expressed by the other complainants cannot be interpreted as that party's incorporation of the other complainants' claims and arguments into its own case."²⁸⁷ Therefore, the Panel erred in finding that the European Union requested the Panel to "narrow" its terms of reference.²⁸⁸

158. Second, with respect to the Panel's reliance on the European Union's argument that the legal instrument subjecting bauxite to an export duty in 2009 was within the Panel's terms of reference, the European Union alleges that the statement of the European Union to which the Panel refers did not discuss replacement measures at all. Instead, it discussed the way the Panel should treat expired measures that were not replaced, and could not have been the basis for a finding that the European Union had withdrawn its claims on measures that were replaced.

159. Third, with respect to the Panel's reliance on the European Union's inclusion of only one measure that took effect after 1 January 2010 in certain tables provided to the Panel in response to questions, the European Union observes that the Panel asked for the tables in order to assess China's assertion that the European Union's first written submission to the Panel did not specify the challenged legal instruments in sufficient detail. The European Union considers that there was no basis for the Panel to consider, based on these responses, that the European Union was requesting the Panel not to make findings on legal instruments taking effect after 1 January 2010.

160. In the European Union's view, since the Panel erred in excluding "the 'amendments or extensions, replacement measures, renewal measures and implementing measures' that took effect after January 1 2010" from its terms of reference, the Panel acted inconsistently with its obligations under Article 7.1 of the DSU, which obliges panels to respect their terms of reference.²⁸⁹ According to the European Union, a panel's interpretation of a party's written submissions, oral statements, and replies to questions constitute a part of the panel's assessment of the "matter" before it and thus, the Panel's failure to make an objective assessment in this respect was inconsistent with Article 11 of the DSU. The European Union also argues that, as a result of the Panel's erroneous determination of its terms of reference, and its "consequent failure" to make findings on the consistency of the replacement measures, the Panel failed to recommend that China bring its replacement measures into compliance with the covered agreements, thereby acting inconsistently with Article 19.1 of the DSU.²⁹⁰ The European Union requests the Appellate Body to complete the Panel's analysis and find

²⁸⁷European Union's other appellant's submission, para. 8.

²⁸⁸European Union's other appellant's submission, para. 8.

²⁸⁹European Union's other appellant's submission, para. 46.

²⁹⁰European Union's other appellant's submission, paras. 46-49.

that the 2010 replacement measures are inconsistent with China's obligations under Article XI of the GATT 1994; and to recommend that China bring the measures into compliance with its WTO obligations.

G. *Arguments of China – Appellee*

1. Conditional Appeals of the United States and Mexico regarding the Panels' Recommendations

161. China recalls that the appeals by the United States and Mexico are conditional upon the Appellate Body upholding China's appeal that the Panel was not entitled to make a recommendation regarding the "series of measures" that extends to replacement measures. China highlights that, in their conditional other appeal, the United States and Mexico requests the Appellate Body to find that the Panel erred in failing to make a recommendation regarding the expired 2009 measures that extends to replacement measures. However, if the Appellate Body finds that the recommendation regarding a "series of measures" cannot extend to replacement measures, as requested by China, then a recommendation regarding the expired 2009 measures cannot extend to the replacement measures either, because they were excluded from the Panel's terms of reference.

162. Regarding the argument by the United States and Mexico that the Appellate Body's findings in *US – Certain EC Products* do not apply to measures that expire after a panel's establishment, China submits that the Appellate Body's finding in that case was not dependent on the measure at issue expiring before a panel's establishment. Rather, the Appellate Body's finding is premised on a "straightforward" view that, if a measure no longer exists, it cannot be modified or withdrawn, and that, therefore, there is no legal basis for a recommendation under Article 19.1 of the DSU, because the DSB cannot "compel" a Member to undertake action that can no longer be undertaken.²⁹¹ In support of its argument, China refers to the panel report in *US – Poultry (China)*, where the panel refused to make a recommendation regarding the impugned US measure in that case because the measure had expired after the panel's establishment.

163. China observes that the United States and Mexico distinguish between "legal instruments" and "measures"²⁹², and suggests that their conception of a "measure" consists of an "*ongoing conduct*" that stretches into the future through 'individual legal instruments', with the alleged ongoing conduct

²⁹¹ China's appellee's submission, paras. 84 and 85.

²⁹² China's appellee's submission, para. 89 (referring to United States' other appellant's submission, para. 61; and Mexico's other appellant's submission, paras. 5 and 6). (emphasis added by China omitted)

in this case being the "maintenance" of export duties and quotas on certain products "over time".²⁹³ China notes that the particular arguments put forward by the United States and by Mexico are "highly reminiscent" of the arguments made by Brazil and by the European Union in *US – Orange Juice (Brazil)* and *US – Continued Zeroing*, respectively, but contends that these "analogies are misplaced".²⁹⁴ Unlike in *US – Continued Zeroing* and *US – Orange Juice (Brazil)*, the complainants did not identify any "ongoing conduct" measure that 'serves to maintain the imposition of export duties and quotas over time' in their panel requests.²⁹⁵

164. According to China, the evidentiary standard for demonstrating the existence of an "ongoing conduct" measure is high, and requires a "density" of facts, over time, to demonstrate [its] existence'.²⁹⁶ China asserts that, in the present dispute, the complainants have not even attempted to prove the existence of "ongoing conduct" through a string of annual measures'.²⁹⁷ China notes that during the Panel proceedings, the United States and Mexico argued that the 2009 and 2010 measures did not form a "continuum of 'ongoing conduct'" that serves to maintain the same export duties and quotas over time, arguing instead that the 2010 measures were "substantively different" and "were irrelevant to the legal question before the Panel".²⁹⁸ For these reasons, China asserts that the complainants "neither challenged nor proved the existence of a series of annual measures that 'serve to maintain the imposition of export duties and quotas over time'".²⁹⁹

165. China disagrees with the argument made by the United States and by Mexico that, if no recommendation were made regarding the replacement measures, there would be no resolution to the dispute, thereby creating a "loophole in the system".³⁰⁰ According to China, a Member's strategic choices about which acts and omissions it challenges do not create a "loophole"; instead, China highlights that the "responsibility" for a complainant's choices lies "squarely" with the complainant.³⁰¹ The "fundamental flaw" in the United States' and Mexico's arguments is that they seek a recommendation that "stretches" to include replacement measures that they themselves expressly

²⁹³ China's appellee's submission, para. 90. (original emphasis)

²⁹⁴ China's appellee's submission, paras. 91 and 92.

²⁹⁵ China's appellee's submission, para. 93.

²⁹⁶ China's appellee's submission, para. 94 (referring to Panel Report, *US – Orange Juice (Brazil)*, paras. 7.175 and 7.177, in turn referring to Appellate Body Report, *US – Continued Zeroing*, para. 191).

²⁹⁷ China's appellee's submission, para. 95.

²⁹⁸ China's appellee's submission, paras. 95-97 (referring to United States' second written submission to the Panel, para. 338; Mexico's second written submission to the Panel, para. 343; and the complainants' joint opening statement at the first Panel meeting, para. 52).

²⁹⁹ China's appellee's submission, paras. 97 and 98.

³⁰⁰ China's appellee's submission, paras. 99 and 100.

³⁰¹ China's appellee's submission, para. 101.

excluded from the dispute.³⁰² Finally, China "strongly objects" to the argument that, during the Panel proceedings, it "moved the target" in order to "evade 'responsibility'"³⁰³, rather, China recognized that the Panel had discretionary authority to make findings regarding the expired 2009 measures and to make findings and recommendations on the 2010 replacement measures.

2. Conditional Appeal of the European Union regarding the Panels' Recommendations

166. China agrees with the European Union that an objective assessment of the parties' arguments forms part of a panel's obligations under Article 11 of the DSU. However, China claims that the Panel did undertake an objective assessment of the European Union's arguments, and requests the Appellate Body to reject the European Union's claims of error. China argues that, even though the Panel did not refer to the complainants' joint opening statement at the first Panel meeting in finding that the European Union had joined the United States and Mexico in withdrawing its claims regarding the replacement measures, the objectivity of the Panel's assessment must be assessed in the light of this joint statement. In response to the European Union's argument that its statement of agreement with the United States' opening statement at the second Panel meeting was only a "simple statement of solidarity"³⁰⁴, China argues that, whatever the "subjective intentions" of the European Union, the Panel was required to judge the European Union's statement "'objectively' on the basis of the plain meaning of the words used".³⁰⁵ According to China, in assessing the European Union's remarks, the Panel took them at "face value" and did not commit any legal error.³⁰⁶

167. China also disagrees that the table of measures submitted by the European Union was only for the preparation of the descriptive part of the Panel Reports and that the Panel therefore erred in relying on it for determining its terms of reference. The European Union's responses were used for the purpose for which they were given, that is, "to clarify the rather uncertain scope of the matter before the Panel".³⁰⁷ China highlights that the European Union gave the same response regarding the 2010 replacement measures in two separate instances and, therefore, the European Union's response was not influenced by the Panel's stated purpose of seeking guidance in drafting the descriptive part of its Reports. China "sees no reason" why responses to questions posed by a panel cannot be used to

³⁰²China's appellee's submission, para. 102.

³⁰³China's appellee's submission, paras. 107 and 108 (referring to China's first written submission to the Panel, paras. 51 and 70).

³⁰⁴China's appellee's submission, para. 132 (quoting European Union's other appellant's submission, para. 23).

³⁰⁵China's appellee's submission, para. 133. (emphasis omitted)

³⁰⁶China's appellee's submission, paras. 131-134.

³⁰⁷China's appellee's submission, para. 123.

determine that a complainant has withdrawn its claims as, by definition, a complainant can only "impart" such information after the panel request has been filed.³⁰⁸ In the light of these arguments, China asserts that the Panel properly concluded from the European Union's submissions "as a whole" that the European Union had withdrawn its claims regarding the 2010 replacement measures.³⁰⁹

168. Regarding the European Union's request for the Appellate Body to complete the analysis with respect to Article XI of the GATT 1994, China notes that the Appellate Body has used its authority to complete the analysis "sparingly", "taking care" to ensure that it respects the "institutional limits" placed on its authority.³¹⁰ In China's view, the panel is the "trier of facts" and the Appellate Body cannot "seek facts" or make "factual findings".³¹¹ China contends that the European Union has not set out an adequate basis for the Appellate Body to complete the analysis. First, the European Union has not stated which replacement measures it now wishes to be the subject of findings and recommendations. Second, although the European Union requests the Appellate Body to find that certain export duties violate Article XI of the GATT 1994, neither the European Union's panel request, nor the tables submitted by it, include a claim that China's export duties are inconsistent with Article XI. Third, China highlights that the European Union has not advanced any legal argument in support of its request to the Appellate Body to complete the analysis. Moreover, China notes that the European Union has not identified any facts that would be relevant to the Appellate Body's completion of the analysis.

3. Involvement of the CCCMC in the Allocation of Export Quotas and Article X:3(a) of the GATT 1994

169. China requests the Appellate Body to deny Mexico's appeal and uphold the Panel's finding that the involvement of the CCCMC in the administration of China's export quota regime is consistent with Article X:3(a) of the GATT 1994.³¹² China contends that Mexico's interpretation of Article X:3(a) is flawed, specifically with respect to the legal standard and the evidence required to meet that standard in the context of "as such" claims. China also contests Mexico's submission that the Panel failed to make an objective assessment of the matter as required by Article 11 of the DSU.

³⁰⁸China's appellee's submission, paras. 128 and 129.

³⁰⁹China's appellee's submission, para. 135.

³¹⁰China's appellee's submission, para. 137 (referring to Appellate Body Report, *Australia – Apples*, para. 368; Appellate Body Report, *Australia – Salmon*, paras. 209, 212, 241, and 255; Appellate Body Report, *Canada – Autos*, paras. 133 and 144; Appellate Body Report, *Korea – Dairy*, para. 102; Appellate Body Report, *Korea – Various Measures on Beef*, para. 128; Appellate Body Report, *US – Continued Zeroing*, para. 189; and Appellate Body Report, *US – Zeroing (EC) (Article 21.5 – EC)*, para. 438).

³¹¹China's appellee's submission, para. 137.

³¹²China's appellee's submission, paras. 13 and 263.

170. China submits that Mexico's proffered legal standard for "as such" claims is erroneous and contrary to the Appellate Body's approach, and should therefore be rejected. Based on an interpretation of the term "administer", and consistent with the requirement that a Member provide "solid evidence"³¹³ in support of such a claim, the Appellate Body has found that a complainant challenging a measure "as such" under Article X:3(a) must demonstrate that action foreseen or anticipated pursuant to the measure will, at least in defined circumstances, "necessarily lead to" WTO-inconsistent administration.³¹⁴ China disagrees with Mexico's assertion that the Panel interpreted Article X:3(a) in the context of its "as such" challenge so as to require a demonstration of specific instances of actual unreasonable or partial administration. Rather, the Panel found that Mexico had failed to show that the CCCMC "*ex*ercise any discretion" in such a way as to constitute WTO-inconsistent administration, much less that the challenged measure would necessarily lead to WTO-inconsistent administration.³¹⁵ China also rejects Mexico's suggestion that requiring evidence of partiality or unreasonableness "ignores" certain realities.³¹⁶ This is not a reason to abandon the interpretation stated by the Appellate Body, namely, that a complainant must provide "solid evidence"³¹⁷ showing how and why the features of the measure and the administrative processes challenged "as such" "necessarily lead to" WTO-inconsistent administration.³¹⁸

171. Contrary to Mexico's assertion, the Appellate Body report in *EC – Selected Customs Matters* does not provide any support for Mexico's suggestion that the term "uniform" should be interpreted to require demonstration that a measure challenged "as such" "necessarily leads to" non-uniform administration, while the terms "impartial" and "reasonable" enable a complainant to benefit from an "*assumption* [that a significant possibility [of partial and unreasonable administration] exists".³¹⁹ Indeed, the Appellate Body stated that the "necessarily leads to" standard arises from an interpretation of the term "administer", and applies whether non-uniform, partial, or unreasonable administration is

³¹³China's appellee's submission, para. 190 (referring to Appellate Body Report, *US – Oil Country Tubular Goods Sunset Reviews*, para. 217).

³¹⁴China's appellee's submission, para. 190 (referring to Appellate Body Report, *EC – Selected Customs Matters*, paras. 201 and 226).

³¹⁵China's appellee's submission, para. 203 (quoting Panel Reports, para. 7.783). (emphasis added by China)

³¹⁶China's appellee's submission, para. 198 (referring to Mexico's other appellant's submission, para. 31).

³¹⁷China's appellee's submission, para. 199 (referring to Appellate Body Report, *US – Oil Country Tubular Goods Sunset Reviews*, para. 217).

³¹⁸China's appellee's submission, para. 199 (referring to Appellate Body Report, *EC – Selected Customs Matters*, para. 226).

³¹⁹China's appellee's submission, para. 196 (referring to Mexico's other appellant's submission, para. 58). (emphasis added by China)

alleged.³²⁰ China also points out that the "erroneous presumption of WTO-inconsistency" implicated by Mexico's proffered standard would be at odds with the requirement that complainants bear the burden of establishing that the administration of a measure is inconsistent with Article X:3(a).³²¹

172. China contests Mexico's suggestion that the Panel disregarded the proper interpretation of Article X:3(a) when it found that the involvement of the CCCMC in the quota administration regime was not WTO-inconsistent. Rather, the Panel found that "Mexico had *failed to demonstrate that the defined circumstances it identifies arise in the present case*."³²² Specifically, the Panel distinguished the CCCMC members from the CCCMC Secretariat, and found that the CCCMC Secretariat does not have commercial interests adverse to those of the quota applicants.³²³ In addition, Mexico did not establish that the tasks delegated to the CCCMC were more than clerical or administrative, and the Panel correctly found that the CCCMC Secretariat may not exercise significant discretion or judgement in evaluating whether applicants meet the eligibility criteria that are "objectively specified in Chinese law".³²⁴ Moreover, the Panel did not find that the provision of information to the CCCMC Secretariat amounted to providing information to quota applicants' competitors, because the Panel had found that "[a]pplicants for export quotas are provided solely to CCCMC's Minerals & Metals Department and not to the membership of the CCCMC itself".³²⁵

173. China emphasizes that, contrary to Mexico's argument, there is no basis on which the Appellate Body can assume that confidential business information submitted by quota applicants to the CCCMC Secretariat will be disclosed to their competitors. In the light of the presumption that China will abide by its WTO obligations, the "possibility" that such confidential information "may be leaked" cannot be assumed.³²⁶ While this presumption can be rebutted, Mexico "failed to provide any such evidence".³²⁷ In fact, rather than providing solid evidence demonstrating that a measure challenged "as such" will "necessarily lead to" WTO-inconsistent administration, Mexico conceded that the CCCMC Secretariat's involvement in certain elements of quota administration can be and has

³²⁰China's appellee's submission, para. 197 (referring to Appellate Body Report, *EC – Selected Customs Matters*, para. 226).

³²¹China's appellee's submission, para. 193.

³²²China's appellee's submission, para. 211. (original emphasis)

³²³China's appellee's submission, para. 212 (referring to Panel Reports, para. 7.774). China highlights the fact that Mexico did not contest this fact during the Panel proceedings (*ibid.*, para. 212) and that Mexico's assertion on appeal that the CCCMC Secretariat has commercial interests adverse to applicants is not supported by a Panel finding (*ibid.*, para. 213).

³²⁴China's appellee's submission, para. 236.

³²⁵China's appellee's submission, para. 222 (quoting Panel Reports, para. 7.778). (emphasis added by China)

³²⁶China's appellee's submission, para. 230.

³²⁷China's appellee's submission, para. 230. (original emphasis)

the CCCMC departments in quota administration, the Panel concluded that Mexico had failed to establish "even the 'risk' of WTO-inconsistent administration."³³⁷

4. Article VIII:1(a) of the GATT 1994 and Paragraph 11.3 of China's Accession Protocol

176. China requests the Appellate Body to uphold the Panel's finding that the bid-winning price imposed by China does not constitute a fee or charge of whatever character imposed in connection with exportation within the meaning of Article VIII:1(a) of the GATT 1994, and that the bid-winning price is not a charge applied to exports falling within the scope of Paragraph 11.3 of China's Accession Protocol.

177. China maintains that the Panel was correct to conclude, based on the substantive nature of China's bidding procedure, that the bid-winning price does not constitute a fee or charge imposed "on or in connection with ... exportation". In addition, the Panel correctly found that the bid-winning price is not a fee or charge in the sense of Article VIII:1(a), because it is not collected in exchange for a "service rendered". China disagrees with the United States' contention that, if no service is rendered, a fee or charge will be inconsistent with Article VIII:1(a), rather than fall outside the scope of the provision. Instead, Article VIII:1(a) is meant to ensure that, when services are rendered, the amount charged for those services is proportionate to their cost. Where there is no service, however, a fee or charge is not related to any "service rendered", and, therefore, the "mischief" addressed by the clause", namely charging an excessive amount for "services rendered", is not present.³³⁸

178. China also claims that, in order to establish that a fee or charge is inconsistent with Article VIII:1(a), a complainant must demonstrate that the fee or charge is inconsistent with every condition set out in Article VIII:1(a). In China's view, the GATT panel report in *US – Customs User Fee* stands for that proposition.³³⁹ Furthermore, Article VIII:1(a) would have been drafted differently had the drafters intended the provision to constitute a residual prohibition in the sense advanced by the United States. For instance, the provision could have been drafted to say "no fees or charges (other than duties or internal taxes) shall be instituted or maintained on in connection with importation or exportation, unless limited in amount to the approximate cost of a service rendered".³⁴⁰ China further contends that, even if the bid-winning price were to fall within the scope of Article VIII:1(a),

³³⁷China's appellee's submission, para. 260 (quoting Panel Reports, para. 7.783).

³³⁸China's appellee's submission, para. 302.

³³⁹China's appellee's submission, para. 307 (referring to GATT Panel Report, *US – Customs User Fee*, para. 69).

³⁴⁰China's appellee's submission, para. 303.

been implemented in a WTO-consistent manner, thus confirming that the measures do not "necessarily lead to" unreasonable and partial conduct.

174. With regard to the Panel's assessment of the matter under Article 11 of the DSU, China contends that Mexico has merely demonstrated that the Panel, as the trier of facts, concluded that Mexico failed to establish that the "CCCMC Secretariat *can* exercise any discretion, partiality or bias in the administration' of export quotas".³³⁸ Recalling the relevant standard under Article 11 of the DSU, China agrees with Mexico's statement that the Panel was obliged "to consider evidence before it in its totality"³²⁹, but adds that the Appellate Body has also underscored a panel's discretion to give "certain elements of evidence more weight than other elements".³³⁰ Furthermore, to support a claim of violation under Article 11, "a participant must explain why evidence [not explicitly referred to by the panel] is so material to its case that the panel's failure explicitly to address and rely upon the evidence has a bearing on the objectivity of the panel's factual assessment."³³¹ Mexico failed to identify any evidence demonstrating that the CCCMC Secretariat undertakes its delegated quota administration tasks with "no real oversight"³³², or that it has significant discretion to affect the award of quotas.

175. China maintains that the Panel found the CCCMC Secretariat's role to be "circumscribed" by Chinese law³³³, and that Mexico had not demonstrated that the CCCMC Secretariat can exercise any discretion. In the context of quotas allocated directly, the Panel found the CCCMC Secretariat's role to be "limited to assisting MOFCOM"³³⁴ in verifying the compliance of applicants with the qualifying criteria "*objectively specified under Chinese law*".³³⁵ It was also on the basis of the same evidence described by Mexico that the Panel found, with respect to quotas allocated through bidding, that the CCCMC Secretariat assists MOFCOM's Bidding Committee, which is the "main authority responsible for organizing the bidding process".³³⁶ Having reflected on all of the evidence concerning the roles of

³³⁸China's appellee's submission, paras. 22 and 261 (quoting Panel Reports, para. 7.783). (emphasis added by China)

³³⁹China's appellee's submission, para. 243 (quoting Appellate Body Report, *EC – Fasteners (China)*, para. 441).

³⁴⁰China's appellee's submission, para. 244 (quoting Appellate Body Report, *EC – Asbestos*, para. 161).

³³¹China's appellee's submission, para. 244 (quoting Appellate Body Report, *EC – Fasteners (China)*, para. 442).

³³²China's appellee's submission, para. 246 (quoting Mexico's other appellant's submission, para. 56).

³³³China's appellee's submission, paras. 21 and 251 (referring to Panel Reports, paras. 7.780 and 7.781).

³³⁴China's appellee's submission, para. 255 (quoting Panel Reports, para. 7.780).

³³⁵China's appellee's submission, para. 255. (original emphasis)

³³⁶China's appellee's submission, paras. 251 and 258 (quoting Panel Reports, para. 7.766).

the United States did not demonstrate that the bid-winning price "represents an indirect protection or a taxation of exports for fiscal purposes".³⁴¹

179. China notes that quota allocation through auctioning ensures that the most efficient producers are granted the right to export and that this ensures allocation of quotas in the least trade-distorting manner. Finding China's bid-winning price to be inconsistent with Article VIII:1(a) would mean that all quota allocation accomplished through bidding or auctioning by WTO Members would be prohibited.

180. Finally, China submits that the United States did not establish that the bid-winning price is inconsistent with Paragraph 11.3 of China's Accession Protocol. The United States' argument is based solely on the allegation that the Panel's analysis with respect to Paragraph 11.3 flowed from its erroneous analysis of Article VIII:1(a). China maintains that the Panel's finding under Article VIII:1(a) was correct, and that, therefore, the Panel was also correct in finding that the bid-winning price is not inconsistent with Paragraph 11.3 of China's Accession Protocol.

H. *Arguments of the Third Participants*

1. Brazil

181. With respect to China's claim that the Panel erred in finding that Section III of the complainants' panel requests complied with Article 6.2 of the DSU, Brazil cautions that an excessively formalistic approach to the interpretation of Article 6.2 could unjustifiably increase the procedural burden on the parties. Brazil submits that the Appellate Body has identified two major objectives of a panel request: a jurisdictional function and a due process function. In situations affecting the proper delimitation of a panel's jurisdiction, corrections or clarifications of an alleged error or imprecision cannot modify the scope of the dispute as expressed in the panel request. Conversely, where defects in the panel request allegedly affect the due process function of the request, subsequent submissions may be taken into consideration by panels and the Appellate Body in the analysis of whether the due process rights of a party have been prejudiced. Therefore, subsequent submissions should not, in Brazil's view, be *a priori* excluded from serving as evidence relevant to that legal determination.

182. Brazil maintains that the Panel correctly interpreted the words "temporarily applied" in Article XI:2(a) of the GATT 1994. A "temporary" measure must either have a time-limit for its

³⁴¹China's appellee's submission, para. 313.

application, or must address a passing need, the termination of which is foreseeable at some point in the near future. If a measure is applied to address a permanent need, its design and structure would indicate that it is not "temporarily" applied. As such, Brazil notes that a shortage of exhaustible natural resources caused by declining reserves cannot be addressed by measures "temporarily applied". Brazil also highlights that Articles XI:2(a) and XX(g) of the GATT 1994 serve different purposes by means of different requirements. While Article XX(g) disciplines long-term conservation policies, Article XI:2(a) relates to temporary supply crises. Therefore, Brazil contends that measures adopted pursuant to Article XI:2(a) are not intended to deal with permanent needs, because such needs, in any event, could not be addressed by temporary measures.

183. Brazil argues that the Panel read into the phrase "made effective in conjunction with" in Article XX(g) of the GATT 1994 two cumulative requirements, namely, one relating to the joint application of domestic and international restrictions, and the other relating to the effectiveness of domestic restrictions. Brazil quotes from the Appellate Body reports in *US – Gasoline* and *US – Shrimp* in support of the proposition that, in previous disputes, the expression "made effective in conjunction with" has been found to relate only to the joint application of domestic restrictions with measures relating to the conservation of exhaustible natural resources.³⁴² Brazil contends that, while the GATT panel in *Canada – Herring and Salmon* may have interpreted differently the phrase "made effective in conjunction with", the Spanish and French versions of Article XX(g) confirm that the Appellate Body's interpretation in *US – Gasoline* and *US – Shrimp* was correct. Article XX(g) aims simply at ensuring even-handedness in the application of measures relating to the conservation of exhaustible natural resources.

2. Canada

184. Canada submits that the Appellate Body should uphold the Panel's finding that Article XX of the GATT 1994 is not available as a defence for inconsistencies with Paragraph 11.3 of China's Accession Protocol. First, the ordinary meaning of the Note to Annex 6 of China's Accession Protocol "does not support the argument that China may impose export duties on any products at any rate in 'exceptional circumstances'", because the phrase "exceptional circumstances" is used only with respect to increasing the rates applied at the time of China's accession to the maximum levels set out

³⁴²Brazil's third participant's submission, para. 26 (quoting Appellate Body Report, *US – Gasoline*, pp. 20-21, DSR 1996:1, 3, at 19-20) and para. 27 (quoting Appellate Body Report, *US – Shrimp*, paras. 143 and 144).

in Annex 6.³⁴³ The Panel, therefore, erred in "acquiescing"³⁴⁴ to the European Union's argument that China acted inconsistently with Paragraph 11.3 by not consulting with affected Members before imposing export duties on raw materials that are not listed in Annex 6, as there is no right to impose export duties on those products in the first place. Canada argues that the legal effect of the reference in Paragraph 11.3 to Article VIII of the GATT 1994 is to "circumscribe" the application of export charges by China in accordance with Article VIII, and Article XX is not a "necessary extension" of Article VIII such that it may be assumed to be incorporated by reference to Article VIII.³⁴⁵ Canada also asserts that the Panel was correct in finding that Paragraph 170 of China's Accession Working Party Report repeats China's commitments under GATT rules, and is not related to export duties prohibited under Paragraph 11.3. Relying on the ordinary meaning and context of China's Accession Protocol, Canada does not dispute that Article XX is available to justify inconsistencies with the GATT 1994 obligations set out in Paragraph 170, but contends that there is no suggestion that obligations going beyond the requirements of the GATT 1994, which China undertook pursuant to Paragraph 11.3, are subject to the Article XX exceptions. If the negotiators had intended to incorporate Article XX justifications into Paragraph 11.3, they could have incorporated language similar to that contained in Paragraph 5.1 of China's Accession Protocol.

185. With respect to the words "temporarily applied", Canada disagrees with China's contention that the Panel found that Article XI:2(a) imposes an "absolute limit" on the time period for which export restrictions may be imposed.³⁴⁶ Rather, the Panel found that the duration of an export restriction must match the time it takes to prevent or relieve a critical shortage, a finding with which Canada agrees. Measures that are reviewed regularly, but imposed indefinitely, as the Panel found China's measures to be, are not applied for a fixed time, and hence fall outside the scope of Article XI:2(a). Canada also disagrees with China's contention that the Panel's interpretation of the phrase "critical shortages" excludes from the scope of Article XI:2(a) export restrictions on non-renewable, exhaustible natural resources. Rather, the Panel's interpretation permits a WTO Member to relieve a critical shortage of an exhaustible natural resource through the temporary application of an export restriction as long as the shortage is caused by a factor other than the resource's inherent exhaustibility. With respect to the relationship between Article XI:2(a) and Article XX(g) of the GATT 1994, Canada argues that the Panel did not find that the two provisions are mutually exclusive,

³⁴³Canada's third participant's submission, para. 14.

³⁴⁴Canada's third participant's submission, para. 16.

³⁴⁵Canada's third participant's submission, para. 18.

³⁴⁶Canada's third participant's submission, para. 36 (referring to China's appellants' submission, paras. 337-341).

but rather that the absence in Article XI:2(a) of the safeguards found in the chapeau of Article XX supports the conclusion that restrictions under Article XI:2(a) must be of a limited duration.

186. Canada agrees with the United States that the Panel erred in finding that the bid-winning fee is consistent with Article VIII:1(a) of the GATT 1994 and with Paragraph 11.3 of China's Accession Protocol. For Canada, the Panel rightly found that the bid-winning fee is a "fee" or "charge" within the meaning of Article VIII:1(a). The Panel erred, however, in interpreting the phrase "in connection with" exportation to cover only charges connected with "customs-related activities" and in finding that only charges collected in exchange for a "service rendered" fall within the scope of Article VIII.³⁴⁷ Instead, the Panel should have adopted the same broad interpretation as the panel in *China – Auto Parts*.³⁴⁸ Even if the bid-winning fee is not covered by Article VIII:1(a) of the GATT 1994, the charge constitutes an "export duty" prohibited under Paragraph 11.3 of China's Accession Protocol. Paragraph 11.3 specifically addresses what Article VIII:1 does not, namely, export duties, and as such these two provisions "create a tightly woven mesh that catches all charges imposed by the Chinese government in connection with exportation".³⁴⁹

3. Colombia

187. Colombia submits that the Panel erred by finding that Section III of the complainants' panel requests "present[ed] the problem clearly" in the sense of Article 6.2 of the DSU because the complainants failed to provide sufficient connections between the 37 listed measures and the 13 listed treaty provisions.³⁵⁰ The Appellate Body has found that a complainant must provide a brief summary of the case, explaining succinctly how or why the measure at issue is inconsistent with a specific WTO obligation. In failing to do so, the complainant renders the due process objective of Article 6.2 ineffective, because neither the responding party nor the third parties would be able to identify with sufficient clarity the claims or problem at issue.

188. Colombia submits that the Appellate Body should confirm the Panel's finding that Article XX of the GATT 1994 may not be invoked as a justification for inconsistencies with Paragraph 11.3 of China's Accession Protocol. Colombia submits that the Panel erred in finding that China has acted inconsistently with Paragraph 11.3 by not consulting with Members before imposing export duties on

³⁴⁷Canada's third participant's submission, para. 57 (quoting Panel Reports, para. 7.838) and para. 58 (quoting Panel Reports, para. 7.844).

³⁴⁸See Canada's third participant's submission, para. 57 (referring to Panel Reports, *China – Auto Parts*, paras. 7.177, 7.190, and 7.191).

³⁴⁹Canada's third participant's submission, para. 67.

³⁵⁰Colombia's third participant's submission, para. 2 and heading I.A.1.

raw materials not listed in Annex 6 to the Protocol, because the obligation to consult relates only to the products listed in Annex 6, none of which were at issue here. With respect to the reference to Article VIII in Paragraph 11.3, Colombia asserts that the "rule-exception relationship" between Article VIII and Article XX of the GATT 1994 shows that the reference to Article VIII incorporates only that provision's conditions and not the availability of the general exceptions to Article XX.³⁵¹

189. Colombia also suggests that irrespective of the applicability of Paragraph 170 of China's Accession Working Party Report to export duties, the requirement that such duties be "in full conformity with [China's] WTO obligations" cannot be understood as allowing recourse to Article XX. In accordance with effective treaty interpretation, the use of the phrase "WTO obligations" in Paragraph 170, as compared to "the WTO Agreement" in Paragraph 5.1 of China's Accession Protocol, indicates that the former excludes exceptions, whereas the latter covers both obligations and exceptions.³⁵²

190. Colombia contends that the Panel erred in finding that measures relating to exhaustible natural resources fall exclusively within the scope of Article XX(g) and not within Article XI:2(a) of the GATT 1994. The ordinary meaning of the terms of Article XI:2(a), in their context, suggest that the scope of application of the provision is not contingent on whether the product is an exhaustible natural resource or not, as any product is potentially covered by Article XI:2(a). The "ultimate test" is whether the product is essential to the exporting Member or is a "foodstuff" as that term is used in Article XI:2(a).³⁵³ In Colombia's view, a single measure could be justified under several exceptions contained in the GATT 1994, such as Article XI:2(a) and Article XX, so long as they fulfil the particular requirements established in each provision.

191. Colombia submits that the Panel erred in interpreting the phrase "made effective in conjunction with" in Article XX(g) of the GATT 1994 to require that a measure not only be related to the conservation of natural resources, but also ensure the effectiveness of domestic restrictions on that resource. In Colombia's view, the Panel's interpretation is at odds with the interpretation provided by the Appellate Body in *US – Gasoline* and in *US – Shrimp*, which did not require such a "dual purpose".³⁵⁴

³⁵¹Colombia's third participant's submission, para. 22.

³⁵²Colombia's third participant's submission, paras. 30-35 (referring to Appellate Body Report, *US – Wool Shirts and Blouses*, para. 46, and Appellate Body Report, *China – Publications and Audiovisual Products*, para. 223).

³⁵³Colombia's third participant's submission, para. 49.

³⁵⁴Colombia's third participant's submission, paras. 59 and 60.

192. Regarding China's export licensing system, Colombia disputes China's contention that the "open-ended" discretion" accorded to Chinese licensing authorities is not sufficient to conclude that its export licensing system constitute a "restriction" under Article XI:1 of the GATT 1994.³⁵⁵ In Colombia's opinion, it is not the open-ended nature (that is, the discretion to choose between a WTO-consistent and a WTO-inconsistent application of the measure) that is at issue. Rather, the Appellate Body should "focus on the economic consequences in a given marketplace so as to evaluate whether economic operators will interpret the discretion as [a] restriction".³⁵⁶ Although not "*a priori* a 'restriction'"³⁵⁷, if such discretion causes "a *reasonable uncertainty* that will discourage exports", then it constitutes a "restriction" on exports under Article XI:1.³⁵⁸ This interpretation would be in keeping with the purpose of Article XI, which, as China acknowledges, is "to protect the competitive opportunities for exports".³⁵⁹

193. Colombia agrees with China that the Panel erred in interpreting and applying Article X:3(a) of the GATT 1994 with regard to the "operation capacity" requirement for export quota administration. Specifically, in Colombia's view, the Panel erred in interpreting the meaning of "administer" to encompass the complainants' claim and in finding that the complainants challenged "the features of an administrative process".³⁶⁰

4. Japan

194. Japan notes that the "security and predictability" of the multilateral trading system, as well as the "prompt settlement" of disputes, will be "endangered" if panels can make recommendations only for measures that have "not cease[d] to exist during panel proceedings", and if the dispute settlement process can be "circumvented" through "rapid-fire substitution" or annual revision of WTO-inconsistent measures.³⁶¹ Japan sees the Panel's recommendations on the "series of measures" as aimed at plugging this "loophole".³⁶² Japan supports the conditional appeals of the United States and Mexico because, in its view, where a challenged measure is removed before the issuance of a

³⁵⁵Colombia's third participant's submission, para. 65.

³⁵⁶Colombia's third participant's submission, para. 66.

³⁵⁷Colombia's third participant's submission, para. 71.

³⁵⁸Colombia's third participant's submission, para. 66. (original emphasis) Colombia substantiates its argument on this point by referring to the interpretation of the term "restrictions" provided in Panel Report, *Brazil – Retreaded Tyres*, para. 7.370, and Panel Report, *Colombia – Ports of Entry*, para. 7.240. (*Ibid.*, para. 68).

³⁵⁹Colombia's third participant's submission, para. 68 (referring to China's appellant's submission, para. 548).

³⁶⁰Colombia's third participant's submission, para. 77 (quoting Panel Reports, para. 7.709).

³⁶¹Japan's third participant's submission, para. 12.

³⁶²Japan's third participant's submission, paras. 12 and 13.

panel report and where "factual and/or legal circumstances" suggest that the measure is likely to be renewed, a finding without a recommendation cannot lead to a conclusive settlement of the dispute.³⁶³

195. Japan submits that the Appellate Body should confirm the Panel's finding that Article XX of the GATT 1994 may not be invoked as a justification for inconsistencies with Paragraph 11.3 of China's Accession Protocol. Japan doubts that the reference to "exceptional circumstances" in the Note to Annex 6 to China's Accession Protocol establishes the applicability of Article XX to Paragraph 11.3, and, even if it did, the possibility for China to impose higher rates in "exceptional circumstances" is meant to apply only with respect to the products listed in Annex 6, which are not at issue in this dispute. Moreover, the reference to Article VIII of the GATT 1994 does not confirm the availability of Article XX. China did not invoke Article VIII for any of the export duties at issue and "there seems to be little question" that the duties in the present dispute are outside the scope of Article VIII.³⁶⁴ In fact, export duties do not fall within the substantive scope of any provision of the GATT 1994 and, therefore, cannot be inconsistent with the GATT 1994. On this basis, Japan argues that Paragraph 170 of China's Accession Working Party Report cannot be interpreted as permitting recourse to Article XX in cases of inconsistency with Paragraph 11.3 of China's Accession Protocol.

196. Japan also supports the Panel's interpretation of the phrase "made effective in conjunction with" in Article XX(g). Japan contends that the Panel's analysis and interpretation of Article XX(g) is supported by the text and context of the provision, as well as the object and purpose and the structure of the GATT 1994. In particular, Japan asserts that the Panel's reference to the purpose of an export restriction being to render effective domestic restrictions on production or consumption that serve a conservation goal is consistent with the approach that has been taken by the Appellate Body as well as that of the GATT panel in *Canada – Herring and Salmon*. Japan further alleges that China's argument appears to imply that the objective or effect of a trade-restrictive measure should not be relevant to an Article XX(g) analysis, and that this would reverse a consistent line of GATT and WTO case law requiring a substantial relationship between the trade measure and a genuine conservationist goal.

197. Japan further submits that China "effectively glosses over" the difference between limited availability and a "critical shortage" of a resource within the meaning of Article XI:2(a).³⁶⁵ The Panel correctly established that there is no possibility of an existing shortage of an exhaustible natural

³⁶³Japan's third participant's submission, para. 14.

³⁶⁴Japan's third participant's submission, para. 30.

³⁶⁵Japan's third participant's submission, para. 92 (referring to joint appellees' submission of the United States and Mexico, para. 153).

resource ever to cease to exist, meaning that it will not be possible to "relieve or prevent" it through export restrictions applied on a temporary basis.³⁶⁶ Furthermore, the phrase "temporarily applied" must be read in the context of "critical shortages". A shortage of an exhaustible natural resource, by its very nature, cannot be restored in the future, and any restrictions imposed to relieve or prevent such shortage can therefore not be of a "temporal" nature.³⁶⁷ Japan also supports the European Union's argument that the fact that Article XX(g) allows for derogations from GATT obligations under stricter conditions than Article XI:2(a) suggests that the requirements of the latter provision must be given a narrow interpretation in order not to render redundant the provision of the former.³⁶⁸

198. Japan contends that the Panel effectively addressed China's argument regarding interpreting Paragraphs 83 and 84 of China's Accession Working Party Report "harmoniously" with Paragraph 5.1 of China's Accession Protocol.³⁶⁹ That is, the Panel appropriately read Paragraph 5.1 of the Accession Protocol to incorporate, as part of the *WTO Agreement*, the specific commitments China made in Paragraphs 83 and 84 of its Accession Working Party Report.³⁷⁰ Japan expresses "serious doubts" about China's apparent rationale for applying an export performance condition as a basis for quota allocation³⁷¹, and notes the "significant trade-restrictive effects" of China's export performance requirement, which make it "effectively impossible" for new entrants to obtain quota share.³⁷² Finally, Japan insists that China cannot have recourse to the quota eligibility or allocation criteria that it expressly committed to eliminate as part of its WTO accession process, and which are significantly more trade-restrictive than necessary.

5. Korea

199. Korea observes that the complainants "effectively withdrew" their request to review the 2010 Chinese measures and requested the Panel to confine its review to the 2009 measures.³⁷³ Korea notes the "apparent discrepancy" between the Panel's statement that it would look at the 2009 measures only, and its subsequent references to the review of the "series of measures" acting in concert.³⁷⁴

³⁶⁶Japan's third participant's submission, para. 92.

³⁶⁷Japan's third participant's submission, para. 94.

³⁶⁸See Japan's third participant's submission, para. 98 (referring to European Union's statement, second written submission to the Panel, para. 206, referenced in Panel Reports, para. 7.293).

³⁶⁹Japan's third participant's submission, paras. 84 and 85 (referring to Panel Reports, para. 7.665).

³⁷⁰Japan's third participant's submission, para. 85 (referring to Panel Reports, para. 7.665).

³⁷¹Japan's third participant's submission, para. 86.

³⁷²Japan's third participant's submission, para. 87.

³⁷³Korea's third participant's submission, para. 10.

³⁷⁴Korea's third participant's submission, para. 11.

According to Korea, it is not clear whether the "inherent discretion" accorded to a panel permits such a discrepancy.³⁷⁵ In Korea's view, Article 19 of the DSU requires that only a measure found to be inconsistent with a covered agreement can be the subject of a panel's recommendations; that is, a recommendation should be "in parallel" with the challenged measure, and a panel only has the "discretion" to "suggest" ways of implementing the recommendation.³⁷⁶ Since the complainants deliberately chose to forego the "nexus-based" claims, Korea suggests that the Panel may not have been "free to insert" the claim in the subsequent remedy phase of its analysis.³⁷⁷

200. Regarding the applicability of Article XX to inconsistencies with Paragraph 11.3 of China's Accession Protocol, Korea agrees with the Panel that, if two legal provisions contain different wording in the same article or treaty, they must be interpreted to have different meanings. However, the "gravity" and importance of an "Article XX defense" suggests that "[m]ore explicit wording" should have been used in this dispute to express the "relinquishment of such an important right".³⁷⁸ Given the implications for other protocols of accession, China's appeal warrants "careful scrutiny".³⁷⁹ Nonetheless, in Korea's view, the "difference in tone and nuance" between Paragraph 11.3 and Paragraphs 11.1 and 11.2 of China's Accession Protocol, as well as the context of the other provisions of Paragraph 11, supports the Panel's ultimate conclusion in the present dispute, and should be upheld by the Appellate Body.³⁸⁰

201. Korea suggests that the Panel's finding under Articles X:3(a) and XI:1 of the GATT 1994, that "vagueness" in the terms of a law or regulation can result in "as such" inconsistencies, requires careful scrutiny.³⁸¹ With regard to the "operation capacity" requirement under Article 19 of the *Export Quota Administration Measures*, for example, the complainants claimed that the vagueness of this term equates to "unlimited discretion in contravention of the GATT 1994".³⁸² In *EC – Selected Customs Matters*, however, the Appellate Body found that the mere showing of the existence of non-uniform features, for example, is not sufficient to prove an inconsistency with Article X:3(a) of the GATT 1994. Rather, the complainant must show that these features necessarily lead to non-uniform, partial or unreasonable administration. Furthermore, "it seems undeniable" that China's export

³⁷⁵Korea's third participant's submission, para. 11.

³⁷⁶Korea's third participant's submission, para. 27.

³⁷⁷Korea's third participant's submission, para. 28.

³⁷⁸Korea's third participant's submission, para. 32.

³⁷⁹Korea's third participant's submission, para. 32.

³⁸⁰Korea's third participant's submission, para. 33.

³⁸¹Korea's third participant's submission, p. 13, heading III.C.

³⁸²Korea's third participant's submission, para. 36 (referring to European Union's first written submission to the Panel, paras. 165, 239-241, 320, and 348; and United States' first written submission to the Panel, paras. 196 and 340).

licensing system includes "vague provisions" and thus accords licence-issuing agencies "a significant degree of discretion", which could result in export restrictions inconsistent with Article XI:1 of the GATT 1994.³⁸³ However, when examining "legislative documents of a Member that contain 'discretionary' language" in the framework of an "as such" complaint, a panel should adopt a "cautious approach" guided by the presumption, identified by the Appellate Body in *US – Oil Country Tubular Goods Sunset Reviews*, "that WTO Members act in good faith in the implementation of their WTO commitments".³⁸⁴ In the present dispute, Korea argues that "it does not seem to be entirely clear" whether the complainants presented sufficient evidence to overcome that "good faith" presumption.³⁸⁵

6. Saudi Arabia

202. Saudi Arabia contends that Article XX(g) of the GATT 1994 requires that the challenged measure be applied jointly with domestic restrictions on the production or consumption of an exhaustible natural resource. The Panel, however, erred in finding that, in addition, the "purpose" of the challenged measure must be to ensure the effectiveness of a domestic restriction on production or consumption. Nothing in the text of Article XX(g) suggests such a finding. The Panel appears to have been guided by the GATT panel report in *Canada – Herring and Salmon*, and Saudi Arabia suggests that the Panel did so in error. The Appellate Body report in *US – Gasoline* did not endorse the approach of the GATT panel in *Canada – Herring and Salmon*, and instead found that Article XX(g) imposed only a requirement of "even-handedness".³⁸⁶ Saudi Arabia points out that, in *US – Gasoline*, Venezuela and Brazil referred the Appellate Body to the relevant part of the GATT panel report in *Canada – Herring and Salmon*, but that, nonetheless, the Appellate Body did not adopt that panel's interpretation. In Saudi Arabia's view, the object and purpose of Article XX(g) will be fulfilled if the restrictions imposed on foreign and domestically produced goods are applied jointly.

203. While taking no position on whether China's export licensing system is inconsistent with Article XI of the GATT 1994, Saudi Arabia welcomes the Panel's finding that "non-automatic" export

³⁸³Korea's third participant's submission, para. 39.

³⁸⁴Korea's third participant's submission, para. 40 (quoting Appellate Body Report, *US – Oil Country Tubular Goods Sunset Reviews*, para. 173).

³⁸⁵Korea's third participant's submission, para. 41. Enlarging the scope of its analysis beyond the framework of Article XI:1, Korea also refers to the Appellate Body's statement in *EC – Selected Customs Matters* that: "[i]n order to find that an administrative process has led to non-uniform administration of a measure under Article X:3(a), a panel cannot merely rely on identifying the features of an administrative process that it may view as non-uniform; a panel must go further and undertake an analysis to determine whether those features of the administrative process necessarily lead to non-uniform administration of a legal instrument of the kind described in Article X:1." (*Ibid.*, para. 42 (quoting Appellate Body Report, *EC – Selected Customs Matters*, para. 239 (original emphasis)))

³⁸⁶Saudi Arabia's third participant's submission, para. 22.

licensing systems are not inconsistent with this provision unless they create "a restriction or limiting effect on ... exportation".³⁸⁷ In particular, Saudi Arabia agrees with the Panel's ultimate conclusions that two types of export licensing systems are consistent with Article XI:1: "(i) those in which licences are granted upon application in all cases; and (ii) those which require the applicant to meet a certain objective prerequisite" before being granted a licence.³⁸⁸ However, the Panel's assertion that, in addition to "quantitative restrictions" Article XI also disciplines "other measures", is "unclear" because it does not specify whether those "other measures" must also restrict export *quantities*, or whether they comprise "all applicable measures" regardless of whether they limit quantities.³⁸⁹ In Saudi Arabia's opinion, Article XI prohibits only "measures that restrict, and are designed to restrict, export quantities".³⁹⁰

204. Saudi Arabia reiterates its view, based on the panel report in *China – Publications and Audiovisual Products*, that a licensing system is "discretionary" where the administering authority enjoys "the freedom to choose, based essentially on its own preference, whether or not such [licences] are granted".³⁹¹ A system in which export licences "are not 'granted in all cases', but which mandates the authority's application of a 'hard-and-fast rule' that limits the freedom of the administering authority to determine whether to grant a licence", would not be discretionary and would therefore be permissible under Article XI:1 of the GATT 1994.³⁹²

7. Turkey

205. Recalling the text of Paragraph 11.3 of China's Accession Protocol, Turkey notes that it "openly refers" to Annex 6 and Article VIII as exceptions, and suggests that, had it been foreseen that

³⁸⁷Saudi Arabia's third participant's submission, para. 23 (quoting Panel Reports, para. 7.917). Saudi Arabia notes that, although the Panel found that the *Import Licensing Agreement* provided "only limited assistance" in interpreting Article XI of the GATT 1994 and therefore chose not to use the "standard nomenclature" of "automatic", "non-automatic", and "discretionary", these terms help to create "a systematic analytical framework for determining permissible licensing under Article XI". (*Ibid.*, para. 24 (quoting Panel Reports, paras. 7.911 and 7.915))

³⁸⁸Saudi Arabia's third participant's submission, para. 24 (referring to Panel Reports, paras. 7.916 and 7.917).

³⁸⁹Saudi Arabia's third participant's submission, para. 26 (quoting Panel Reports, paras. 7.912 and 7.913).

³⁹⁰Saudi Arabia's third participant's submission, para. 29. (original emphasis)

³⁹¹Saudi Arabia's third participant's submission, para. 35 (quoting Panel Report, *China – Publications and Audiovisual Products*, para. 7.324). See also Panel Report, *Turkey – Rice*, paras. 7.128, 7.133, and 7.134. Based on this interpretation of the term "discretion", Saudi Arabia agrees with the panel's findings in *India – Quantitative Restrictions* that "India's licensing system for goods ... is a discretionary import licensing system, in that licences are not granted in all cases, but rather on unspecified 'merits'". (Saudi Arabia's third participant's submission, para. 36 (quoting Panel Report, *India – Quantitative Restrictions*, para. 5.130))

³⁹²Saudi Arabia's third participant's submission, para. 37.

the exceptions in Article XX of the GATT 1994 would apply to Paragraph 11.3 of the Protocol, there would have also been an "open referral" to Article XX.³⁹³ Recalling China's argument that a harmonious reading of Paragraph 11.3 of its Accession Protocol and Paragraph 170 of its Accession Working Party Report would justify China's export duties, Turkey notes that the textual differences between Paragraphs 11.3 and 5.1 of China's Accession Protocol may preclude this.

206. Regarding the interpretation of the words "temporarily applied" in Article XI:2(a), Turkey submits that temporarily applied measures are limited to measures that are: (i) applied for a "determined and limited period of time"; (ii) predicted to last until a "certain date"; or (iii) predicted to expire upon "the occurrence of certain events".³⁹⁴ For Turkey, the temporariness of the application of the measure must be expected from the beginning of the application of the measure, and the amount of time that the measure is intended to stay in place should be "foreseeable".³⁹⁵ Furthermore, Turkey maintains that there must be a "close link" between the temporary nature of the measure and its objective to relieve or prevent a critical shortage, and that therefore a measure applied under Article XI:2(a) "should be capable" of preventing or relieving the shortage.³⁹⁶

III. **Issues Raised on Appeal**

207. The following issues are raised on appeal by China:

- (a) whether the Panel erred in finding that Section III of the complainants' panel requests complies with the requirement in Article 6.2 of the DSU to "provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly";
- (b) whether the Panel acted inconsistently with Articles 7.1, 11, and 19.1 of the DSU by recommending that China bring its export duty and export quota measures into conformity with its WTO obligations such that the "series of measures" in force at the date of the Panel's establishment do not operate to bring about a WTO-inconsistent result;
- (c) whether the Panel erred in finding that China may not have recourse to the exceptions contained in Article XX of the GATT 1994 in order to justify a violation of China's export duty commitments contained in Paragraph 11.3 of China's Accession Protocol;

³⁹³Turkey's third participant's submission, para. 8.

³⁹⁴Turkey's third participant's submission, para. 14.

³⁹⁵Turkey's third participant's submission, para. 14.

³⁹⁶Turkey's third participant's submission, para. 15.

- (d) whether the Panel erred in its interpretation and application of Article XI:2(a) of the GATT 1994, and in its assessment of the matter under Article 11 of the DSU, when it found that China's export quota on refractory-grade bauxite is not "temporarily applied" to prevent or relieve a "critical shortage";
- (e) whether the Panel erred by interpreting the phrase "made effective in conjunction with" in Article XX(g) of the GATT 1994 to require that the purpose of the export restriction be to ensure the effectiveness of restrictions on domestic production and consumption;
- (f) whether the Panel erred in finding that China acts inconsistently with Paragraphs 1.2 and 5.1 of China's Accession Protocol, read in combination with Paragraphs 83 and 84 of China's Accession Working Party Report, by requiring exporters to comply with prior export performance and minimum registered capital requirements in order to obtain a quota allocation of certain raw materials;
- (g) whether the Panel erred in its interpretation and application of Article X:3(a) of the GATT 1994, and acted inconsistently with its obligations under Article 11 of the DSU, in finding that the administration of the "operation capacity" criterion in Article 19 of China's *Export Quota Administration Measures* is non-uniform and unreasonable; and
- (h) whether the Panel erred in its interpretation and application of Article XI:1 of the GATT 1994, and acted inconsistently with Article 11 of the DSU, in finding that China's export licensing system is inconsistent with China's WTO obligations, because it constitutes a restriction on exportation.

208. The following issues are raised on appeal by the United States:

- (a) if the Appellate Body reverses the Panel's recommendations as requested by China on appeal, then whether the Panel erred, under Articles 6.2, 7.1, 11, and 19.1 of the DSU, in not making recommendations on the 2009 export quota and export duty measures that were annually recurring and in effect at that time; and
- (b) whether the Panel erred in finding that China's imposition of a bid-winning price on the allocation of export quotas on bauxite, fluorspar, and silicon carbide based on the

bid-winning price is not inconsistent with Article VIII:1(a) of the GATT 1994 or Paragraph 11.3 of China's Accession Protocol.

209. The following issue is raised on appeal by the European Union:

- (a) if the Appellate Body reverses the Panel's recommendations as requested by China on appeal, and rejects the relevant other appeals submitted by the United States and Mexico, then whether the Panel erred in finding that the European Union requested the Panel not to make any findings and recommendations on the 2010 "replacement measures" and thereby narrowed the Panel's terms of reference.

210. The following issues are raised on appeal by Mexico:

- (a) if the Appellate Body reverses the Panel's recommendations as requested by China on appeal, then whether the Panel erred, under Articles 6.2, 7.1, 11, and 19.1 of the DSU, in not making recommendations on the 2009 export quota and export duty measures that were annually recurring and in effect at that time; and
- (b) whether the Panel erred in its interpretation and application of Article X:3(a) of the GATT 1994, and acted inconsistently with Article 11 of the DSU, in finding that the participation of China's Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters (the "CCCMEC") in China's export quota allocation process is not partial or unreasonable.

IV. The Panel's Terms of Reference

211. We begin by examining China's appeal of the Panel's finding that Section III of the complainants' panel requests³⁹⁷, entitled "Additional Restraints Imposed on Exportation", identifies the measures and claims at issue in a manner sufficient to present the problem clearly, as required under Article 6.2 of the DSU. China requests the Appellate Body to reverse this finding, and to find instead that Section III of the panel requests does not comply with Article 6.2 of the DSU, with the

³⁹⁷Request for the Establishment of a Panel by the United States (WT/DS394/7); Request for the Establishment of a Panel by the European Communities (WT/DS395/7); Request for the Establishment of a Panel by Mexico (WT/DS398/6). The panel requests are attached to these Reports as Annexes I-III, respectively.

exception of the complainants' claims under Article X:1 of the GATT 1994 regarding the non-publication of the total amount and procedure for the allocation of the zinc export quota.³⁹⁸

212. Before turning to assess China's claim of error under Article 6.2 of the DSU, we consider it useful to describe briefly how this issue arose before the Panel, as well as the Panel's approach to the issue.

A. *Proceedings before the Panel and the Panel's Findings*

213. On 4 November 2009, the United States, the European Communities, and Mexico filed the panel requests that form the basis of the present dispute. At the request of the complainants, the DSB established a single panel pursuant to Article 9.1 of the DSU at its 21 December 2009 meeting. At this DSB meeting, China informed the DSB of its intention to seek a preliminary ruling on the adequacy of the complainants' panel requests and their consistency with the requirements of Article 6.2 of the DSU.³⁹⁹ On 31 March 2010, one day after Panel composition, China submitted a request for a preliminary ruling by the Panel.⁴⁰⁰ China contended that the panel requests did not comply with the requirements of Article 6.2 of the DSU because they failed to provide "a brief

³⁹⁸See China's appellant's submission, paras. 97 and 98 (referring to Panel Reports, para. 7.3(b); and second phase of the Preliminary Ruling by the Panel dated 1 October 2010, Panel Reports, Annex F-2 (the "Panel's preliminary ruling (second phase)"), para. 77). As a consequence of this reversal, China also requests the Appellate Body to reverse the Panel's findings regarding claims made by the complainants on the basis of Section III of the panel requests, including the findings in paragraphs 7.669, 7.670, 7.678, 7.756, 7.807, 7.958, 7.1082, 7.1102, 7.1103, 8.4(a)-(b), 8.5(b), 8.6(a)-(b), 8.11(a), (c), (e), and (f), 8.12(b), 8.13(a)-(b), 8.18(a)-(b), 8.19(b), and 8.20(a)-(b) of the Panel Reports. (China's appellant's submission, para. 98) Although China includes paragraph 8.11(f) of the Panel Reports in its request for reversal, we note that this finding concerns the failure to publish the total amount and procedure for the allocation of the zinc export quota, which China specifically excludes from its appeal in its appellant's submission.

³⁹⁹WT/DSB/M/277, para. 74; see also Panel Reports, para. 1.10. The intervention of the representative of China at the 21 December 2009 regular meeting of the DSB is reflected as follows in the minutes of the meeting:

The representative of China said that ... Section III of the Complainants' Panel Requests, titled "Additional Restraints Imposed on Exportation", described various "complaints", and listed 37 "measures", along with 13 treaty provisions. However, the requests had failed to make any connection between: (1) the "complaints" and the "measures"; (2) the "measures" and the treaty provisions; and, (3) the treaty provisions and the "complaints". As a result, the complainants' requests were "[i]nsufficient to present the problem clearly", within the meaning of Article 6.2 of the DSU. In those and other respects, the three complainants had prejudiced China's ability to prepare its defence. Since the complainants wished to proceed with panel establishment, China would seek a preliminary ruling on the requests' consistency with Article 6.2 of the DSU.

⁴⁰⁰Communication from China to the Panel: China's request for a preliminary ruling pursuant to Article 6.2 of the DSU, 30 March 2010 ("China's request for a preliminary ruling"); Panel Reports, para. 1.11.

summary of the legal basis of the complaint sufficient to present the problem clearly".⁴⁰¹ In particular, with respect to Section III of the panel requests, China alleged that the requests failed to "plainly connect": (i) the narrative paragraphs and the 37 listed measures; (ii) the 37 listed measures and the 13 listed treaty provisions; and (iii) the 13 listed treaty provisions and the narrative paragraphs.⁴⁰²

214. On 21 April 2010, the complainants submitted a joint response to China's request for a preliminary ruling.⁴⁰³ In their joint response, the complainants argued that Section III of their panel requests starts by providing a narrative description of the additional restraints on exportation, "identifies the relevant Chinese measures", and indicates that the complainants considered "the identified measures to be inconsistent with the enumerated legal obligations".⁴⁰⁴ For the complainants, this was "sufficient to connect the relevant measures with the legal obligations".⁴⁰⁵ The complainants did not provide additional information at that stage of the proceedings. The Panel held a meeting with the parties, as well as a separate session with the third parties, on 29 April 2010.⁴⁰⁶

215. The Panel issued a preliminary ruling in two phases⁴⁰⁷ responding to China's allegation that Section III of the complainants' panel requests failed to comply with Article 6.2 of the DSU.⁴⁰⁸ The first phase of the preliminary ruling was issued to the parties on 7 May 2010 and circulated to WTO Members on 18 May 2010.⁴⁰⁹ The Panel stated that "the sufficiency of a panel request is to be determined by taking into account the Parties' first written submissions in order to assess fully whether the ability of the respondent to defend itself was prejudiced."⁴¹⁰ Accordingly, the Panel decided to "reserve its decision" on whether Section III of the complainants' panel requests satisfied the requirements of Article 6.2 of the DSU until after it had examined the parties' first written submissions and was "more able to take fully into account China's ability to defend itself".⁴¹¹ In so doing, the Panel referred to an "undertaking from a representative" of the complainants to the effect

⁴⁰¹China's request for a preliminary ruling, paras. 3 and 30.

⁴⁰²China's request for a preliminary ruling, para. 50.

⁴⁰³Joint Communication from the United States, the European Union, and Mexico to the Request for a Preliminary Ruling submitted by China, 21 April 2010 (the "complainants' response to China's request for a preliminary ruling"); Panel Reports, para. 1.11.

⁴⁰⁴Complainants' response to China's request for a preliminary ruling, para. 30.

⁴⁰⁵Complainants' response to China's request for a preliminary ruling, para. 30.

⁴⁰⁶Panel Reports, para. 1.11.

⁴⁰⁷The first and second phases of the preliminary ruling were attached as Annexes F-1 and F-2 to the Panel Reports. (See Panel Reports, paras. 1.12 and 1.13)

⁴⁰⁸Panel Reports, para. 1.12.

⁴⁰⁹WT/DS394/9, WT/DS395/9, WT/DS398/8.

⁴¹⁰Panel's preliminary ruling (first phase), para. 37.

⁴¹¹Panel's preliminary ruling (first phase), para. 39.

that "all possible concerns over the undefined scope of their challenge [would] be answered once China and the Panel receive[d] the Complainants' first written submissions".⁴¹² The Panel added that it was not saying that "all flaws in a panel request can be cured by a first written submission".⁴¹³ The Panel also said that it "expect[ed] that the Complainants [would] clarify in their first written submissions which of the listed measures (or group thereof) for which specific products (or group thereof) are inconsistent with which specific WTO obligations among those listed in the last part of Section III of their panel requests".⁴¹⁴

216. On 6 September 2010, following the first Panel meeting, the Panel requested the complainants to list all the measures for which they were seeking recommendations and which WTO provisions each of these measures was alleged to violate.⁴¹⁵ In response, the complainants submitted, on 13 September 2010, a chart setting out, in three columns, the type of "Export Restraint" involved, the respective "Measures, *i.e.*, Legal Instruments" implicated, and the "WTO Provisions Violated" by each measure. Subsequently, on 1 October 2010, the Panel issued the second phase of its preliminary ruling, where it noted that the complainants "did not directly address in their submissions or in their subsequent oral statements" the question of whether Section III of the complainants' panel requests complied with Article 6.2 of the DSU.⁴¹⁶ Nonetheless, the Panel ultimately concluded that "the complainants' first written submission[s] set out sufficient connections between the challenged measures and certain violations attributed to such measures."⁴¹⁷ In reaching this conclusion, the Panel based itself on information contained in the charts filed by the complainants in response to a question posed by the Panel following the first Panel meeting.⁴¹⁸ At the second Panel meeting on 22 November 2010, the United States, in order "[t]o clarify any confusion"⁴¹⁹, attached to its opening statement a revised chart specifying the measures on which it was seeking a finding by the Panel.⁴²⁰

217. The Panel's preliminary ruling was incorporated without changes or additional reasoning into the final Panel Reports.⁴²¹ Ultimately, the Panel rejected China's claim that Section III of the

⁴¹²Panel's preliminary ruling (first phase), para. 38.

⁴¹³Panel's preliminary ruling (first phase), para. 39.

⁴¹⁴Panel's preliminary ruling (first phase), para. 46.

⁴¹⁵Panel Question 2 following the first Panel meeting.

⁴¹⁶Panel's preliminary ruling (second phase), para. 32.

⁴¹⁷Panel's preliminary ruling (second phase), para. 65.

⁴¹⁸See Panel's preliminary ruling (second phase), para. 66: "Indeed, the complainants clarified the connection of the measures at hand with the specific claims in their responses to question No. 2 posed by the Panel" after the first Panel meeting.

⁴¹⁹United States' opening statement at the second Panel meeting, para. 128.

⁴²⁰Revised Chart B in response to Panel Question 2 submitted by the United States following the second Panel meeting (Panel Exhibit US-1).

⁴²¹Panel Reports, Annex F; see also paras. 7.1-7.4.

complainants' panel requests failed to provide "a brief summary of the legal basis of the complaint sufficient to present the problem clearly". The Panel concluded that, with the exception of one claim of the European Union, "[t]he complainants' Panel Requests, as clarified by their first submissions, provide sufficient connection between the measures listed in Section III and the listed claims of violations".⁴²²

B. *Whether Section III of the Complainants' Panel Requests Complies with the Requirements of Article 6.2 of the DSU*

218. Article 6.2 of the DSU provides, in relevant part:

The request for the establishment of a panel shall be made in writing. It shall indicate whether consultations were held, identify the specific measures at issue and provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly.

219. The Appellate Body has explained that Article 6.2 of the DSU serves a pivotal function in WTO dispute settlement and sets out two key requirements that a complainant must satisfy in its panel request, namely, the "identification of the specific measures at issue, and the provision of a brief summary of the legal basis of the complaint (or the claims)".⁴²³ Together, these two elements constitute the "*matter*" referred to the DSB, so that, if either of them is not properly identified, the matter would not be within the panel's terms of reference.⁴²⁴ Fulfilment of these requirements, therefore, is "not a mere formality".⁴²⁵ As the Appellate Body has noted, a panel request forms the basis for the terms of reference of panels, in accordance with Article 7.1 of the DSU.⁴²⁶ Moreover, it serves the due process objective of notifying the respondent and third parties of the nature of a complainant's case.⁴²⁷ The identification of the specific measures at issue and the provision of "a brief summary of the legal basis of the complaint sufficient to present the problem clearly" are therefore central to defining the scope of the dispute to be addressed by the panel.

⁴²²Panel Reports, para. 7.3(b).

⁴²³Appellate Body Report, *US – Carbon Steel*, para. 125. (emphasis omitted)

⁴²⁴Appellate Body Report, *US – Carbon Steel*, para. 125. (emphasis added)

⁴²⁵Appellate Body Report, *Australia – Apples*, para. 416.

⁴²⁶See Appellate Body Report, *Guatemala – Cement I*, paras. 72 and 73; Appellate Body Report, *US – Carbon Steel*, para. 125; Appellate Body Report, *US – Continued Zeroing*, para. 160; and Appellate Body Report, *US – Zeroing (Japan) (Article 21.5 – Japan)*, para. 107.

⁴²⁷Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 786; see also paras. 639 and 640 (referring to Appellate Body Report, *US – Carbon Steel*, para. 126, in turn referring to Appellate Body Report, *Brazil – Desiccated Coconut*, p. 22, DSR 1997:1, 167, at 186).

220. In order to determine whether a panel request is sufficiently precise to comply with Article 6.2 of the DSU, a panel must scrutinize carefully the language used in the panel request.⁴²⁸ This involves a case-by-case analysis. Submissions by a party may be referenced in order to *confirm* the meaning of the *words used* in the panel request; but the content of those submissions "cannot have the effect of curing the failings of a deficient panel request".⁴²⁹ For example, whether a panel request identifies the "specific measures at issue" may depend on the particular context in which those measures operate and may require examining the extent to which they are capable of being precisely identified.⁴³⁰ At the same time, whether a panel request challenging a number of measures on the basis of multiple WTO provisions sets out "a brief summary of the legal basis of the complaint sufficient to present the problem clearly" may depend on whether it is sufficiently clear which "problem" is caused by which measure or group of measures. The Appellate Body has explained that, in order "to present the problem clearly", a panel request must "plainly connect the challenged measure(s) with the provision(s) of the covered agreements claimed to have been infringed".⁴³¹ Furthermore, to the extent that a provision contains not one single, distinct obligation, but rather multiple obligations, a panel request might need to specify which of the obligations contained in the provision is being challenged.⁴³² In our view, a defective panel request may impair a panel's ability to perform its adjudicative function within the strict timeframes contemplated in the DSU and, thus, may have implications for the prompt settlement of a dispute in accordance with Article 3.3 of the DSU. A complaining Member should therefore be particularly vigilant in preparing its panel request, especially when numerous measures are challenged under several different treaty provisions.

221. With these considerations in mind, we turn to the panel requests at issue in this dispute. We note that the complainants' panel requests are each structured in three separate sections. Section I, entitled "Export Quotas", challenges the imposition of export quotas on bauxite, coke, fluorspar, silicon carbide, and zinc as inconsistent with Article XI:1 of the GATT 1994 and Paragraphs 162 and 165 of the Report of the Working Party on the Accession of China⁴³³ ("China's Accession Working Party Report"). In Section II, entitled "Export Duties", the complainants claim that China imposes export duties on bauxite, coke, fluorspar, magnesium, manganese, silicon metal, yellow

⁴²⁸See Appellate Body Report, *EC – Fasteners (China)*, para. 562.

⁴²⁹Appellate Body Report, *EC – Fasteners (China)*, para. 562 (referring to Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 642; Appellate Body Report, *EC – Bananas III*, para. 143; and Appellate Body Report *US – Carbon Steel*, para. 127).

⁴³⁰Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 641.

⁴³¹Appellate Body Report, *US – Oil Country Tubular Goods Sunset Reviews*, para. 162.

⁴³²See Appellate Body Report, *Korea – Dairy*, para. 124. See also Appellate Body Report, *EC – Fasteners (China)*, para. 598.

⁴³³WT/ACC/CHN/49 and Corr.1.

phosphorous, and zinc in violation of its commitments under Paragraph 11.3 of the Protocol on the Accession of the People's Republic of China to the WTO⁴³⁴ ("China's Accession Protocol"). Whereas Sections I and II each addresses a single form of export restriction, Section III covers a wider set of allegations directed at what is referred to in the title of Section III as "Additional Restraints Imposed on Exportation".

222. The introductory paragraph in Section III states, in broad terms, that "China imposes other restraints on the exportation of the materials, administers its measures in a manner that is not uniform, impartial, and reasonable, imposes excessive fees and formalities on exportation, and does not publish certain measures pertaining to requirements, restrictions, or prohibitions on exports." This paragraph is followed by five separate paragraphs in the case of the United States and Mexico, and six paragraphs in the case of the European Union, setting out different allegations of violation relating to varied situations in which obligations under the WTO agreements might not be satisfied, namely, allegations relating to the administration of export quotas, allocation of export quotas, publication of export quota amounts and application procedures, export licensing requirements, minimum export price requirements, and fees and formalities.

223. Each of these paragraphs briefly describes a number of different allegations of violation relating to different types of restraints. These narrative paragraphs are worded in virtually identical terms in each of the three panel requests. They state:

China administers the export quotas imposed on bauxite, coke, fluorspar, silicon carbide, and zinc discussed in Section I above, through its ministries and other organizations under the State Council as well as chambers of commerce and industry associations, in a manner that restricts exports and is not uniform, impartial and reasonable. In connection with the administration of the quotas for these materials, China imposes restrictions on the right of Chinese enterprises as well as foreign enterprises and individuals to export.

China allocates the export quotas imposed on bauxite, fluorspar, and silicon carbide discussed in Section I above, through a bidding system. China administers the requirements and procedures for this bidding system through its ministries and other organizations under the State Council as well as chambers of commerce and industry associations, in a manner that restricts exports and is not uniform, impartial and reasonable. In connection with the administration of this bidding system, China also requires foreign-invested enterprises to satisfy certain criteria in order to export these materials that Chinese enterprises need not satisfy. [Further, China requires

⁴³⁴WT/L/432.

enterprises to pay a charge in order to export these materials that is excessive and imposes excessive formalities on the exportation of these materials.*]

China does not publish the amount for the export quota for zinc or any conditions or procedures for applying entities to qualify to export zinc.

In addition, China restricts the exportation of bauxite, coke, fluorspar, manganese, silicon carbide, and zinc by subjecting these materials to non-automatic licensing. China imposes the non-automatic export licensing for bauxite, coke, fluorspar, silicon carbide, and zinc in connection with the administration of the export quotas discussed in Section I, as an additional restraint on the exportation of those materials.

China also imposes quantitative restrictions on the exportation of the materials by requiring that prices for the materials meet or exceed a minimum price before they may be exported. Further, through its ministries and other organizations under the State Council as well as chambers of commerce and industry associations, China administers the price requirements in a manner that restricts exports and is not uniform, impartial, and reasonable. China also does not publish certain measures relating to these requirements in a manner that enables governments and traders to become acquainted with them.

[China also imposes excessive fees and formalities in relation to the exportation of the materials.**]

[*This sentence is contained in the panel requests of the United States and Mexico only.]

**This sentence is contained in the panel request of the European Union only.]

224. Following these narrative paragraphs, each of the three panel requests provides an identical bullet point list of 37 legal instruments, introduced by the phrase: "[The complainant] understands that these Chinese measures are reflected in, among others: ..."⁴³⁵ The legal instruments listed range from entire codes or charters (such as the Foreign Trade Law of the People's Republic of China⁴³⁶ (China's "*Foreign Trade Law*") to specific administrative measures (such as the Quotas of Fluorspar

⁴³⁵While the phrase introducing the 37 legal instruments refers to "these Chinese measures" in a manner that might suggest that the complainants regarded the text of the narrative paragraphs as setting forth the measures at issue, the subsequent submissions clarified the meaning of the word "measures" as a synonym for the 37 legal instruments. In fact, in its response to Panel Question 2 following the first Panel meeting, the United States and Mexico referred to them as "Measures, i.e., Legal Instruments" and the European Union as "Measures/Legal instruments".

⁴³⁶Foreign Trade Law of the People's Republic of China, adopted at the 8th Session of the Standing Committee of the Tenth National People's Congress on 6 April 2004, 1 July 2004 (Panel Exhibits CHN-151 and JE-72).

Lump (Powder) of 2009⁴³⁷ ("*2009 First Round Fluorspar Bidding Procedures*"). The complainants' panel requests do not identify specific sections or provisions of any of the listed instruments.

225. The final paragraph of Section III of the panel requests consists of a list of 13 treaty provisions. The United States and Mexico state that they consider that "these measures are inconsistent with Article VIII:1(a) and VIII:4, Article X:1 and X:3(a), and Article XI:1 of the GATT 1994 and paragraphs 2(A)2, 5.1, 5.2 and 8.2 of Part I of the Accession Protocol, as well as China's obligations under the provisions of paragraph 1.2 of Part I of the Accession Protocol, which incorporates commitments in paragraphs 83, 84, 162, and 165 of the Working Party Report."⁴³⁸ The final paragraph in Section III of the European Union's panel request is textually identical, except that it refers to Article VIII:1 of the GATT 1994 instead of Article VIII:1(a) of the GATT 1994.

226. China does not contest that Section III of the panel requests identifies the challenged measures with sufficient specificity to comply with Article 6.2 of the DSU. Rather, at issue here is whether Section III provides "a brief summary of the legal basis of the complaint sufficient to present the problem clearly". As the Appellate Body found in *EC – Selected Customs Matters*, a brief summary of the legal basis of the complaint as required by Article 6.2 of the DSU should "explain succinctly *how or why* the measure at issue is considered by the complaining Member to be violating the WTO obligation in question".⁴³⁹ Based on our reading of the complainants' panel requests in the present case, it is not clear which allegations of error pertain to which particular measure or set of measures identified in the panel requests. Furthermore, it is unclear whether each of the listed measures relates to one specific allegation described in the narrative paragraphs, or to several or even all of these allegations, and whether each of the listed measures allegedly violates one specific provision of the covered agreements, or several of them.⁴⁴⁰

227. First, the complainants identify, for instance, China's *Foreign Trade Law* as a measure at issue. Yet from the language of Section III of the panel requests it is impossible to discern which of the several allegations of violation described in the narrative paragraphs is alleged to have been

⁴³⁷Quotas of Fluorspar Lump (Powder) of 2009, Committee for the Invitation for bid for Export Commodity Quotas, 10 December 2008 (Panel Exhibit JE-93).

⁴³⁸See, for example, United States' panel request, p. 9.

⁴³⁹Appellate Body Report, *EC – Selected Customs Matters*, para. 130.

⁴⁴⁰As noted *supra*, para. 211, China does not argue that the claim regarding the non-publication of the zinc export quota fails to comply with Article 6.2 of the DSU. Moreover, as this claim concerns a failure to publish a measure, we consider that the language in the fourth narrative paragraph of Section III of the panel requests, together with the listing of Article X:1 of the GATT 1994 in Section III, satisfies the requirements of Article 6.2 of the DSU.

caused by the *Foreign Trade Law*, or which provision or provisions of the covered agreements listed in the concluding paragraph are alleged to have been violated by that measure.

228. Second, the WTO provisions listed in Section III contain a wide array of dissimilar obligations.⁴⁴¹ More specifically, the complainants state that "these measures are inconsistent with Article VIII:1(a)⁴⁴² and VIII:4, Article X:1 and X:3(a), and Article XI:1 of the GATT 1994 and paragraphs 2(A)2, 5.1, 5.2 and 8.2 of Part I of the Accession Protocol, as well as China's obligations under the provisions of paragraph 1.2 of Part I of the Accession Protocol, which incorporates commitments in paragraphs 83, 84, 162, and 165 of the Working Party Report." China's obligations under these various provisions are quite diverse and therefore it cannot be discerned what the particular "problem" is under Article 6.2 of the DSU with respect to the legal instruments listed in Section III.

229. Third, the narrative paragraphs describe in a general manner different allegations of error related to different types of restraints, and do not make clear which measures, or which groups of measures acting collectively, are alleged to be inconsistent with which treaty provisions. For example, the second narrative paragraph of the complainants' panel requests states that "China administers the export quotas ... through its ministries and other organizations under the State Council as well as chambers of commerce and industry associations, in a manner that restricts exports and is not uniform, impartial and reasonable" and alleges that, "[i]n connection with the administration of the quotas for these materials, China imposes restrictions on the right of Chinese enterprises as well as foreign enterprises and individuals to export".⁴⁴³ This language, when read together with the legal instruments identified in the panel requests and the WTO provisions identified in Section III, groups together disparate problems arising under different treaty provisions.

⁴⁴¹See Appellate Body Report, *Korea – Dairy*, para. 124.

⁴⁴²We note that, in its panel request, the European Union invokes more broadly Article VIII:1 of the GATT 1994.

⁴⁴³The second narrative paragraph of Section III of the complainants' panel requests reads in full as follows:

China administers the export quotas imposed on bauxite, coke, fluorspar, silicon carbide, and zinc discussed in Section I above, through its ministries and other organizations under the State Council as well as chambers of commerce and industry associations, in a manner that restricts exports and is not uniform, impartial and reasonable. In connection with the administration of the quotas for these materials, China imposes restrictions on the right of Chinese enterprises as well as foreign enterprises and individuals to export.

230. As the Appellate Body has explained, a claim must be presented in a manner that presents the problem clearly within the meaning of Article 6.2.⁴⁴⁴ We do not consider this to have been the case here, where Section III of the complainants' panel requests refers generically to "Additional Restraints Imposed on Exportation" and raises multiple problems stemming from several different obligations arising under various provisions of the GATT 1994, China's Accession Protocol, and China's Accession Working Party Report. Neither the titles of the measures nor the narrative paragraphs reveal the different groups of measures that are alleged to act collectively to cause each of the various violations, or whether certain of the measures is considered to act alone in causing a violation of one or more of the obligations.

231. Like the Panel, we do not read Section III of the complainants' panel requests as advancing all claims, under all treaty provisions, with respect to all measures. Instead, it appears to us that the complainants were challenging some (groups of) measures as inconsistent with some (groups) of the listed WTO obligations.⁴⁴⁵ In the present case, the combination of a wide-ranging list of obligations together with 37 legal instruments ranging from China's *Foreign Trade Law* to specific administrative measures applying to particular products is such that it does not allow the "problem" or "problems" to be discerned clearly from the panel requests. Because the complainants did not, in either the narrative paragraphs or in the final listing of the provisions of the covered agreements alleged to have been violated, provide the basis on which the Panel and China could determine with sufficient clarity what "problem" or "problems" were alleged to have been caused by which measures, they failed to present the legal basis for their complaints with sufficient clarity to comply with Article 6.2 of the DSU.

232. With respect to the consequences of the failure to comply with the requirements of Article 6.2 of the DSU, the participants disagree as to whether the Panel frustrated China's due process rights under that provision. China alleges that, when the panel requests were filed, it was not able to begin preparation of its defence with respect to the claims listed in Section III of the panel requests, "because the measures implicated by the different narrative paragraphs, and the claims made regarding those measures, could not be identified".⁴⁴⁶ The European Union responds that China "effectively and exhaustively" defended all the claims made by the complainants in its first written submission to the Panel, and that this demonstrates that China's due process rights were not compromised.⁴⁴⁷ Referring to China's statement that the complainants have made "several subsets of

⁴⁴⁴See Appellate Body Report, *EC – Fasteners (China)*, para. 597.

⁴⁴⁵Panel's preliminary ruling (first phase), para. 36.

⁴⁴⁶China's appellant's submission, para. 85.

⁴⁴⁷European Union's appellee's submission, para. 25.

claims with respect to several subsets of measures affecting several subsets of product categories"⁴⁴⁸, the United States and Mexico argue that China was aware of "both the possible and likely claims that the Co-Complainants could advance against it".⁴⁴⁹

233. The Appellate Body has clarified that due process "is not constitutive of, but rather follows from, the proper establishment of a panel's jurisdiction".⁴⁵⁰ We find it troubling therefore that the Panel, having correctly recognized that a deficient panel request cannot be cured by a complaining party's subsequent written submissions, nonetheless decided to "reserve its decision" on whether the panel requests complied with the requirements of Article 6.2 until after it had examined the parties' first written submissions and was "more able to take fully into account China's ability to defend itself".⁴⁵¹ The fact that China may have been able to defend itself does not mean that Section III of the complainants' panel requests in this dispute complied with Article 6.2 of the DSU. In any event, compliance with the due process objective of Article 6.2 cannot be inferred from a respondent's response to arguments and claims found in a complaining party's first written submission. Instead, it is reasonable to expect, in our view, that a rebuttal submission would address arguments contained in the complaining party's first written submission. We also find it troubling that the second phase of the Panel's preliminary ruling came only at an advanced stage in the proceedings, on 1 October 2010.

234. In the light of the failure to provide sufficiently clear linkages between the broad range of obligations contained in Articles VIII:1(a), VIII:4, XI:1, X:3(a), and XI:1 of the GATT 1994, Paragraphs 2(A)2, 5.1, 5.2, and 8.2 of Part I of China's Accession Protocol, and Paragraphs 83, 84, 162, and 165 of China's Accession Working Party Report, and the 37 challenged measures, we do not consider that Section III of the complainants' panel requests satisfies the requirement in Article 6.2 of the DSU to provide "a brief summary of the legal basis of the complaint sufficient to present the problem clearly".

235. Consequently, we find that the Panel erred under Article 6.2 of the DSU in making findings regarding claims allegedly identified in Section III of the complainants' panel requests. We therefore declare moot and of no legal effect the Panel's findings in paragraphs 8.4(a)-(d), 8.11(a)-(e), and 8.18(a)-(d) in respect of claims concerning export quota administration and allocation; paragraphs 8.5(a)-(b), 8.12(a)-(b), and 8.19(a)-(b) in respect of claims concerning export licensing

⁴⁴⁸Joint appellees' submission of the United States and Mexico, para. 57 (referring to China's comments on the complainants' joint response to China's request for a preliminary ruling, para. 49).

⁴⁴⁹Joint appellees' submission of the United States and Mexico, para. 57.

⁴⁵⁰Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 640.

⁴⁵¹Panel's preliminary ruling (first phase), para. 39.

requirements; paragraphs 8.6(a)-(b), 8.13(a)-(b), and 8.20(a)-(b) in respect of claims concerning a minimum export price requirement; and paragraphs 8.4(c) and 8.18(e) of the Panel Reports in respect of claims concerning fees and formalities in connection with exportation. In these circumstances, we have no basis to consider further the arguments raised by China in its appeal and by the complainants in their other appeals regarding these findings.

V. The Panel's Recommendations

236. We now turn to address China's appeal regarding the Panel's recommendations concerning export duties and export quotas.

237. China seeks review of the Panel's recommendations "to the extent that they apply to annual replacement measures" adopted after the establishment of the Panel on 21 December 2009.⁴⁵² China argues that the complainants had excluded such measures from the scope of the dispute and, hence, by making recommendations extending to such measures, the Panel acted inconsistently with its obligations under Article 7.1 of the DSU; failed to make an objective assessment of the matter under Article 11 of the DSU; and made recommendations on measures that were not part of the matter, inconsistently with Article 19.1 of the DSU.⁴⁵³ In response, the United States, the European Union, and Mexico argue that the Panel's recommendations were correctly made in accordance with Articles 7.1, 11, and 19.1 of the DSU on the measures challenged by the complainants as they existed at the time of the Panel's establishment. The United States and Mexico posit that, without such recommendations, "trade measures imposed in part through annually recurring legal instruments could never be successfully challenged through WTO dispute settlement".⁴⁵⁴ The European Union adds that "this is not the proper forum to determine the actions China should take in order to bring itself into compliance with its WTO obligations"; rather, China should follow the procedures provided for under Article 21 of the DSU in order to identify the scope of its compliance obligations.⁴⁵⁵

238. The Panel included the following paragraph in the final section of its Reports, setting out its conclusions and recommendations:

Pursuant to Article 19.1 of the DSU, having found that China has acted inconsistently with Articles X:1, X:3(a) and XI:1 of the GATT 1994; Paragraphs 1.2, 5.1 and 11.3 of China's Accession Protocol; and Paragraphs 83 and 84 of China's Working Party Report,

⁴⁵²China's appellant's submission, para. 136.

⁴⁵³China's appellant's submission, section III.D.2.

⁴⁵⁴Joint appellees' submission of the United States and Mexico, para. 72.

⁴⁵⁵European Union's appellee's submission, para. 43.

the Panel recommends that the Dispute Settlement Body requests China to bring the existing measures at issue into conformity with its obligations under the GATT 1994, China's Accession Protocol and China's Working Party Report. The Panel makes no recommendation on expired measures, namely the 2009 measures at issue and pre-2009 MEP-related measures. In respect of findings concerning export duties and export quotas, the Panel found that the series of measures operating collectively has resulted in the imposition of export duties or export quotas that are inconsistent with China's WTO obligations. The Panel, therefore, recommends that the Dispute Settlement Body requests China to bring its measures into conformity with its WTO obligations such that the "series of measures" does not operate to bring about a WTO-inconsistent result.⁴⁵⁶

239. Before turning to address China's arguments on appeal, we consider it useful to describe the procedural context in which this issue arose and to outline the multiple steps in the Panel's analysis that led it to make findings and recommendations on a "series of measures".

A. *Proceedings before the Panel and the Panel's Findings*

240. Before the Panel, the complainants alleged that China has acted inconsistently with its WTO obligations by imposing export quotas on certain forms of bauxite⁴⁵⁷, coke, fluorspar, silicon carbide, and zinc; and export duties on certain forms of bauxite, coke, fluorspar, magnesium, manganese, silicon metal, and zinc.⁴⁵⁸ The Panel found that these export restrictions were not introduced through a single legal instrument, but rather resulted from the application of several measures operating together.⁴⁵⁹ For each product, this group of measures, or "series of measures" as the Panel referred to it, consisted of standing framework legislation and implementing regulations, as well as a specific legal instrument or instruments identifying the individual export quotas or export duties imposed on a specific product during a particular timeframe, usually one year.⁴⁶⁰ For example, the Panel found that China imposed an export quota on certain forms of bauxite in 2009⁴⁶¹ through China's *Foreign Trade Law*, Regulation of the People's Republic of China on the Administration of the Import and Export of

⁴⁵⁶Panel Reports, paras. 8.8, 8.15, and 8.22. The Panel made the same recommendation with respect to each of the complainants.

⁴⁵⁷Three forms of bauxite are at issue in this dispute: refractory-grade bauxite (Harmonized System ("HS") number 2508.3000), aluminium ores and concentrates (HS number 2606.0000), and aluminium ash and residues (HS number 2620.4000).

⁴⁵⁸See Panel Reports, paras. 3.2, 3.3, 7.59-7.63, and 7.172-7.201. The export duty on yellow phosphorous was also challenged, but the Panel found that this duty was no longer in effect at the time of the Panel's establishment. (See *infra*, footnote 553)

⁴⁵⁹Panel Reports, paras. 7.68 and 7.218.

⁴⁶⁰Panel Reports, paras. 7.76, 7.80, 7.84, 7.88, 7.92, 7.97, 7.101, and 7.219-223.

⁴⁶¹See Panel Reports, para. 7.219.

Goods⁴⁶² ("Regulation on Import and Export Administration"), Measures of Quota Bidding for Export Commodities⁴⁶³ ("Export Quota Bidding Measures"), Measures for the Administration of Licence for the Export of Goods⁴⁶⁴ ("2008 Export Licence Administration Measures"), Announcement of the Ministry of Commerce Issuing the "2009 Graded Licence-Issuing List of Commodities Subject to Export Licence Administration"⁴⁶⁵ ("2009 Graded Export Licensing Entities Catalogue"), Working Rules on Issuing Export Licences⁴⁶⁶ ("2008 Export Licensing Working Rules"), Implementation Rules of Export Quota Bidding for Industrial Products⁴⁶⁷ ("Export Quota Bidding Implementation Rules"), Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products⁴⁶⁸ ("2009 Export Quota Amounts"), Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009⁴⁶⁹ ("2009 Announcement of Second Bidding Round for Taic and Silicon Carbide"), Notice "2009 Export Licensing Management Commodities List"⁴⁷⁰ ("2009 Export Licensing Catalogue"), Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009⁴⁷¹ ("2009 First Round Export Quota Bidding Announcement"), Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009⁴⁷² ("2009 Second Round

⁴⁶²Regulation of the People's Republic of China on the Administration of the Import and Export of Goods, passed at the forty-sixth executive meeting of the State Council on 31 October 2001, 1 January 2002 (Panel Exhibits CHN-152 and JE-73).

⁴⁶³Measures of Quota Bidding for Export Commodities, Decree of the Ministry of Foreign Trade and Economic Cooperation No. 11, adopted at the 9th ministerial office meeting of the Ministry of Foreign Trade and Economic Co-operation, 1 January 2002 (Panel Exhibits CHN-304 and JE-77).

⁴⁶⁴Measures for the Administration of Licence for the Export of Goods, Order of the Ministry of Commerce (2008) No. 11, 1 July 2008 (Panel Exhibits CHN-342 and JE-74).

⁴⁶⁵Announcement of the Ministry of Commerce Issuing the "2009 Graded Licence-Issuing List of Commodities Subject to Export Licence Administration", Ministry of Commerce, Notice (2008) No. 124, 1 January 2009 (Panel Exhibit JE-96).

⁴⁶⁶Working Rules on Issuing Export Licences, Ministry of Commerce, Shangpeifa (2008) No. 398, 9 October 2008 (Panel Exhibits CHN-344 and JE-97).

⁴⁶⁷Implementation Rules of Export Quota Bidding for Industrial Products, Ministry of Foreign Trade and Economic Cooperation, 8 November 2001 (Panel Exhibits CHN-305 and JE-78).

⁴⁶⁸Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products, Ministry of Commerce, Notice (2008) No. 83, 1 January 2009 (Panel Exhibit JE-79).

⁴⁶⁹Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009, Committee for the Invitation for bid for Export Commodity Quotas, 16 September 2009 (Panel Exhibit JE-132).

⁴⁷⁰Notice "2009 Export Licensing Management Commodities List", Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, 1 January 2009 (Panel Exhibits CHN-6 and JE-22).

⁴⁷¹Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009, Ministry of Commerce, Announcement (2008) No. 85, 30 October 2008 (Panel Exhibits CHN-309 and JE-90).

⁴⁷²Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009, Ministry of Commerce, Announcement (2009) No. 42, 8 June 2009 (Panel Exhibits CHN-310 and JE-91).

Export Quota Bidding Announcement"), and Quotas of Bauxite of 2009⁴⁷³ ("2009 First Round Bauxite Bidding Procedures"). Similarly, the Panel found that the export duties imposed in 2009 on the raw materials at issue⁴⁷⁴ were imposed through the application of China's Customs Law of the People's Republic of China⁴⁷⁵ (China's "Customs Law"), the Regulations of the People's Republic of China on Import and Export Duties⁴⁷⁶ ("Regulations on Import and Export Duties"), and the Notice Regarding the 2009 Tariff Implementation Program⁴⁷⁷ ("2009 Tariff Implementation Program").

241. In our discussion below, we refer, as did the Panel, to the groups of measures challenged by the complainants as a whole, and in force at the time of the Panel's establishment, as the various "series of measures".⁴⁷⁸ More specifically, we use the term "series of measures" to describe, collectively, the entire hierarchy of legal instruments applicable to each product, that is, the framework legislation, the regulations implementing this legislation, and the specific legal instrument or instruments identifying the individual export quotas or duties imposed on the product in 2009. We therefore do not use that term to refer, for example, to any specific legal instrument setting out an export quota amount or an export duty rate taken in isolation.

242. While the framework legislation and implementing regulations remained in effect, certain of the legal instruments setting out an export quota amount or an export duty rate identified by the complainants in their panel requests expired or were replaced during the course of the Panel proceedings.⁴⁷⁹ This was the case, for example, for the 2009 *Tariff Implementation Program*, which specified export duty rates for seven of the nine raw materials at issue during calendar year 2009. This measure expired at the end of 2009 and was replaced, with effect from 1 January 2010, by the Circular of the State Council Tariff Commission on the 2010 Tariff Implementation Plan⁴⁸⁰ ("2010

⁴⁷³Quotas of Bauxite of 2009, Committee for the Invitation for bid for Export Commodity Quotas, 10 December 2008 (Panel Exhibit JE-94).

⁴⁷⁴See Panel Reports, paras. 7.76, 7.80, 7.84, 7.88, 7.92, 7.97, and 7.101.

⁴⁷⁵Customs Law of the People's Republic of China, adopted at the 19th Meeting of the Standing Committee of the Sixth National People's Congress on 22 January 1987, amended 8 July 2000 (Panel Exhibits CHN-14 and JE-68).

⁴⁷⁶Regulations of the People's Republic of China on Import and Export Duties, Order of the State Council (2003) No. 392, adopted at the 26th executive meeting of the State Council on 29 October 2003, 1 January 2004 (Panel Exhibits CHN-13 and JE-67).

⁴⁷⁷Notice Regarding the 2009 Tariff Implementation Program, State Council Tariff Policy Commission, Shuiweihui (2008) No. 40, 1 January 2009 (Panel Exhibit JE-21).

⁴⁷⁸The term "series of measures" can be used in both the plural, as here, to refer to the various series of measures upon which the Panel made findings and recommendations in this case, or in the singular to apply to the specific series (or group) of measures imposing an export duty or export quota on a single product in 2009.

⁴⁷⁹Panel Reports, para. 7.5.

⁴⁸⁰Circular of the State Council Tariff Commission on the 2010 Tariff Implementation Plan, Shui Wei Hui [2009] No. 28, promulgated by the Customs Tariff Commission of the State Council on 8 December 2009 (Panel Exhibit CHN-5).

Tariff Implementation Plan"), which specified export duty rates for the raw materials at issue applicable as of 1 January 2010.⁴⁸¹

243. The parties disagreed as to whether the Panel should consider the series of measures as it existed in 2010, and including the specific measures setting out export duty rates or quota amounts for each product in 2010, or the series of measures as it existed at the time of the Panel's establishment in 2009, including the 2009 export duty rates and quota amounts.⁴⁸² China recognized that the Panel could make findings on 2009 measures specifying export quota and duty levels⁴⁸³, but nevertheless argued that it "would serve no purpose" for the Panel to rule on measures that have ceased to exist since they no longer violate WTO obligations or nullify or impair benefits.⁴⁸⁴

244. For their part, the complainants argued that the Panel should make findings on the "legal situation prevailing on the date of the establishment of the Panel".⁴⁸⁵ They asserted that the Panel "should not consider the claims as addressing the 2010 measures"⁴⁸⁶, and requested that the Panel not "make any findings and recommendations on any of the 2010 measures invoked by China".⁴⁸⁷ The

⁴⁸¹In 2009, bauxite and fluorspar had been subject to both export quotas and export duties. As from 1 January 2010, they were subject to only one restraint each, that is, an export quota and an export duty, respectively. (See China's first written submission to the Panel, paras. 63-67; see also United States' other appellant's submission, para. 64.)

⁴⁸²The Panel appears to have used the terms "replacement measures" and "2010 measures" interchangeably. We note, however, that the United States and Mexico explained to the Panel that:

[t]he reference in the [US][Mexico] panel request to "replacement measures" and "renewal measures" is a reference to legal instruments in existence at the time of the [US][Mexico] panel request but of which the [US][Mexico] may not have been aware, that formally "replaced" or "renewed" a legal instrument listed in the [US][Mexico] panel request but did not change its content or effect. The Panel's terms of reference are therefore not broad enough to include these legal instruments that took effect on January 1, 2010 (the January 1, 2010 Measures).

(United States' second written submission to the Panel, para. 338; Mexico's second written submission to the Panel, para. 342.)

In other words, the United States and Mexico used the term "replacement measures" to refer to measures that were in existence at the time of the panel requests. China, on the other hand, characterized the legal instruments through which the export quotas and export duties were imposed as "replacement measures", and argued that the ones that were in effect on the date of Panel establishment (effective during 2009) had "expired" and had been "replaced" by "new" measures on 1 January 2010. China refers to the first category of measures as "2009 measures" and the second as "2010 measures".

⁴⁸³Panel Reports, para. 7.6 (referring to China's first written submission to the Panel, para. 52).

⁴⁸⁴Panel Reports, para. 7.6 (referring to China's first written submission to the Panel, paras. 49-51, 56, 62, 64, and 67; China's second written submission to the Panel, section II, entitled "Panel Should Rule on the 2010 Measures To resolve the Disputes, and Should Not Rule on the 2009 Measure" and para. 12, where China states that, "[i]n sum, the prompt and positive resolution of this dispute calls for the Panel to address the 2010 measures, and not the 2009 measures").

⁴⁸⁵Panel Reports, para. 7.7.

⁴⁸⁶Panel Reports, para. 7.7.

⁴⁸⁷Panel Reports, para. 7.22.

complainants considered, however, that "the measures invoked in the context of China's defence under GATT Article XX form part of China's evidence and should be evaluated as evidence, but not as measures *per se*."⁴⁸⁸

245. The Panel observed that the complainants' panel requests refer to "any amendments or extensions; related measures; replacement measures; renewal measures; and implementing measures".⁴⁸⁹ As it had done in the first phase of its preliminary ruling⁴⁹⁰, the Panel decided that its terms of reference were broad enough to encompass "amendments or replacement measures of the 2009 measures challenged by the complainants".⁴⁹¹

246. However, after considering the parties' arguments, the Panel decided to adopt the following approach, which we consider useful to set out in full:

(a) The Panel will make findings on the WTO consistency of original measures included in its terms of reference. In light of the request by the complainants that the Panel not make any findings on any amendments or replacement measures, the Panel will only make findings on 2009 measures and the Panel will not make findings on 2010 measures.

(b) In situations where a 2010 replacement measure appears to correct the WTO inconsistency of the original 2009 measure—in whole or in part (and therefore is considered not to have the same essence, in whole or in part, as the expired measure)—the Panel will decline to make findings or recommendations on the 2010 measure, as it falls outside its terms of reference. However, in order to make a determination on whether the new measure is of the same essence as the expired measure, and hence imbuces the expired measure with ongoing effect or prospective application, the Panel will necessarily have to determine (without making a formal finding) whether the WTO inconsistency is no longer present in the new measure.

(c) Nonetheless, with a view to ensuring that annually renewed measures do not evade review by virtue of their annual nature—and relying on the Appellate Body ruling in *US – Continued Zeroing* where the Appellate Body recognized the possibility for a panel to make a ruling on measures that have a "prospective application and a life potentially stretching into the future"—the Panel will make findings with respect to the series of measures comprised of the relevant framework legislation, the implementing regulation(s), other

⁴⁸⁸Panel Reports, para. 7.7.

⁴⁸⁹Panel Reports, para. 7.15.

⁴⁹⁰Panel's preliminary ruling (first phase), para. 20.

⁴⁹¹Panel Reports, para. 7.20.

applicable laws and the specific measure imposing export duties or export quotas in force at the date of the Panel's establishment.

(d) With respect to recommendations, generally the Panel will not make recommendations on any original measure or on any measure no longer in existence (or part thereof) on 15 December 2010, unless there is clear evidence that the measure has ongoing effect.

(e) In situations where the claim is based on an annual measure, as is the case with measures imposing export duties and with some of the measures relating to export quotas, the Panel will make recommendations with respect to the series of measures comprised of the relevant framework legislation, the implementing regulation(s), other applicable laws and the specific measure imposing export duties or export quotas in force at the date of the Panel's establishment.⁴⁹²

247. We understand the Panel to have set out to make findings on all of the series of measures in effect in 2009, including specific measures setting out export duties and export quotas that had expired during the course of the Panel proceedings. The Panel also clarified that it would not make findings on the specific measures assigning export duty rates and quota levels for 2010 in the light of the request of the complainants not to make findings on such measures. The Panel further specified that it would make findings and recommendations relating to the export quotas and export duties on the basis of "the series of measures comprised of the relevant framework legislation, the implementing regulation(s), other applicable laws and the specific measure imposing export duties or export quotas in force at the date of the Panel's establishment."⁴⁹³ The Panel added that it would not make recommendations on expired measures, unless there was clear evidence that such measures had ongoing effect. The Panel expressed the view that, because the measures operating to impose export duties and export quotas included measures of an annually recurring nature, its approach would ensure that these measures did not "evade review".⁴⁹⁴

B. *China's Appeal*

1. Arguments on Appeal

248. On appeal, China does not dispute that the complainants had the "option" of pursuing claims against the "future life" of the export duties and quotas at issue by challenging the measures

⁴⁹²Panel Reports, para. 7.33.

⁴⁹³Panel Reports, paras. 7.33(c) and 7.33(e).

⁴⁹⁴Panel Reports, para. 7.33(c).

specifying such duty rates and quota levels in 2010.⁴⁹⁵ China adds that it even "encouraged" the complainants to do so.⁴⁹⁶ However, according to China, the complainants decided to exclude those 2010 measures from the dispute, thereby "breaking the chain of measures subject to dispute settlement".⁴⁹⁷ In these circumstances, by making recommendations extending to measures specifying export duty rates and quota amounts for 2010, China claims that the Panel acted inconsistently with its terms of reference under Article 7.1 of the DSU; failed to make an objective assessment of the matter under Article 11 of the DSU; and acted inconsistently with Article 19.1 of the DSU.

249. In response, the United States and Mexico submit that "China has not understood the Panel's recommendations correctly".⁴⁹⁸ In particular, they consider that the Panel did not make recommendations on measures on which it had not made findings and did not make recommendations on the basis of measures that were outside of its terms of reference. Instead, the Panel made findings and recommendations on the series of measures "in force at the date of panel establishment".⁴⁹⁹ According to the United States and Mexico, China's appeal therefore "may be dismissed on this basis alone".⁵⁰⁰ The European Union makes arguments along the same lines, noting that the Panel did not refer explicitly to "2010 'replacement measures'" in its recommendations.⁵⁰¹ The European Union also points out that the Panel did not refer to any such "replacement" measures in its Reports when it identified the measures that composed the "series of measures".⁵⁰²

250. China's appeal regarding the Panel's recommendations rests on the proposition that the Panel made recommendations on a "series of measures" that extends into the future and includes the 2010 measures. That is, China faults the Panel for "making recommendations regarding a so-called 'series of measures' with a prospective life extended through annual replacement measures" that were not before the Panel when it made its recommendations.⁵⁰³ In order to address China's arguments on appeal, we begin by reviewing the nature of the challenge brought by the complainants before the Panel.

⁴⁹⁵ China's appellant's submission, para. 163.

⁴⁹⁶ China's appellant's submission, para. 163.

⁴⁹⁷ China's appellant's submission, para. 165. (emphasis omitted)

⁴⁹⁸ Joint appellees' submission of the United States and Mexico, para. 81.

⁴⁹⁹ Joint appellees' submission of the United States and Mexico, para. 83.

⁵⁰⁰ Joint appellees' submission of the United States and Mexico, para. 83.

⁵⁰¹ European Union's appellee's submission, para. 39.

⁵⁰² European Union's appellee's submission, para. 39.

⁵⁰³ China's appellant's submission, para. 153.

2. Analysis

251. A panel is required, under Article 7 of the DSU, to examine the "matter" referred to the DSB by the complainant in the request for the establishment of a panel, and to make such findings as will assist the DSB in making recommendations. The language in a complainant's panel request is therefore important because "a panel's terms of reference are governed by the request for establishment of a panel".⁵⁰⁴ Article 19.1 of the DSU establishes a link between a panel's finding that "a measure is inconsistent with a covered agreement", and its recommendation that the respondent "bring the measure into conformity". The "measures" that may be the subject of recommendations in Article 19.1 are limited to those measures that are included within a panel's terms of reference.

252. In order to identify the object of the complainants' challenge, we begin with the language used by the complainants in their panel requests.⁵⁰⁵ With respect to export quotas, the complainants claim in Section I of their panel requests that "China subjects the exportation of bauxite, coke, fluorspar, silicon carbide, and zinc to quantitative restrictions such as quotas." The complainants further contend that these restrictions "are reflected in" 25 legal instruments listed in the panel requests, including China's *Foreign Trade Law, Regulation on Import and Export Administration, Export Quota Bidding Measures, 2008 Export Licence Administration Measures, 2008 Export Licensing Working Rules, and Export Quota Bidding Implementation Rules*, which constitute the general legal framework and implementing regulations allowing for the imposition of export quotas, as well as the specific measures that established the export quota amounts and allocation procedures on bauxite, coke, fluorspar, silicon carbide, and zinc for 2009.⁵⁰⁶ Similarly, with respect to export duties, the complainants identified in Section II of their panel requests the object of their challenge as export duties "reflected in" 19 specifically identified legal instruments. These include measures setting out the general legal framework for the imposition of export duties—that is, China's *Customs Law* and the *Regulations on Import and Export Duties*—as well as the specific measure that sets out particular export duty rates for 2009 on bauxite, coke, fluorspar, magnesium, manganese, silicon metal, yellow phosphorous, and zinc—that is, the *2009 Tariff Implementation Program*.

253. The complainants did not use the words "series of measures" to describe the object of their challenge. However, as noted above, they did identify the specific measures that, collectively, compose China's legal system for the imposition of export duties and export quotas in their panel

⁵⁰⁴ Appellate Body Report, *US – Carbon Steel*, para. 124.

⁵⁰⁵ WT/DS394/7, WT/DS395/7, and WT/DS398/6. See Annexes I-III of these Reports.

⁵⁰⁶ Panel Reports, para. 7.17; see also paras. 7.219-7.223.

requests.⁵⁰⁷ Moreover, they contended that the imposition of export duties and export quotas on particular products, through the application of those measures, is contrary to China's WTO obligations.⁵⁰⁸ The complainants further clarified that the Panel should not consider their claims as addressing measures adopted after the establishment of the Panel, and requested that the Panel not "make any findings and recommendations on any of the 2010 measures invoked by China".⁵⁰⁹

254. As the Panel explained, China's legislative system for the imposition of export duties comprises basic framework legislation, an implementing regulation, and specific "annual measures that set the level of duty for specific products".⁵¹⁰ The Panel added that, with respect to export quotas, there is also a basic framework legislation, an implementing regulation, "a set of regulations applicable to the relevant allocation system—direct allocation or quota bidding—and finally a set of measures (of varying duration, from a few months to a year or indefinite) that determine the level of quotas for specific products".⁵¹¹ The Panel did not consider that "individually each of those measures would necessarily be WTO-inconsistent"; rather, the Panel said that, "when they operate in concert to result in WTO-inconsistent [export duties or quotas], it is then that they would become *prima facie* WTO-inconsistent".⁵¹² The Panel added that it is only by examining these "measures as they work in concert that the Panel can reach a final determination on the complainants' export duty" and export quota claims.⁵¹³ In our view, the Panel correctly described the object of the complainants' challenge. Indeed, the complainants' panel requests and subsequent arguments before the Panel reveal that the complainants brought their claims with respect to all the measures through which export duties and quotas were imposed on particular raw materials at the time of the establishment of the Panel in 2009.

255. Based on the foregoing, we do not consider that the Panel erred in setting out to make recommendations on the "series of measures" imposing export duties or export quotas in force at the date of the Panel's establishment.⁵¹⁴ Moreover, in the light of the Panel's express statement that it would make recommendations on measures "in force at the date of the Panel's establishment", and that it would not make findings on the measures imposing specific export duty rates and quota levels

⁵⁰⁷See Panel Reports, paras. 7.17 and footnotes 55 and 56 thereto.

⁵⁰⁸Panel Reports, para. 3.2.

⁵⁰⁹Panel Reports, para. 7.22.

⁵¹⁰Panel Reports, para. 7.17 and footnote 55 thereto. The Panel noted that the complainants' panel requests identify measures comprising China's system for applying export duties. The Panel described this system in further detail in its Reports at paras. 7.59-7.63.

⁵¹¹Panel Reports, para. 7.17 and footnote 56 thereto. The Panel noted that the complainants' panel requests identify measures comprising China's system for applying export quotas. The Panel described this system in further detail in Panel Reports, paras. 7.172-7.201.

⁵¹²Panel Reports, paras. 7.68 and 7.224.

⁵¹³See, for example, Panel Reports, para. 7.68.

⁵¹⁴Panel Reports, para. 7.33(e).

for 2010, we consider that the Panel made no express recommendations regarding measures that were excluded from the Panel's terms of reference by the complainants.

256. The question remains whether the recommendations that the Panel made regarding the series of measures in force in 2009 have consequences for the measures imposing specific export duty rates and quota levels for 2010, or indeed any existing or subsequent measures imposing export duties or quotas on these products.

257. In China's view, because the complainants did not seek findings and recommendations on the specific 2010 measures that replaced the measures imposing export duty rates and quota amounts in effect at the time of the Panel's establishment, no recommendation should have consequences for any 2010 or other "replacement measures". The United States and Mexico respond that they were not required to challenge and obtain findings and recommendations against "replacement measures" in order for "future" measures to fall within the scope of China's implementation obligation if the challenged measures were found to be WTO-inconsistent. China's approach, they submit, "would frustrate the aims of the dispute settlement system"⁵¹⁵ by creating a "moving target", whereby "both Complainants and the Panel would continually have had to recast their arguments and assessment of the legal state of play as it evolved through the proceedings".⁵¹⁶

258. The United States and Mexico also fault China for confusing the distinction between "the basis on which a recommendation is made" and "the application or effect of the recommendation once it is made".⁵¹⁷ They maintain that "the fact that a recommendation may have a temporal application in the future (in the sense of requiring the Member concerned to ensure that it has complied with the recommendation) does not contradict the fact that it is necessarily made on the basis of a finding whose temporal application is in the past".⁵¹⁸

259. In alleging that the Panel erred in making recommendations extending to the measures imposing specific export duty rates and quota amounts in 2010, China appears to assume that a finding that is made with respect to a "series of measures" as it existed at the time the Panel was established cannot have consequences for measures adopted in 2010 or thereafter, through the effect of the recommendation made by the Panel or the Appellate Body after adoption by the DSB. We disagree.

⁵¹⁵Joint appellees' submission of the United States and Mexico, para. 87.

⁵¹⁶Joint appellees' submission of the United States and Mexico, para. 73 (referring to Appellate Body Report, *Chile – Price Band System*, para. 144).

⁵¹⁷Joint appellees' submission of the United States and Mexico, para. 85.

⁵¹⁸Joint appellees' submission of the United States and Mexico, para. 85.

260. Pursuant to Article 19.1 of the DSU, when a panel concludes that a measure is inconsistent with a covered agreement, it shall recommend that the Member concerned bring its measure into conformity with that agreement. While a finding by a panel concerns a measure as it existed at the time the panel was established, a recommendation is prospective in nature in the sense that it has an effect on, or consequences for, a WTO Member's implementation obligations that arise after the adoption of a panel and/or Appellate Body report by the DSB. As the Appellate Body noted in *US – Continued Zeroing*, "it is not uncommon for remedies sought in WTO dispute settlement to have prospective effect, such as a finding against laws or regulations, as such, or a subsidy programme with regularly recurring payments".⁵¹⁹

261. At issue in this case are several groups, or series, of measures—that is, the relevant framework legislation, the implementing regulations, and the specific measures in force at the date the Panel was established imposing export duties or quotas on each raw material. As the Panel noted, these groups of measures operate collectively to impose export duties or export quotas on the raw materials at issue. The object of the complainants' challenge was the legal situation prevailing in 2009, that is, the "series of measures" pursuant to which China imposed export quotas and duties on the raw materials at issue at the time the Panel was established. As the Panel found, such measures include China's *Customs Law* and the *Regulations on Import and Export Duties*, which authorize the imposition of export duties; China's *Foreign Trade Law*, which confers the authority to restrict or prohibit the exportation of goods through export quotas and subjects those goods to an export quota administration; as well as the regulations implementing this framework legislation. In addition to these standing measures, each series of measures also includes the specific measures imposing export duty rates or quota amounts in force at a particular time. These latter measures are, as the Panel found, of varying duration. In a particular year, China may, for example, increase or decrease the amount of export duty imposed on a particular product, or it may even eliminate that duty altogether, while the framework legislation and implementing regulations remain in place.⁵²⁰ Against this background, we do not consider that it was necessary for the complainants to include claims with regard to the specific export duty and quota measures applied in 2010, in addition to those that were in force when the Panel was established in 2009, in order to obtain a recommendation with prospective effect.

⁵¹⁹ Appellate Body Report, *US – Continued Zeroing*, para. 171.

⁵²⁰ The Panel found that such a change occurred, for example, with respect to the export duty rate imposed on yellow phosphorous in 2009. (See Panel Reports, paras. 7.69–7.71)

262. In arguing that the complainants "decided" to exclude the "annual replacement measures" from the dispute, thereby "breaking the chain of measures subject to dispute settlement"⁵²¹, China appears to assume that the complainants were initially challenging annually reviewed export duties and export quotas as separate and independent acts, or as a series of such acts, extending into the future. China characterizes such measures as "a chain of annually renewed measures", and submits that the complainants later "narrowed the scope of the dispute to exclude the annual replacement measures".⁵²² Had the complainants' challenge been lodged against "ongoing conduct", as China alleges, a recommendation would have served the purpose of directing China to discontinue its WTO-inconsistent conduct. However, while the setting of export duty rates and export quotas for a particular year is clearly a distinct action, the complainants' challenge in this case was not to specific annual export duty or quota measures in isolation, or to ongoing conduct consisting of a "chain of annually reviewed measures". Rather, the complainants challenged China's framework legislation, implementing regulations, and the specific measures in force at the date of the Panel's establishment imposing export duties or export quotas on each raw material. As the Panel noted, when these measures "operate in concert to result in WTO-inconsistent [export duties or quotas], it is then that they would become *prima facie* WTO-inconsistent".⁵²³ This being the case, the Panel rightly recommended that China bring its measures into conformity with its WTO obligations, such that the "series of measures" does not operate to bring about a WTO-inconsistent result. The fact that the Panel directed its findings and recommendations at the legal situation prevailing in 2009 does not mean that China has no compliance obligations with respect to the Panel's findings.⁵²⁴

263. We note that, in making its recommendations, the Panel was concerned about making recommendations on what it viewed to be "expired" measures.⁵²⁵ The Panel noted, for example, that previous panels had found that it would not be appropriate to make recommendations on measures

⁵²¹ China's appellant's submission, para. 165. (emphasis omitted)

⁵²² China's appellant's submission, para. 165.

⁵²³ Panel Reports, paras. 7.68 and 7.224.

⁵²⁴ As a separate matter, we note that the Panel expressed the view that "the WTO consistency of a measure is necessarily relevant to its 'essence'" in the context of WTO dispute settlement procedures. (Panel Reports, para. 7.17) The Panel added that, "[i]f a new measure appears to be WTO consistent, while the original was not, the new measure takes on a different character in the context of WTO dispute settlement and cannot be said to be of the 'same essence'." (*Ibid.*) We fail to see why the "apparent" consistency, or inconsistency, of a measure would necessarily have a bearing on the issue of whether it would be deemed to be of the "same essence" as the original measure. For example, the fact that one measure imposes a lesser export duty rate than another measure might mean that the former is consistent while the latter is inconsistent with a WTO Member's obligations under Article II of the GATT 1994. It is not clear, however, why this fact, taken alone, would necessarily mean that the two measures are not of the "same essence".
⁵²⁵ Panel Reports, para. 7.33(b) and (d).

that no longer exist.⁵²⁶ The DSU does not specifically address whether a WTO panel may or may not make findings and recommendations with respect to a measure that expires or is repealed during the course of the panel proceedings. Panels have made findings on expired measures in some cases and declined to do so in others, depending on the particularities of the disputes before them.⁵²⁷ In the present dispute, China takes issue with the recommendations made by the Panel, and not with its findings on particular measures. In *US – Upland Cotton*, the Appellate Body drew a distinction between the question of whether a panel can make findings with respect to an expired measure and the question of whether an expired measure is susceptible to a recommendation under Article 19.1 of the DSU:

The Appellate Body in *US – Certain EC Products* confirmed that the 3 March Measure had ceased to exist. It noted that there was an obvious inconsistency between the finding of the panel that "the 3 March Measure is no longer in existence" and the panel's subsequent recommendation that the Dispute Settlement Body (the "DSB") request the United States to bring the 3 March Measure into conformity with its WTO obligations. Thus, the fact that a measure has expired may affect what recommendation a panel may make. It is not, however, dispositive of the preliminary question of whether a panel can address claims in respect of that measure.⁵²⁸ (footnote omitted)

264. Contrary to the Panel's approach in this dispute, the Appellate Body indicated that the fact that a measure has expired "may affect" what recommendation a panel may make. The Appellate Body did not suggest that a panel was precluded from making a recommendation on such a measure in a particular case. In general, in cases where the measure at issue consists of a law or regulation that has been repealed during the panel proceedings, it would seem there would be no need for a panel to make a recommendation in order to resolve the dispute. The same considerations do not apply, in our view, when a challenge is brought against a group or "series of measures" comprised of basic framework legislation and implementing regulations, which have not expired, and specific measures imposing export duty rates or export quota amounts for particular products on an annual or time-bound basis, as is the case here. The absence of a recommendation in such a case would effectively mean that a finding of inconsistency involving such measures would not result in implementation

⁵²⁶Panel Reports, para. 7.28 (referring to Panel Reports, *EC – Trademarks and Geographic Indications*, para. 7.14; and Panel Report, *US – Poultry (China)*, para. 7.56).

⁵²⁷See, for instance, Panel Report, *US – Wool Shirts and Blouses*, para. 6.2; Panel Report, *Indonesia – Autos*, para. 14.9; Panel Report, *Chile – Price Band System*, para. 7.126; Panel Report, *Dominican Republic – Imports and Sale of Cigarettes*, para. 7.344; and Panel Report, *EC – Approval and Marketing of Biotech Products*, paras. 7.1303-7.1312.

⁵²⁸Appellate Body Report, *US – Upland Cotton*, para. 271.

obligations for a responding member, and in that sense would merely be declaratory.⁵²⁹ This cannot be the case.

265. Article 3.7 of the DSU provides that "[t]he aim of the dispute settlement mechanism is to secure a positive solution to a dispute." This is affirmed in Article 3.4 of the DSU, which stipulates that "[r]ecommendations or rulings made by the DSB shall be aimed at achieving a satisfactory settlement of the matter in accordance with the rights and obligations under this Understanding and under the covered agreements." In our view, in order to "secure a positive solution to the dispute" and to make "sufficiently precise recommendations and rulings so as to allow for prompt compliance"⁵³⁰, it was appropriate for the Panel in this case to have recommended that the DSB request China "to bring its measures into conformity with its WTO obligations such that the 'series of measures' does not operate to bring about a WTO-inconsistent result".⁵³¹

3. Conclusion

266. We do not consider that the Panel erred in recommending that the DSB request China "to bring its measures into conformity with its WTO obligations such that the 'series of measures' does not operate to bring about a WTO-inconsistent result".⁵³² Nor do we consider the Panel to have made a recommendation on a matter that was not before it. Accordingly, we do not agree with China that the Panel acted inconsistently with its obligations under Article 7.1 of the DSU. China's claims under Article 11 and Article 19.1 of the DSU are consequential in nature and depend on whether we find that the Panel correctly understood the object of the complainants' challenge, that is, the "matter" on which the Panel was required to make its findings. In the light of our view that the Panel did not make findings on a matter that was not before it, we dismiss these claims by China. In sum, therefore, we *find* that the Panel did not err in recommending, in paragraphs 8.8, 8.15, and 8.22 of the Panel Reports, that China bring its export duty and export quota measures into conformity with its WTO obligations.

⁵²⁹In fact, China argued at the oral hearing that, because the complainants brought an "as applied" claim regarding the application of measures in 2009, and because they expressly excluded "replacement measures" from the Panel's terms of reference, all the export duty and quota measures within the Panel's terms of reference have since expired. In China's view, a recommendation cannot be made with respect to an expired measure, nor with respect to a measure that is outside the Panel's terms of reference.

⁵³⁰Appellate Body Report, *Australia – Salmon*, para. 223.

⁵³¹Panel Reports, paras. 8.8, 8.15, and 8.22.

⁵³²Panel Reports, paras. 8.8, 8.15, and 8.22. The Panel made the same recommendation with respect to each of the complainants.

obligations such that the "series of measures" do not operate to bring about a WTO-inconsistent result.⁵³³

C. *Conditional Other Appeals of the United States, Mexico, and the European Union*

267. In their other appeals, the United States and Mexico refer to the possibility that the Appellate Body might reverse the Panel's recommendations in paragraphs 8.8, 8.15, and 8.22 of the Panel Reports "to the extent that they apply to replacement measures", and find that no recommendation should have been made on the "series of measures" as they existed on the date of Panel establishment.⁵³⁴ In the event that the Appellate Body were to so find, the United States and Mexico would seek review of the Panel's interpretation and conclusion that it could not make recommendations on the 2009 export quota and export duty measures that were annually recurring and in effect as of the date of Panel establishment.

268. The European Union also submits a conditional appeal in the event the Appellate Body were to accept the relevant ground of appeal raised by China, and also reject the relevant other appeals submitted by the United States and Mexico. In that case, the European Union would argue that the Panel erred in finding that, during the course of the Panel proceedings, the European Union "requested the Panel not to make any findings and recommendations on the legal instruments taking effect on 1 January 2010" and thereby narrowed the Panel's terms of reference.⁵³⁵

269. As the condition on which the United States and Mexico's request is premised has not been met, there is no need for us to address the United States' and Mexico's conditional appeal. For the same reason, we do not address the European Union's conditional appeal.

VI. Applicability of Article XX

270. In this section, we address China's claim that Article XX of the GATT 1994 is available as a defence to China in relation to export duties found to be inconsistent with China's obligations under Paragraph 11.3 of China's Accession Protocol.

⁵³³Panel Reports, paras. 8.8, 8.15, and 8.22. The Panel made the same recommendation with respect to each of the complainants.

⁵³⁴United States' other appellant's submission, para. 8; Mexico's other appellant's submission, para. 16.

⁵³⁵European Union's other appellant's submission, para. 3 (referring to Panel Reports, paras. 7.21 and 7.22).

A. *The Panel's Findings*

271. The Panel began its interpretation of Paragraph 11.3 of China's Accession Protocol by observing that Paragraph 11.3 "does not include any express reference to Article XX of the GATT 1994, or to provisions of the GATT 1994 more generally".⁵³⁶ In so doing, the Panel drew a contrast between the text of Paragraph 11.3 and the language contained in Paragraph 5.1 of China's Accession Protocol—"without prejudice to China's right to regulate trade in a manner consistent with the WTO Agreement"—which the Appellate Body examined in *China – Publications and Audiovisual Products*.⁵³⁷ In particular, the Panel noted that Paragraph 11.3 contains only a "specific set of exceptions: those covered by Annex 6 and those covered by GATT Article VIII".⁵³⁸ For the Panel, the language in Paragraph 11.3, together with the "omission of general references to the WTO Agreement or to the GATT 1994"⁵³⁹, suggest that WTO Members did not intend to incorporate the defences available under Article XX into Paragraph 11.3.⁵⁴⁰ The Panel also found no support in the provisions of China's Accession Working Party Report for the proposition that China could invoke Article XX of the GATT 1994 to justify violations of Paragraph 11.3 of China's Accession Protocol.

272. Regarding the context provided by the provisions of the other WTO agreements, the Panel noted that there are no general exceptions in the *WTO Agreement*, and that each of the covered agreements provides its own "set of exceptions or flexibilities" applicable to the specific commitments in each agreement.⁵⁴¹ Referring to Article XX of the GATT 1994, the Panel considered that the reference to "this Agreement" *a priori* suggests that the exceptions therein relate only to the GATT 1994.⁵⁴² Noting that, in several instances, provisions of Article XX have been incorporated into other WTO agreements by cross-reference, the Panel observed that, since no such language is found in Paragraph 11.3 of China's Accession Protocol, Article XX could not be intended to apply to Paragraph 11.3. Furthermore, whereas the Panel agreed that WTO Members have an "inherent right"

⁵³⁶Panel Reports, para. 7.124.

⁵³⁷Paragraph 5.1 of China's Accession Protocol provides:

Without prejudice to China's right to regulate trade in a manner consistent with the WTO Agreement, China shall progressively liberalize the availability and scope of the right to trade, so that, within three years after accession, all enterprises in China shall have the right to trade in all goods throughout the customs territory of China, except for those goods listed in Annex 2A which continue to be subject to state trading in accordance with this Protocol.

⁵³⁸Panel Reports, para. 7.126.

⁵³⁹Panel Reports, para. 7.129.

⁵⁴⁰Panel Reports, paras. 7.126-7.129.

⁵⁴¹Panel Reports, para. 7.150.

⁵⁴²Panel Reports, para. 7.153.

to regulate trade, the Panel considered that China had exercised this right in negotiating and ratifying the *WTO Agreement*, including the terms of its accession to the WTO.⁵⁴³ On this basis, the Panel concluded that the defences of Article XX of the GATT 1994 are not available to justify violations of the obligations contained in Paragraph 11.3 of China's Accession Protocol.⁵⁴⁴

B. *Arguments on Appeal*

273. China alleges various errors in the Panel's analysis and requests the Appellate Body to reverse the Panel's finding that China may not seek to justify export duties pursuant to Article XX of the GATT 1994 that were found to be inconsistent with its commitment to eliminate export duties under Paragraph 11.3 of its Accession Protocol.⁵⁴⁵ China further requests us to find that Article XX is available to China to justify such measures.

274. China contends, in particular, that the Panel erred in determining that there is "no textual basis" in China's Accession Protocol for it to invoke Article XX in defence of a claim under Paragraph 11.3.⁵⁴⁶ In China's view, the Panel's finding that Paragraph 11.3 excludes recourse to Article XX of the GATT 1994 was based on the Panel's erroneous assumption that the absence of language expressly granting the right to regulate trade in a manner consistent with Article XX means that China and other Members intended to deprive China of that right. Moreover, China argues that WTO Members have an "inherent right" to regulate trade, "including using export duties to promote non-trade interests".⁵⁴⁷

275. Although China takes issue with the Panel's finding that Article XX is not available to China to justify measures that would otherwise be inconsistent with its commitment to eliminate export duties under Paragraph 11.3 of its Accession Protocol, it does not request the Appellate Body to reverse the Panel's finding that China failed to demonstrate that the export duties at issue in this dispute are justified under Article XX of the GATT 1994.

276. The United States, the European Union, and Mexico support the Panel's finding that Article XX of the GATT 1994 cannot be invoked to justify export duties that are inconsistent with Paragraph 11.3 of China's Accession Protocol. The United States and Mexico recall that, in *China –*

⁵⁴³Panel Reports, para. 7.156.

⁵⁴⁴Panel Reports, para. 7.158.

⁵⁴⁵China's appellant's submission, para. 168 (referring to Panel Reports, paras. 7.158, 7.159, 8.2(b)-(c), 8.9(b)-(c), and 8.16(b)-(c)).

⁵⁴⁶China's appellant's submission, para. 190.

⁵⁴⁷China's appellant's submission, para. 208.

Publications and Audiovisual Products, the Appellate Body interpreted the language of Paragraph 5.1 of China's Accession Protocol as including a reference to Article XX. They note, however, that the language of Paragraph 11.3 is "in sharp contrast" to that of Paragraph 5.1, as it is "specific and circumscribed", "sets forth particular commitments", and two exceptions to those commitments. According to the European Union, while WTO Members can "incorporate" Article XX of the GATT 1994 into another WTO agreement if they so "wish", the legal basis for "applying" that provision to another agreement would be the "very text of the incorporation", and not Article XX itself, as Article XX is limited by its "express terms" to the GATT 1994.⁵⁴⁸ The European Union also asserts that the Panel was correct in finding that China had exercised its inherent and sovereign right to regulate trade by negotiating the terms of its accession to the WTO such that this inherent right to regulate trade, without more, does not permit recourse to Article XX.

277. Canada, Colombia, Japan, Korea, and Turkey generally agree with the complainants that Article XX of the GATT 1994 cannot be invoked in order to justify a violation of China's export duty commitments contained in Paragraph 11.3 of China's Accession Protocol.⁵⁴⁹

C. *Availability of Article XX to Justify Export Duties that Are Found to Be Inconsistent with Paragraph 11.3 of China's Accession Protocol*

278. Paragraph 1.2 of China's Accession Protocol provides that the Protocol "shall be an integral part" of the *WTO Agreement*. As such, the customary rules of interpretation of public international law, as codified in Articles 31 and 32 of the *Vienna Convention on the Law of Treaties*⁵⁵⁰ (the "*Vienna Convention*"), are, pursuant to Article 3.2 of the DSU, applicable in this dispute in clarifying the meaning of Paragraph 11.3 of the Protocol.⁵⁵¹ Article 31(1) of the *Vienna Convention* provides that a "treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose." Therefore, we will begin our analysis with the text of Paragraph 11.3.

⁵⁴⁸European Union's appellee's submission, para. 54.

⁵⁴⁹See Canada's third participant's submission, paras. 14-24; Colombia's third participant's submission, paras. 11 and 12; and Japan's third participant's submission, paras. 26-30, 34-37, and 39-42. For its part, Korea considers that the "gravity" and importance of an Article XX defence suggests that "[n]lore explicit wording should have been used to express the 'relinquishment' of such an 'important right'. Nonetheless, in Korea's view, the difference in 'tone and nuance' between Paragraph 11.3 and Paragraphs 11.1 and 11.2 of China's Accession Protocol, as well as the context of the other provisions of Section 11, support the Panel's ultimate conclusion in the present disputes and should be upheld by the Appellate Body. (Korea's third participant's submission, paras. 32 and 33)

⁵⁵⁰Done at Vienna, 23 May 1969, 1155 UNTS 331; 8 International Legal Materials 679.

⁵⁵¹See Appellate Body Report, *US – Gasoline*, p. 17, DSR 1996:1, 3, at 16; and Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 10, DSR 1996:1, 97, at 104.

1. Paragraph 11.3 of China's Accession Protocol

279. Paragraph 11.3 of China's Accession Protocol provides that:

China shall eliminate all taxes and charges applied to exports unless specifically provided for in Annex 6 of this Protocol or applied in conformity with the provisions of Article VIII of the GATT 1994.

280. By its terms, Paragraph 11.3 of China's Accession Protocol requires China to "eliminate all taxes and charges applied to exports" unless one of the following conditions is satisfied: (i) such taxes and charges are "specifically provided for in Annex 6 of [China's Accession] Protocol"; or (ii) such taxes and charges are "applied in conformity with the provisions of Article VIII of the GATT 1994".

281. As noted, Paragraph 11.3 of China's Accession Protocol refers explicitly to "Annex 6 of this Protocol". Annex 6 of China's Accession Protocol is entitled "Products Subject to Export Duty". It sets out a table listing 84 different products (each identified by an eight-digit Harmonized System ("HS") number and product description), and a maximum export duty rate for each product.⁵⁵² Following the table, Annex 6 includes the following text (the "Note to Annex 6"):

China confirmed that the tariff levels in this Annex are maximum levels which will not be exceeded. China confirmed furthermore that it would not increase the presently applied rates, except under exceptional circumstances. If such circumstances occurred, China would consult with affected members prior to increasing applied tariffs with a view to finding a mutually acceptable solution.

282. Except for yellow phosphorus, none of the raw materials at issue in this dispute is listed in Annex 6 of China's Accession Protocol.⁵⁵³ China argues that the use of the term "exceptional circumstances" in the Note to Annex 6 indicates "a substantive overlap between the scope of the exceptions set forth, respectively, in Annex 6 and Article XX of the GATT 1994".⁵⁵⁴ In China's view, "by allowing China to adopt otherwise WTO-inconsistent export duties in 'exceptional circumstances', China and other WTO Members have demonstrated a shared intent that China is permitted to have recourse—whether directly or indirectly—to the 'exceptional circumstances' set forth in Article XX to

⁵⁵²Panel Reports, para. 7.66.

⁵⁵³The Panel found that, on 21 December 2009, yellow phosphorus was subject to an export duty of 20 per cent, which did not exceed the maximum rate listed in Annex 6 of China's Accession Protocol. The Panel found, therefore, that the provision of the 2009 *Tariff Implementation Program* applicable to yellow phosphorus that was in force at the time of the Panel's establishment was not inconsistent with China's WTO obligations. (See Panel Reports, para. 7.71) This finding by the Panel has not been challenged on appeal.

⁵⁵⁴China's appellant's submission, para. 2.16.

justify such duties."⁵⁵⁵ China suggests that such "exceptional circumstances" can be invoked both to exceed the maximum rates specified in Annex 6 for the 84 products listed in the Annex, and to impose export duties on non-listed products.

283. In response, the United States and Mexico assert that the first sentence of the Note "makes clear" that China committed not to impose export duties on the 84 products listed in Annex 6 above the maximum rates set out therein.⁵⁵⁶ In their view, the second and third sentences of the Note also impose a further obligation upon China that, in the event that the applied rate for any of the 84 products listed in Annex 6 is less than the maximum rate, China can raise the applied rate only in "exceptional circumstances", and only after consulting with the affected Members. In the light of this additional obligation, the United States and Mexico consider that the Note to Annex 6 does not provide "any basis" for China to impose export duties on the 84 listed products above the maximum rates specified in Annex 6, or "to impose any export duties at all with respect to the products not listed in Annex 6".⁵⁵⁷

284. Paragraph 11.3 requires China to eliminate taxes and charges applied to exports unless such taxes and charges are "specifically provided for in Annex 6" of China's Accession Protocol. Annex 6 in turn "specifically provides for" maximum export duty levels on 84 listed products. The Note to Annex 6 clarifies that the maximum rates set out in Annex 6 "will not be exceeded" and that China will "not increase the presently applied rates, except under exceptional circumstances". The Note therefore indicates that China may increase the "presently applied rates" on the 84 products listed in Annex 6 to levels that remain within the maximum levels listed in the Annex. We find it difficult to see how this language could be read as indicating that China can have recourse to the provisions of Article XX of the GATT 1994 in order to justify imposition of export duties on products that are *not* listed in Annex 6 or the imposition of export duties on listed products in excess of the maximum levels set forth in Annex 6.

285. We further note that the third sentence of the Note to Annex 6 refers to the "exceptional circumstances" described in the second sentence of that provision, stating that, "[i]f such circumstances occurred, China would consult with affected members prior to increasing applied tariffs with a view to finding a mutually acceptable solution." This language further supports our view that the "exceptional circumstances" referred to in the Note to Annex 6 are ones that, if shown to exist,

⁵⁵⁵China's appellant's submission, para. 220.

⁵⁵⁶Joint appellees' submission of the United States and Mexico, para. 113.

⁵⁵⁷Joint appellees' submission of the United States and Mexico, para. 113; see also Canada's third participant's submission, paras. 14 and 15.

would allow China to increase applied tariffs up to the maximum tariff levels set out in Annex 6 for the products listed. We therefore see nothing in the Note to Annex 6 suggesting that China could invoke Article XX of the GATT 1994 to justify the imposition of export duties that China had committed to eliminate under Paragraph 11.3 of China's Accession Protocol.⁵⁵⁸

286. China recalls that, before the Panel, the European Union claimed that China violated its obligations under Annex 6 by failing to consult with affected Members prior to the imposition of export duties on particular forms of bauxite, coke, fluorspar, magnesium, manganese, silicon metal, and zinc, none of which are among the 84 products listed in Annex 6.⁵⁵⁹ Noting the Panel's finding that China has acted inconsistently with its obligations under Annex 6 because it failed to consult with other affected WTO Members prior to imposing export duties on the raw materials at issue⁵⁶⁰, China argues that, because none of the products subject to the European Union's claim is included in the Annex 6 schedule, the European Union's claim and the Panel's finding necessarily mean that "the exception in Annex 6 permits China to impose export duties on all products, provided that there are 'exceptional circumstances', and that China consults with the affected Members."⁵⁶¹

287. In our view, the use of the word "furthermore" in the second sentence of the Note to Annex 6 suggests that the obligations contained in the second and third sentences of the Note, including the consultation obligation, are "in addition" to China's obligation under the first sentence not to exceed the maximum tariff levels provided for in Annex 6. We see nothing in the Note to Annex 6 that would allow China to: (i) impose export duties on products not listed in Annex 6; or (ii) increase the applied export duties on the 84 products listed in Annex 6, in a situation where "exceptional circumstances" have not "occurred". We therefore disagree with the Panel to the extent it found that China's failure to consult with other WTO affected Members prior to the imposition of export duties on raw materials not listed in Annex 6 is inconsistent with its obligations under Annex 6.⁵⁶² The imposition of these export duties is inconsistent with Paragraph 11.3 of China's Accession Protocol, and because the raw materials at issue are not listed in Annex 6, the consultation requirements contained in the Note to Annex 6 are not applicable.

⁵⁵⁸Furthermore, as the European Union notes, the Note to Annex 6 resembles to some extent the situation envisaged in Article XXVIII of the GATT 1994 and Article XXI of the GATS (Modification of Schedules), which deal with changes in tariff bindings and changes in the Services Schedules of Specific Commitments. However in these situations, WTO Members are required to "compensate" by offering increased market access in other areas on different tariff lines or service sectors. (European Union's appellee's submission, para. 68)

⁵⁵⁹China's appellant's submission, para. 213.

⁵⁶⁰China's appellant's submission, para. 214 (referring to Panel Reports, para. 7.104).

⁵⁶¹China's appellant's submission, para. 215.

⁵⁶²See Panel Reports, para. 7.104. We note that this finding by the Panel has not been appealed.

288. We turn next to examine the relevance of the reference to Article VIII of the GATT 1994 in Paragraph 11.3 of China's Accession Protocol. Article VIII provides, in relevant part, as follows:

All fees and charges of whatever character (other than import and export duties and other than taxes within the purview of Article III) imposed by contracting parties on or in connection with importation or exportation shall be limited in amount to the approximate cost of services rendered and shall not represent an indirect protection to domestic products or a taxation of imports or exports for fiscal purposes.

289. China asserts that the reference to Article VIII in Paragraph 11.3 confirms the availability of Article XX of the GATT 1994. China reasons that Paragraph 11.3 of its Accession Protocol "requires" that export taxes and charges be "applied in conformity with the provisions of Article VIII of the GATT 1994".⁵⁶³ According to China, "[i]f they are not, the measure violates both Paragraph 11.3 and Article VIII."⁵⁶⁴ China argues that, "[i]n the event that a measure violates Article VIII of the GATT 1994, it may, of course, be justified under Article XX of the GATT 1994".⁵⁶⁵ It follows that "China is not deprived of its right to justify a measure that violates Article VIII through recourse to Article XX simply because a complainant chooses to bring a claim under Paragraph 11.3" of China's Accession Protocol.⁵⁶⁶ In China's view, the fact that Article VIII applies to certain export charges and fees covered by Paragraph 11.3, and not to export duties, does not render the reference to Article VIII "irrelevant", as the reference shows that the obligations under Paragraph 11.3 are "not absolute and unqualified", and that China did not agree to abandon its right to resort to Article XX.⁵⁶⁷

290. Although Article VIII covers "[a]ll fees and charges of whatever character imposed by [WTO Members] on or in connection with importation or exportation", it expressly excludes export duties, which are at issue here. In our view, as export duties are outside the scope of Article VIII, the question of conformity or consistency with this Article does not arise. Consequently, the fact that Article XX may be invoked to justify those fees and charges regulated under Article VIII does not mean that it can also be invoked to justify export duties, which are not regulated under Article VIII.

⁵⁶³China's appellant's submission, para. 224.

⁵⁶⁴China's appellant's submission, para. 224.

⁵⁶⁵China's appellant's submission, para. 224.

⁵⁶⁶China's appellant's submission, para. 225.

⁵⁶⁷China's appellant's submission, para. 226.

291. As noted by the Panel, "the language in Paragraph 11.3 expressly refers to Article VIII, but leaves out reference to other provisions of the GATT 1994, such as Article XX."⁵⁶⁸ Moreover, there is no language in Paragraph 11.3 similar to that found in Paragraph 5.1 of China's Accession Protocol—"[w]ithout prejudice to China's right to regulate trade in a manner consistent with the WTO Agreement"—which was interpreted by the Appellate Body in *China – Publications and Audiovisual Products*. In our view, this suggests that China may not have recourse to Article XX to justify a breach of its commitment to eliminate export duties under Paragraph 11.3 of China's Accession Protocol.

292. Having examined the text of Paragraph 11.3, we turn to examine the context of that provision.

2. Paragraphs 11.1 and 11.2 of China's Accession Protocol

293. Paragraph 11.1 of China's Accession Protocol provides that "China shall ensure that customs fees or charges applied or administered by national or sub-national authorities, shall be in conformity with the GATT 1994". Paragraph 11.2 further stipulates that "China shall ensure that internal taxes and charges, including value-added taxes, applied or administered by national or sub-national authorities shall be in conformity with the GATT 1994." Both of these provisions contain the obligation to ensure that certain fees, taxes or charges are "in conformity with the GATT 1994". This is not the case for Paragraph 11.3. We also note that Paragraph 11.1 refers to "customs fees and or charges" in general and Paragraph 11.2 refers in turn to "internal taxes and charges", while Paragraph 11.3 refers specifically to the elimination of "taxes and charges applied to exports". Given the references to the GATT 1994 in Paragraphs 11.1 and 11.2, and the differences in the subject matter and nature of the obligations covered by these provisions, we consider that the absence of a reference to the GATT 1994 in Paragraph 11.3 further supports our interpretation that China may not have recourse to Article XX to justify a breach of its commitment to eliminate export duties under Paragraph 11.3. Moreover, as China's obligation to eliminate export duties arises exclusively from China's Accession Protocol, and not from the GATT 1994, we consider it reasonable to assume that, had there been a common intention to provide access to Article XX of the GATT 1994 in this respect, language to that effect would have been included in Paragraph 11.3 or elsewhere in China's Accession Protocol.

3. China's Arguments concerning Paragraph 170

294. China relies on the wording of Paragraph 170 of China's Accession Working Party Report to support its position that China assumed a "qualified" obligation to eliminate export duties, and is entitled to have recourse to the provisions of Article XX of the GATT 1994 to justify export duties that would otherwise be inconsistent with Paragraph 11.3 of China's Accession Protocol.

295. Paragraph 170 of China's Accession Working Party Report is referenced in Paragraph 342 of China's Accession Working Party Report and is therefore, by virtue of Paragraph 1.2 of China's Accession Protocol, incorporated into the Protocol. Paragraph 170 falls under subsection D of China's Accession Working Party Report, which is entitled "Internal Policies Affecting Foreign Trade in Goods"; subsection D(1) is entitled "Taxes and Charges Levied on Imports and Exports". Paragraph 170 provides in relevant part:

The representative of China confirmed that upon accession, China would ensure that its laws and regulations relating to all fees, charges or taxes levied on imports and exports would be in full conformity with its WTO obligations, including Articles I, III:2 and 4, and XI:1 of the GATT 1994[.]

296. China points to the identical language in the title of the subsection under which Paragraph 170 falls, and that of Section 11 of China's Accession Protocol. Both are entitled "Taxes and Charges Levied on Imports and Exports". China argues that this demonstrates a "very considerable overlap" in the scope of measures to which Paragraph 11.3 and Paragraph 170 apply, and that they impose "cumulative obligations" with respect to "taxes" and "charges on exports".⁵⁶⁹ China argues, in essence, that Paragraph 170 of China's Accession Working Party Report and Paragraph 11.3 of China's Accession Protocol both apply to export duties, and that "any flexibilities that Paragraph 170 affords to China to adopt otherwise WTO-inconsistent export 'taxes' and 'charges' must extend equally to Paragraph 11.3".⁵⁷⁰

297. The United States and Mexico consider China's arguments to be "without merit".⁵⁷¹ They submit that Paragraph 169 of China's Accession Working Party Report shows that some Members were concerned about China's internal policies, especially those of sub-national governments imposing discriminatory taxes and other charges that would affect trade in goods, and that China responded to this concern in Paragraph 170 by confirming that its laws relating to all fees, charges, or

⁵⁶⁹China's appellant's submission, para. 233. (original emphasis)

⁵⁷⁰China's appellant's submission, para. 246.

⁵⁷¹Joint appellees' submission of the United States and Mexico, para. 128.

⁵⁶⁸Panel Reports, para. 7.129.

taxes levied on imports and exports would be in full conformity with its WTO obligations. The United States and Mexico argue that it is "untenable to believe"⁵⁷² that Paragraph 170 reflects the negotiators' intent to apply Article XX of the GATT 1994 to Paragraph 11.3 of China's Accession Protocol, which sets forth a "new commitment with respect to export duties and the exceptions applicable to that commitment".⁵⁷³ They further point out that it is Paragraph 155 of China's Accession Working Party Report that reflects concerns with respect to export duties, and which refers to the same specific exceptions as Paragraph 11.3 of China's Accession Protocol.⁵⁷⁴

298. We note that China's Accession Working Party Report sets out many of the concerns raised and obligations undertaken by China during its accession process. The various paragraphs contained in China's Accession Working Party Report are organized according to subject matter, such that the section on "Policies Affecting Trade in Goods" is divided into subsections dealing with "Trading Rights", "Import Regulation", "Export Regulations", and "Internal Policies Affecting Trade in Goods". Paragraph 170 of China's Accession Working Party Report falls under subsection D, entitled "Internal Policies Affecting Foreign Trade in Goods". This subsection contains only two paragraphs. Paragraph 169 indicates that some members of China's Accession Working Party "expressed concern about the application of the [value-added tax ("VAT")] and additional charges levied by sub-national governments on imports" and considered "[n]on-discriminatory application of the VAT and other internal taxes"⁵⁷⁵ to be "essential". The language in the title to subsection D and in Paragraph 169 suggests to us that Paragraph 170 is concerned with "internal policies" affecting "all fees, charges or taxes levied on imports and exports" and sets out China's commitment in response to the concern expressed by WTO Members at the time of China's accession regarding "the application of VAT and additional charges levied by sub-national governments on imports".

299. As we see it, Paragraph 170 of China's Accession Working Party Report is of limited relevance in interpreting Paragraph 11.3 of China's Accession Protocol. In particular, Paragraph 170 does not shed much light on China's commitment to eliminate export duties. Instead, it is Paragraphs 155 and 156 of China's Accession Working Party Report⁵⁷⁶, found in the section entitled "Export Regulations", that deal with China's commitments with respect to the elimination of export

⁵⁷²Joint appellees' submission of the United States and Mexico, para. 130.

⁵⁷³Joint appellees' submission of the United States and Mexico, para. 132.

⁵⁷⁴Joint appellees' submission of the United States and Mexico, para. 134 (referring to Panel Reports, para. 7.145).

⁵⁷⁵Emphasis added.

⁵⁷⁶Paragraphs 155 and 156 are not referenced in Paragraph 342 of China's Accession Working Party Report. Nonetheless, we agree with the Panel that they are of interpretative relevance in that they articulate the concerns of WTO Members at the time with respect to China's use of export duties.

duties. The language of Paragraph 155 is very similar to that found in Paragraph 11.3 of China's Accession Protocol, and provides that taxes and charges applied exclusively to exports "should be eliminated unless applied in conformity with GATT Article VIII or listed in Annex 6 to the Draft Protocol". Paragraph 156, in turn, provides: "China noted that the majority of products were free of export duty, although 84 items ... were subject to export duties". As in the case of Paragraph 11.3, Paragraphs 155 and 156 make no reference to the availability of an Article XX defence for the commitments contained therein. This further supports our interpretation that China does not have recourse to Article XX of the GATT 1994 to justify export duties found to be inconsistent with China's obligations under Paragraph 11.3 of China's Accession Protocol.

4. China's Right to Regulate Trade

300. China argues that, "like any other state", it enjoys the right to regulate trade in a manner that promotes conservation and public health.⁵⁷⁷ Referring to the Appellate Body report in *China – Publications and Audiovisual Products*, China points out that such a right to regulate trade is an "inherent right", and "not a 'right bestowed by international treaties such as the *WTO Agreement*'".⁵⁷⁸ According to China, by acceding to the WTO, Members agree to exercise their inherent right in conformity with disciplines set out in the covered agreements, either by complying with affirmative obligations, or by complying with "the obligations attaching to an exception, such as those included in Article XX" of the GATT 1994.⁵⁷⁹ China further emphasizes that China's Accession Protocol and Accession Working Party Report contain no language showing that China "abandon[ed]" its inherent right to regulate trade. Instead, China submits that its accession commitments "indicate" that it retains this right.⁵⁸⁰ In China's view, the Panel's interpretation of Paragraph 11.3 "turns *inherent* rights into *acquired* rights"⁵⁸¹ and "distorts the balance of rights and obligations" established when China acceded to the WTO.⁵⁸²

301. The United States and Mexico begin by highlighting that, contrary to China's claims, the Panel "nowhere suggested" that WTO Members abandoned their right to regulate trade in entering the WTO.⁵⁸³ They assert that the Appellate Body report in *China – Publications and Audiovisual*

⁵⁷⁷China's appellant's submission, para. 275.

⁵⁷⁸China's appellant's submission, para. 275 (quoting Appellate Body Report, *China – Publications and Audiovisual Products*, para. 222).

⁵⁷⁹China's appellant's submission, para. 278.

⁵⁸⁰China's appellant's submission, para. 286.

⁵⁸¹China's appellant's submission, para. 291. (original emphasis)

⁵⁸²China's appellant's submission, para. 274, subheading IV.C.5.d.

⁵⁸³Joint appellees' submission of the United States and Mexico, para. 140.

Products recognized that, because WTO Members have an inherent right to regulate trade, it was necessary in the context of the WTO agreements to agree on rules that constrain that right.⁵⁸⁴ The United States and Mexico also rely upon the Appellate Body report in *Japan – Alcoholic Beverages II* to argue that China's obligation to eliminate export duties contained in Paragraph 11.3 of China's Accession Protocol is a "commitment" that conditions the exercise of China's sovereignty in exchange for the benefits it derives as a Member of the WTO.⁵⁸⁵ Referring to China's contention that it is entitled to invoke Article XX exceptions for violations of Paragraph 11.3 of China's Accession Protocol in the absence of "specific treaty language", the United States and Mexico assert that this would render the introductory clause in Paragraph 5.1, and the references to the GATT 1994 in Paragraphs 11.1 and 11.2 of China's Accession Protocol, "superfluous".⁵⁸⁶ The United States and Mexico emphasize that the Appellate Body's finding in *China – Publications and Audiovisual Products* that Article XX is available for violations of Paragraph 5.1 of China's Accession Protocol was "grounded" in the language of Paragraph 5.1 and is not a right to regulate trade in the "abstract".⁵⁸⁷ The United States and Mexico note that the language in Paragraph 11.3 is in "contrast" to the language in the accession documents of other WTO Members with respect to their obligations on export duties.⁵⁸⁸ They further assert that China's right to promote non-trade interests is not "at risk" in this dispute, and that there are a number of ways in which China may pursue such interests.⁵⁸⁹ Specifically, they argue that Paragraph 11.3 does not prevent China from adopting measures other than export duties to promote legitimate public health or conservation objectives, and suggest that China has a number of "tools at its disposal" to pursue these ends.⁵⁹⁰

302. The European Union argues that China exercised its inherent right to regulate trade when it completed the accession process and became a Member of the WTO. According to the European Union, the provisions of the covered agreements and China's Accession Protocol in fact "delineate" China's exercise of its inherent and sovereign right to regulate trade.⁵⁹¹ The European Union also highlights the Panel's finding that there is no contradiction between China's

⁵⁸⁴Joint appellees' submission of the United States and Mexico, para. 142 (referring to Appellate Body Report, *China – Publications and Audiovisual Products*, para. 222).

⁵⁸⁵Joint appellees' submission of the United States and Mexico, paras. 143 and 144 (referring to Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 15, DSR 1996:1, 97, at 108).

⁵⁸⁶Joint appellees' submission of the United States and Mexico, para. 145.

⁵⁸⁷Joint appellees' submission of the United States and Mexico, para. 145 (referring to Appellate Body Report, *China – Publications and Audiovisual Products*, paras. 219-228).

⁵⁸⁸Joint appellees' submission of the United States and Mexico, para. 145 (referring to Report of the Working Party on the Accession of Ukraine, WT/ACC/UKR/152, paras. 240 and 512).

⁵⁸⁹Joint appellees' submission of the United States and Mexico, para. 149.

⁵⁹⁰Joint appellees' submission of the United States and Mexico, para. 150.

⁵⁹¹European Union's appellee's submission, para. 109.

inherent right to regulate trade and the commitments undertaken by China in its Accession Protocol.⁵⁹² The European Union further argues that China's obligation under Paragraph 11.3 of the Accession Protocol should not be viewed in isolation, because it is "only a small part" of the rights and obligations that China "entered into and acquired" through its WTO accession.⁵⁹³

303. We note, as did the Panel, that WTO Members have, on occasion, "incorporated, by cross-reference, the provisions of Article XX of the GATT 1994 into other covered agreements".⁵⁹⁴ For example, Article 3 of the *Agreement on Trade-Related Investment Measures* (the "TRIMs Agreement") explicitly incorporates the right to invoke the justifications of Article XX of the GATT 1994, stating that "[a]ll exceptions under GATT 1994 shall apply, as appropriate, to the provisions of this Agreement". In the present case, we attach significance to the fact that Paragraph 11.3 of China's Accession Protocol expressly refers to Article VIII of the GATT 1994, but does not contain any reference to other provisions of the GATT 1994, including Article XX.

304. In *China – Publications and Audiovisual Products*, in the context of assessing a claim brought under Paragraph 5.1 of China's Accession Protocol, the Appellate Body found that China could invoke Article XX(a) of the GATT 1994 to justify provisions found to be inconsistent with China's trading rights commitments under its Accession Protocol and Accession Working Party Report. In reaching this finding, the Appellate Body relied on the language contained in the introductory clause of Paragraph 5.1, which states "[w]ithout prejudice to China's right to regulate trade in a manner consistent with the *WTO Agreement*".⁵⁹⁵ As noted by the Panel, such language is not found in Paragraph 11.3 of China's Accession Protocol. We therefore do not agree with China to the extent that it suggests that the Appellate Body's findings in *China – Publications and Audiovisual Products* indicate that China may have recourse to Article XX of the GATT 1994 to justify export duties that are inconsistent with Paragraph 11.3.

⁵⁹²European Union's appellee's submission, para. 110 (quoting Panel Reports, para. 7.157).

⁵⁹³European Union's appellee's submission, para. 114.

⁵⁹⁴Panel Reports, para. 7.153.

⁵⁹⁵The Appellate Body referred to the question before it as being to assess whether "the introductory clause of paragraph 5.1 allows China to assert a defence under Article XX(a)". (Appellate Body Report, *China – Publications and Audiovisual Products*, para. 215) The Appellate Body characterized China's obligation under Paragraph 5.1 as "a commitment in respect of traders, in the form of a commitment to grant to all enterprises in China the right to import and export goods." (*Ibid.*, para. 226) The Appellate Body added, however, that this commitment is qualified by the introductory clause of Paragraph 5.1. On the basis of the introductory clause to Paragraph 5.1, the Appellate Body found that China's right to regulate trade "may not be impaired by China's obligation to grant the right to trade, provided that China regulates trade 'in a manner consistent with the *WTO Agreement*". (*Ibid.*, para. 221)

305. China refers to language contained in the preambles of the *WTO Agreement*, the GATT 1994, and the *Agreement on the Application of Sanitary and Phytosanitary Measures* (the "*SPS Agreement*"), *Agreement on Technical Barriers to Trade* (the "*TBT Agreement*"), the *Agreement on Import Licensing Procedures* (the "*Import Licensing Agreement*"), the GATS, and the *Agreement on Trade-Related Aspects of Intellectual Property Rights* (the "*TRIPS Agreement*") to argue that the Panel distorted the balance of rights and obligations established in China's Accession Protocol by assuming that China had "abandon[ed]" its right to impose export duties "to promote fundamental non-trade-related interests, such as conservation and public health."⁵⁹⁶

306. The preamble of the *WTO Agreement* lists various objectives, including "raising standards of living", "seeking both to protect and preserve the environment" and "expanding the production of and trade in goods and services, while allowing for the optimal use of the world's resources in accordance with the objective of sustainable development." The preamble concludes with the resolution "to develop an integrated, more viable and durable multilateral trading system". Based on this language, we understand the *WTO Agreement*, as a whole, to reflect the balance struck by WTO Members between trade and non-trade-related concerns. However, none of the objectives listed above, nor the balance struck between them, provides specific guidance on the question of whether Article XX of the GATT 1994 is applicable to Paragraph 11.3 of China's Accession Protocol. In the light of China's explicit commitment contained in Paragraph 11.3 to eliminate export duties and the lack of any textual reference to Article XX of the GATT 1994 in that provision, we see no basis to find that Article XX of the GATT 1994 is applicable to export duties found to be inconsistent with Paragraph 11.3.

5. Conclusion

307. In our analysis above, we have, in accordance with Article 3.2 of the DSU, applied the customary rules of interpretation of public international law as codified in the *Vienna Convention* in a holistic manner to ascertain whether China may have recourse to the provisions of Article XX of the GATT 1994 to justify export duties that are found to be inconsistent with Paragraph 11.3 of China's Accession Protocol. As we have found, a proper interpretation of Paragraph 11.3 of China's Accession Protocol does not make available to China the exceptions under Article XX of the GATT 1994. Consequently, we find that the Panel did not err, in paragraph 7.159 of the Panel Reports, in finding that "there is no basis in China's Accession Protocol to allow the application of Article XX of the GATT 1994 to China's obligations in Paragraph 11.3 of the Accession Protocol."

⁵⁹⁶China's appellant's submission, para. 290; see also para. 274.

We therefore uphold the Panel's conclusion, in paragraphs 8.2(b), 8.9(b), and 8.16(b) of the Panel Reports, that China may not seek to justify the application of export duties to certain forms of fluor spar pursuant to Article XX(g) of the GATT 1994 and the Panel's conclusion, in paragraphs 8.2(c), 8.9(c), and 8.16(c) of the Panel Reports, that China may not seek to justify the application of export duties to certain forms of magnesium, manganese and zinc pursuant to Article XX(b) of the GATT 1994.

VII. Article XI:2(a) of the GATT 1994

308. We turn next to China's appeal of the Panel's finding that China had not demonstrated that its export quota on refractory-grade bauxite was "temporarily applied", within the meaning of Article XI:2(a) of the GATT 1994, to either prevent or relieve a "critical shortage".⁵⁹⁷ China alleges that the Panel erred in its interpretation and application of Article XI:2(a) of the GATT 1994, and acted inconsistently with Article 11 of the DSU.

A. *The Panel's Findings and Arguments on Appeal*

309. The Panel found that China's export quota on refractory-grade bauxite is inconsistent with Article XI:1 of the GATT 1994. China argued that this export quota is a restriction temporarily applied to prevent or relieve a critical shortage of an essential product in the sense of Article XI:2(a) of the GATT 1994 and that it therefore does not fall within the scope of Article XI:1's general prohibition of quantitative restrictions. The Panel determined, however, that China had failed to demonstrate that the export quota applied to refractory-grade bauxite is justified pursuant to Article XI:2(a).⁵⁹⁸ In reaching this conclusion, the Panel agreed with China that "refractory-grade bauxite is currently 'essential' to China, as that term is used in Article XI:2(a)".⁵⁹⁹ The Panel found, however, that China had failed to demonstrate that the export quota was "temporarily applied" within the meaning of Article XI:2(a).⁶⁰⁰ The Panel also found that China had failed to demonstrate that there was a "critical shortage" of refractory-grade bauxite in China.⁶⁰¹

310. With respect to the "temporarily applied" requirement, the Panel found, based on the ordinary meaning of the word "temporarily", that Article XI:2(a) permits measures that are applied for a

⁵⁹⁷Panel Reports, para. 7.355. China also refers to paragraphs 7.257, 7.258, 7.297-7.302, 7.305, 7.306, 7.346, 7.349, 7.351, and 7.354 of the Panel Reports. (See China's appellant's submission, paras. 299 and 388)

⁵⁹⁸Panel Reports, para. 7.353.

⁵⁹⁹Panel Reports, para. 7.340.

⁶⁰⁰Panel Reports, para. 7.346.

⁶⁰¹Panel Reports, para. 7.351.

"limited timeframe".⁶⁰² The Panel considered Article XX(g) of the GATT 1994 as relevant context, and pointed to "additional protections" in the chapeau of that Article that limit Members' actions.⁶⁰³ In the Panel's view, the absence of such additional limitations in Article XI:2(a) suggested that a restriction justified under Article XI:2(a) must be of a limited duration, because otherwise Members could resort indistinguishably to either Article XI:2(a) or Article XX(g) to address the problem of an exhaustible natural resource.⁶⁰⁴ The Panel added that, "[i]f Article XI:2(a) were interpreted to permit the long-term application of measures in the nature of China's export restrictions on refractory grade bauxite, the import of Article XX(g) would be very much undermined, if not rendered redundant".⁶⁰⁵

311. Turning to the facts of the present case, the Panel observed that China's restriction on exports of refractory-grade bauxite had "already been in place for at least a decade with no indication of when it will be withdrawn and every indication that it will remain in place until the reserves have been depleted".⁶⁰⁶ On this basis, the Panel found that China's export quota could not be considered "temporarily applied" to address a critical shortage within the meaning of Article XI:2(a).⁶⁰⁷

312. With regard to the meaning of the phrase "to prevent or relieve critical shortages" in Article XI:2(a), the Panel reviewed dictionary definitions of the terms "to prevent", "to relieve", "shortage", and "critical".⁶⁰⁸ The Panel also considered that the requirement that measures be applied "temporarily" contextually informs the notion of "critical shortage". The Panel reasoned that, if there was no possibility for an existing shortage ever to cease to exist, it would not be possible to "relieve or prevent" it through an export restriction applied on a temporary basis. The Panel added that the temporal focus of "critical shortage" as interpreted by the Panel "seems consistent with the notion of 'critical', defined as 'of the nature of, or constituting, a crisis'".⁶⁰⁹

313. In its application of Article XI:2(a) in the present case, the Panel was not persuaded that there was a "critical shortage" of refractory-grade bauxite in China. The Panel expressed the view that, even if it were to accept China's assertion that natural reserves of refractory-grade bauxite would be depleted in 16 years, as contended by China, this would not demonstrate a situation "of decisive

importance", or one that is "grave", rising to the level of a "crisis".⁶¹⁰ The Panel concluded therefore that China had not demonstrated the existence of a "critical shortage" of refractory-grade bauxite. Accordingly, the Panel found that China had failed to demonstrate that the export quota applied to refractory-grade bauxite was justified pursuant to Article XI:2(a) of the GATT 1994.⁶¹¹

314. On appeal, China claims that the Panel erred in its interpretation and application of Article XI:2(a) of the GATT 1994. In particular, China alleges that the Panel erred in interpreting and applying the term "temporarily" and in interpreting the term "critical shortages" in Article XI:2(a) of the GATT 1994. First, with respect to the Panel's interpretation of the term "temporarily", China asserts that the Panel erred in excluding "long-term" export restrictions from the scope of Article XI:2(a). Second, China alleges that the Panel failed to take into consideration the fact that China's export quota on refractory-grade bauxite is subject to annual review and therefore erred in its application of the term "temporarily" to the facts of this case. Third, China maintains that the Panel erred by interpreting the term "critical shortages" to exclude shortages caused by the "finite" nature or "limited reserve[s]" of a product.⁶¹² Finally, China advances two separate claims that the Panel failed to make an objective assessment of the matter pursuant to Article 11 of the DSU.

315. In response, the United States, the European Union, and Mexico request the Appellate Body to uphold the Panel's finding that China had not demonstrated that its export quota on refractory-grade bauxite is temporarily applied to prevent or relieve a critical shortage within the meaning of Article XI:2(a) of the GATT 1994. The European Union argues that China misunderstands the Panel's statements that Article XI:2(a) should not be interpreted to permit the "long-term application of conservation measures", or "long-term measures related to conservation purposes"⁶¹³, because in making these statements the Panel was focusing on conservation measures and not on export restrictions in general.⁶¹⁴ With respect to China's allegation that the Panel failed to consider that China's export restriction on refractory-grade bauxite is annually renewed, the European Union argues that this does not have an impact on whether the measure is "temporarily" applied, because the measure has effectively been in place for more than ten years.

⁶¹⁰Panel Reports, para. 7.351. We note that the United States and Mexico contested the accuracy of China's estimate of a 16-year remaining reserve lifespan for refractory-grade bauxite, and submitted instead that the remaining lifespan was 91 years. (United States' second written submission to the Panel, para. 235; Mexico's second written submission to the Panel, para. 239; Panel Exhibit JE-165, p. 23) The Panel made no finding concerning the remaining lifespan of refractory-grade bauxite, but found that, even assuming China's assertion of a 16-year remaining reserve lifespan was correct, this would not demonstrate a situation of "crisis".
⁶¹¹Panel Reports, para. 7.353.

⁶¹²China's appellant's submission, para. 356 (quoting Panel Reports, paras. 7.297 and 7.305).

⁶¹³European Union's appellee's submission, para. 174 (quoting Panel Reports, para. 7.349).

⁶¹⁴European Union's appellee's submission, para. 175.

316. The United States and Mexico disagree with China's allegation that the Panel excluded from the scope of Article XI:2(a) any "long-term" application of export restrictions. For them, the Panel did not interpret the words "temporarily applied" so as to impose an "absolute limit" on the time period for which an export restraint may be imposed under Article XI:2(a).⁶¹⁵ Furthermore, the United States and Mexico disagree with China that the Panel erred in interpreting Article XI:2(a) "to exclude shortages caused, in part, by the exhaustibility of the product subject to the export restriction".⁶¹⁶ They submit that the Panel correctly interpreted the term "critical shortage", because the existence of a limited amount of reserves constitutes only a degree of shortage, and a mere degree of shortage does not constitute a "critical" shortage, which is one rising to the level of a crisis.⁶¹⁷ The European Union, Mexico, and the United States also request the Appellate Body to reject China's claim that the Panel acted inconsistently with its obligations under Article 11 of the DSU.

317. China's appeal therefore requires us to assess the Panel's interpretation of the terms "temporarily applied" and "critical shortages" in Article XI:2(a) of the GATT 1994, and then to consider whether the Panel properly assessed the export quota imposed on refractory-grade bauxite in the light of those interpretations.

B. *Article XI:2(a) of the GATT 1994*

318. Article XI of the GATT 1994 provides, in relevant part:

General Elimination of Quantitative Restrictions

1. No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences or other measures, shall be instituted or maintained by any contracting party on the importation of any product of the territory of any other contracting party or on the exportation or sale for export of any product destined for the territory of any other contracting party.
2. The provisions of paragraph 1 of this Article shall not extend to the following:
 - (a) Export prohibitions or restrictions temporarily applied to prevent or relieve critical shortages of foodstuffs or other products essential to the exporting contracting party[.]

⁶¹⁵Joint appellees' submission of the United States and Mexico, paras. 171 and 172.

⁶¹⁶Joint appellees' submission of the United States and Mexico, para. 173 (quoting China's appellants' submission, para. 356).

⁶¹⁷Joint appellees' submission of the United States and Mexico, para. 175.

319. Article XI:2 refers to the general obligation to eliminate quantitative restrictions set out in Article XI:1 and stipulates that the provisions of Article XI:1 "shall not extend" to the items listed in Article XI:2. Article XI:2 must therefore be read together with Article XI:1. Both Article XI:1 and Article XI:2(a) of the GATT 1994 refer to "prohibitions or restrictions". The term "prohibition" is defined as a "legal ban on the trade or importation of a specified commodity".⁶¹⁸ The second component of the phrase "[e]xport prohibitions or restrictions" is the noun "restriction", which is defined as "[a] thing which restricts someone or something, a limitation on action, a limiting condition or regulation"⁶¹⁹, and thus refers generally to something that has a limiting effect.

320. In addition, we note that Article XI of the GATT 1994 is entitled "General Elimination of Quantitative Restrictions".⁶²⁰ The Panel found that this title suggests that Article XI governs the elimination of "quantitative restrictions" generally.⁶²¹ We have previously referred to the title of a provision when interpreting the requirements within the provision.⁶²² In the present case, we consider that the use of the word "quantitative" in the title of the provision informs the interpretation of the words "restriction" and "prohibition" in Article XI:1 and XI:2. It suggests that Article XI of the GATT 1994 covers those prohibitions and restrictions that have a limiting effect on the quantity or amount of a product being imported or exported.

321. Turning to the phrase "[e]xport prohibitions or restrictions" in Article XI:2(a), we note that the words "prohibition" and "restriction" in that subparagraph are both qualified by the word "export". Thus, Article XI:2(a) covers any measure prohibiting or restricting the exportation of certain goods. Accordingly, we understand the words "prohibitions or restrictions" to refer to the same types of measures in both paragraph 1 and subparagraph 2(a), with the difference that subparagraph 2(a) is limited to prohibitions or restrictions on exportation, while paragraph 1 also covers measures relating to importation. We further note that "duties, taxes, or other charges" are excluded from the scope of Article XI:1. Thus, by virtue of the link between Article XI:1 and Article XI:2, the term "restrictions" in Article XI:2(a) also excludes "duties, taxes, or other charges". Hence, if a restriction does not fall within the scope of Article XI:1, then Article XI:2 will also not apply to it.

⁶¹⁸*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 2, p. 2363.

⁶¹⁹*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 2, p. 2553.

⁶²⁰Emphasis added.

⁶²¹Panel Reports, para. 7.912.

⁶²²See Appellate Body Report, *US – Softwood Lumber II*, para. 93; and Appellate Body Report, *US – Carbon Steel*, para. 67.

322. Having examined the meaning of the phrase "[e]xport prohibitions or restrictions", we note that Article XI:2(a) permits such measures to be "temporarily applied to prevent or relieve critical shortages of foodstuffs or other products essential to the exporting Member". We examine the meaning of each of these concepts—"temporarily applied", "to prevent or relieve critical shortages", and "foodstuffs or other products essential"—in turn below.

323. First, we note that the term "temporarily" in Article XI:2(a) of the GATT 1994 is employed as an adverb to qualify the term "applied". The word "temporary" is defined as "[l]asting or meant to last for a limited time only; not permanent; made or arranged to supply a passing need".⁶²³ Thus, when employed in connection with the word "applied", it describes a measure applied for a limited time, a measure taken to bridge a "passing need". As we see it, the definitional element of "supply[ing] a passing need" suggests that Article XI:2(a) refers to measures that are applied in the interim.

324. Turning next to consider the meaning of the term "critical shortage", we note that the noun "shortage" is defined as "[d]eficiency in quantity; an amount lacking"⁶²⁴ and is qualified by the adjective "critical", which, in turn, is defined as "[o]f, pertaining to, or constituting a crisis; of decisive importance, crucial; involving risk or suspense".⁶²⁵ The term "crisis" describes "[a] turning-point, a vitally important or decisive stage; a time of trouble, danger or suspense in politics, commerce, etc."⁶²⁶ Taken together, "critical shortage" thus refers to those deficiencies in quantity that are crucial, that amount to a situation of decisive importance, or that reach a vitally important or decisive stage, or a turning point.

325. We consider that context lends further support to this reading of the term "critical shortage". In particular, the words "general or local short supply" in Article XX(j) of the GATT 1994 provide relevant context for the interpretation of the term "critical shortage" in Article XI:2(a). We note that the term "in short supply" is defined as "available only in limited quantity, scarce".⁶²⁷ Thus, its meaning is similar to that of a "shortage", which is defined as "[d]eficiency in quantity; an amount

⁶²³*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 2, p. 3204.

⁶²⁴*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 2, p. 2813.

⁶²⁵*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 1, p. 562.

⁶²⁶*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 1, p. 561.

⁶²⁷*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 2, p. 3115.

lacking".⁶²⁸ Contrary to Article XI:2(a), however, Article XX(j) does not include the word "critical", or another adjective qualifying the short supply. We must give meaning to this difference in the wording of these provisions. To us, it suggests that the kinds of shortages that fall within Article XI:2(a) are more narrowly circumscribed than those falling within the scope of Article XX(j).

326. For Article XI:2(a) to apply, the shortage, in turn, must relate to "foodstuffs or other products essential to the exporting Member". Foodstuff is defined as "an item of food, a substance used as food".⁶²⁹ The term "essential" is defined as "[a]bsolutely indispensable or necessary".⁶³⁰ Accordingly, Article XI:2(a) refers to critical shortages of foodstuffs or otherwise absolutely indispensable or necessary products. By including, in particular, the word "foodstuffs", Article XI:2(a) provides a measure of what might be considered a product "essential to the exporting Member" but it does not limit the scope of other essential products to only foodstuffs.

327. Article XI:2(a) allows Members to apply prohibitions or restrictions temporarily in order to "prevent or relieve" such critical shortages. The word "prevent" is defined as "[p]rovide beforehand against the occurrence of (something); make impracticable or impossible by anticipatory action; stop from happening".⁶³¹ The word "relieve" means "[t]o ease out of some trouble, difficulty or danger; bring or provide aid or assistance to".⁶³² We therefore read Article XI:2(a) as providing a basis for measures adopted to alleviate or reduce an existing critical shortage, as well as for preventive or anticipatory measures adopted to pre-empt an imminent critical shortage.

328. Finally, we consider that Article XI:2(a) must be interpreted so as to give meaning to each of the concepts contained in that provision. At the same time, we must take into account that these different concepts impart meaning to each other, and thus define the scope of Article XI:2(a). For example, whether a shortage is "critical" may be informed by how "essential" a particular product is. In addition, the characteristics of the product as well as factors pertaining to a critical situation, may inform the duration for which a measure can be maintained in order to bridge a passing need in conformity with Article XI:2(a). Inherent in the notion of criticality is the expectation of reaching a

⁶²⁸*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 2, p. 2813.

⁶²⁹*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 1, p. 1008.

⁶³⁰*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 1, p. 865.

⁶³¹*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 2, p. 2341.

⁶³²*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 2, p. 2522.

point in time at which conditions are no longer "critical", such that measures will no longer fulfil the requirement of addressing a critical shortage. Accordingly, an evaluation of whether a particular measure satisfies the requirements of Article XI:2(a) necessarily requires a case-by-case analysis taking into consideration the nexus between the different elements contained in Article XI:2(a).

C. *The Panel's Evaluation of China's Export Quota on Refractory-Grade Bauxite*

329. As noted above, China argues that the Panel erred in finding that China had not demonstrated that its export quota on refractory-grade bauxite was "temporarily applied", within the meaning of Article XI:2(a) of the GATT 1994, to either prevent or relieve a "critical shortage". With respect to the Panel's interpretation of the term "temporarily", China supports the Panel's finding that the word "temporarily" suggest[s] a fixed time-limit for the application of a measure.⁶³³ China, however, alleges that the Panel subsequently "adjusted" its interpretation of the term "temporarily" to exclude the "long-term" application of export restrictions.⁶³⁴ China argues that the term "temporarily" does not mark a "bright line"⁶³⁵ moment in time after which an export restriction has necessarily been maintained for too long. Instead, Article XI:2(a) requires that the duration of a restriction be limited and bound in relation to the achievement of the stated goal. Furthermore, China argues that the Panel erroneously found that Article XI:2(a) and Article XX(g) are mutually exclusive, and that this finding was a significant motivating factor for the Panel's erroneous interpretation of the term "temporarily" in Article XI:2(a). China submits that the two provisions are not mutually exclusive, and instead apply cumulatively.⁶³⁶

330. We note that the Panel found that the word "temporarily" suggests "a fixed time-limit for the application of a measure"⁶³⁷, and also expressed the view that a "restriction or ban applied under Article XI:2(a) must be of a limited duration and not indefinite".⁶³⁸ We have set out above our interpretation of the term "temporarily" as employed in Article XI:2(a). In our view, a measure applied "temporarily" in the sense of Article XI:2(a) is a measure applied in the interim, to provide relief in extraordinary conditions in order to bridge a passing need. It must be finite, that is, applied

⁶³³ China's appellant's submission, para. 335 (quoting Panel Reports, para. 7.255).

⁶³⁴ China's appellant's submission, para. 336.

⁶³⁵ China's appellant's submission, para. 340.

⁶³⁶ China's appellant's submission, para. 375 (referring to Appellate Body Report, *Argentina – Footwear (EC)*, para. 81; Appellate Body Report, *Chile – Price Band System*, para. 186; Appellate Body Report, *EC – Asbestos*, para. 80; Panel Reports, *EC – Bananas III*, para. 7.160; Appellate Body Report, *Korea – Dairy*, para. 74; and Appellate Body Report, *US – Upland Cotton*, para. 549).

⁶³⁷ Panel Reports, para. 7.255.

⁶³⁸ Panel Reports, para. 7.258.

for a limited time. Accordingly, we agree with the Panel that a restriction or prohibition in the sense of Article XI:2(a) must be of a limited duration and not indefinite.

331. The Panel further interpreted the term "limited time" to refer to a "fixed time-limit"⁶³⁹ for the application of the measure. To the extent that the Panel was referring to a time-limit fixed in advance, we disagree that "temporary" must always connote a time-limit fixed in advance. Instead, we consider that Article XI:2(a) describes measures applied for a limited duration, adopted in order to bridge a passing need, irrespective of whether or not the temporal scope of the measure is fixed in advance.

332. China alleges that the Panel erred in reading the term "temporarily" to exclude the "long-term" application of export restrictions. In particular, China refers to the Panel's statements that Article XI:2(a) cannot be interpreted "to permit the long-term application of... export restrictions", or to "permit long-term measures to be imposed".⁶⁴⁰ We consider that the terms "long-term application" and "long-term measures" provide little value in elucidating the meaning of the term "temporary", because what is "long-term" in a given case depends on the facts of the particular case. Moreover, the terms "long-term" and "short-term" describe a different concept than the term "temporary", employed in Article XI:2(a). Viewed in the context of the Panel's entire analysis, it is clear, however, that the Panel used these words to refer back to its earlier interpretation of the term "temporarily applied" as meaning a "restriction or prohibition for a limited time". Because the Panel merely referred to its earlier interpretation of the term "temporarily applied" and did not provide additional reasoning, the Panel cannot be viewed as having "adjusted" its interpretation of the term "temporarily" to exclude the "long-term" application of export restrictions.

333. This brings us to China's allegation that the Panel erroneously found that Article XI:2(a) and Article XX(g) are mutually exclusive, and that this finding was a significant motivating factor for the Panel's erroneous interpretation of the term "temporarily" in Article XI:2(a).⁶⁴¹ As we see it, the Panel considered Article XX(g) as relevant context in its interpretation of Article XI:2(a). It noted that Article XX(g) "incorporates additional protections in its chapeau to ensure that the application of a measure does not result in arbitrary or unjustifiable discrimination or amount to a disguised restriction on international trade".⁶⁴² The Panel considered that the existence of these further

⁶³⁹ Panel Reports, para. 7.255.

⁶⁴⁰ China's appellant's submission, para. 336 (quoting Panel Reports, paras. 7.298 and 7.305, respectively, and referring to para. 7.349).

⁶⁴¹ China's appellant's submission, para. 374.

⁶⁴² Panel Reports, para. 7.258.

requirements under Article XX(g) lent support to its interpretation that an exception pursuant to Article XI:2(a) must be of a limited duration and not indefinite, because otherwise Members could resort indistinguishably to either Article XI:2(a) or to Article XX(g). We do not understand the Panel to have found that these two provisions are mutually exclusive. Rather, the Panel sought to confirm the result of its interpretation, and stated that the interpretation proffered by China would be inconsistent with the principle of effective treaty interpretation. We therefore see no merit in China's allegation that the Panel erroneously found that Article XI:2(a) and Article XX(g) are mutually exclusive. Nor do we agree that such a finding was a basis for the Panel's interpretation of the term "temporarily" in Article XI:2(a).

334. In any event, we have some doubts as to the validity of the Panel's concern that, if Article XI:2(a) is not interpreted as confined to measures of limited duration, Members could "resort indistinguishably to either Article XI:2(a) or to Article XX(g) to address the problem of an exhaustible natural resource".⁶⁴³ Members can resort to Article XX of the GATT 1994 as an exception to justify measures that would otherwise be inconsistent with their GATT obligations. By contrast, Article XI:2 provides that the general elimination of quantitative restrictions *shall not extend* to the items listed under subparagraphs (a) to (c) of that provision. This language seems to indicate that the scope of the obligation not to impose quantitative restrictions itself is limited by Article XI:2(a). Accordingly, where the requirements of Article XI:2(a) are met, there would be no scope for the application of Article XX, because no obligation exists.

335. Turning then to the Panel's application of the term "temporarily applied" in the present case, China alleges that the Panel failed to take into consideration the fact that China's export restrictions on refractory-grade bauxite are subject to annual review. China faults the Panel for "simply assum[ing]" that China's restriction on exports of refractory-grade bauxite will be maintained indefinitely.⁶⁴⁴ China submits that, at the close of each year, the factual circumstances are assessed in the light of the legal standard set forth in Article XI:2(a) to establish whether the export restriction should be maintained. We note that China has made parallel claims, under Article XI:2(a), alleging an error of application, and under Article 11 of the DSU, alleging that the Panel failed to make an objective assessment of the facts. We consider China's allegation that the Panel "simply assumed" something to

⁶⁴³Panel Reports, para. 7.257.

⁶⁴⁴China's appellant's submission, para. 349. In support, China also quoted the Panel's statement at paragraph 7.350 of its Reports that there is "every indication that [China's restriction on exports of refractory-grade bauxite] will remain in place until the reserves have been depleted".

be more in the nature of a claim made under Article 11 of the DSU, and therefore address it below at the end of our analysis in this section.

336. China further argues that the Panel erred in its interpretation and application of Article XI:2(a) by presuming that export restrictions "imposed to address a limited reserve of an exhaustible natural resource" cannot be "temporary" and that a shortage of an exhaustible non-renewable resource cannot be "critical".⁶⁴⁵ The Panel reasoned that, "if there is no possibility for an existing shortage ever to cease to exist, it will not be possible to 'relieve or prevent' it through an export restriction applied on a temporary basis."⁶⁴⁶ The Panel further stated that, "[i]f a measure were imposed to address a limited reserve of an exhaustible natural resource, such measure would be imposed until the point when the resource is fully depleted."⁶⁴⁷ The Panel added that "[i]n this temporal focus seems consistent with the notion of 'critical', defined as 'of the nature of, or constituting, a crisis'".⁶⁴⁸

337. We do not agree with China that these statements by the Panel indicate that the Panel presumed that a shortage of an exhaustible non-renewable resource cannot be "critical" within the meaning of Article XI:2(a).⁶⁴⁹ The Panel noted instead, correctly in our view, that the reach of Article XI:2(a) is not the same as that of Article XX(g), adding that these provisions are "intended to address different situations and thus must mean different things".⁶⁵⁰ Articles XI:2(a) and XX(g) have different functions and contain different obligations. Article XI:2(a) addresses measures taken to prevent or relieve "critical shortages" of foodstuffs or other essential products. Article XX(g), on the other hand, addresses measures relating to the conservation of exhaustible natural resources. We do not exclude that a measure falling within the ambit of Article XI:2(a) could relate to the same product as a measure relating to the conservation of an exhaustible natural resource. It would seem that Article XI:2(a) measures could be imposed, for example, if a natural disaster caused a "critical shortage" of an exhaustible natural resource, which, at the same time, constituted a foodstuff or other essential product. Moreover, because the reach of Article XI:2(a) is different from that of Article XX(g), an Article XI:2(a) measure might operate simultaneously with a conservation measure complying with the requirements of Article XX(g).⁶⁵¹

⁶⁴⁵China's appellant's submission, paras. 356 and 367 (quoting Panel Reports, 7.297).

⁶⁴⁶Panel Reports, para. 7.297.

⁶⁴⁷Panel Reports, para. 7.297.

⁶⁴⁸Panel Reports, para. 7.297.

⁶⁴⁹China's appellant's submission, paras. 367 (quoting Panel Reports, para. 7.297).

⁶⁵⁰Panel Reports, para. 7.300.

⁶⁵¹European Union's appellee's submission, para. 166.

338. As a final matter, we note that China advances two separate claims that the Panel failed to make an objective assessment of the matter pursuant to Article 11 of the DSU. First, China alleges that the Panel failed properly to assess evidence that China's export restriction is annually reviewed and renewed, and that the Panel's failure to consider this evidence has a bearing on the objectivity of the Panel's factual assessment.⁶⁵² China submits that evidence relating to China's annual review procedures demonstrates that the export restriction will be maintained only as long as it is justified to prevent or relieve the critical shortage of refractory-grade bauxite. For China, this evidence demonstrates that the Panel erred in assuming that the restriction "will remain in place until the reserves have been depleted".⁶⁵³

339. We note that the Panel identified several reasons for finding that China's export restriction is not temporarily applied to prevent or relieve a critical shortage. The Panel observed that China's restriction on exports of refractory-grade bauxite had "already been in place for at least a decade with no indication of when it will be withdrawn and every indication that it will remain in place until the reserves have been depleted".⁶⁵⁴ The Panel also referred to evidence of the existence of an export quota submitted by the parties⁶⁵⁵, as well as China's explanation that its "export quota on refractory-grade bauxite forms part of a conservation plan aimed at extending the reserves of refractory-grade bauxite".⁶⁵⁶

340. To us, these elements of the Panel's reasoning indicate that the Panel's finding was not, as China alleges, based on a mere "assumption" that the restriction would remain in effect until depletion of the reserves. Instead, the Panel considered evidence indicating that the measure had been in place for at least a decade and China does not contest the Panel's finding that this was the case. In particular, the Panel noted that "China has had an export quota in place on exports of bauxite classifiable under HS No. 2508.3000 dating back to at least 2000" and found that "China's estimation of a 16-year reserve for bauxite suggests that China intends to maintain its measure in place until the exhaustion of remaining reserves (in keeping with its contention that it needs to restrain consumption), or until new technology or conditions lessen demand for refractory-grade bauxite."⁶⁵⁷ In addition, as an indication that the restrictions would remain in place until depletion, the Panel noted

⁶⁵²China's appellant's submission, para. 354.

⁶⁵³China's appellant's submission, para. 355 (quoting Panel Reports, para. 7.350).

⁶⁵⁴Panel Reports, para. 7.350.

⁶⁵⁵In particular, footnote 563 to paragraph 7.348 of the Panel Reports demonstrates that the Panel relied on evidence regarding the existence of the export quota.

⁶⁵⁶Panel Reports, para. 7.348 (referring to China's second written submission to the Panel, para. 141).
⁶⁵⁷Panel Reports, para. 7.348.

China's explanation that its export quota on refractory-grade bauxite forms part of a conservation plan aimed at extending the reserves of refractory-grade bauxite.

341. China's argument appears to be directed mainly at the weight the Panel ascribed to evidence indicating that the export restriction is annually reviewed and renewed. The Appellate Body has consistently recognized that panels enjoy a margin of discretion in their assessment of the facts.⁶⁵⁸ This margin includes the discretion of a panel to decide which evidence it chooses to utilize in making its findings⁶⁵⁹, and to determine how much weight to attach to the various items of evidence placed before it by the parties.⁶⁶⁰ A panel does not err simply because it declines to accord to the evidence the weight that one of the parties believes should be accorded to it.⁶⁶¹ A panel is entitled "to determine that certain elements of evidence should be accorded more weight than other elements—that is the essence of the task of appreciating the evidence".⁶⁶² We therefore reject China's claim that the Panel failed to make an objective assessment of the matter as required by Article 11 of the DSU.

342. Next, China asserts that the Panel employed internally inconsistent or incoherent reasoning in stating, on the one hand, that "there is no possibility for an existing shortage [of an exhaustible natural resource] ever to cease to exist" such that "it will not be possible to 'relieve or prevent' it through an export restriction applied on a temporary basis"⁶⁶³ and acknowledging, on the other hand, that "advances in reserve detection or extraction techniques", or the availability of "additional capacity", could "alleviate or eliminate" a shortage of an exhaustible natural resource⁶⁶⁴, or that "new technology or conditions" might "lessen demand" for the resource.⁶⁶⁵

343. The Appellate Body has previously found that a Panel's reasoning may be so internally inconsistent that it amounts to a breach of Article 11 of the DSU.⁶⁶⁶ We do not consider this to be the case here. Contrary to what China suggests, the Panel did not find that "there is no possibility for an existing shortage [of an exhaustible natural resource] ever to cease to exist", such that 'it will not be

⁶⁵⁸Appellate Body Report, *EC – Asbestos*, para. 161; Appellate Body Report, *EC – Hormones*, para. 132; Appellate Body Report, *EC – Sardines*, para. 299; Appellate Body Report, *Japan – Apples*, para. 222; Appellate Body Report, *Korea – Dairy*, paras. 137 and 138; Appellate Body Report, *US – Wheat Gluten*, para. 151.

⁶⁵⁹Appellate Body Report, *EC – Hormones*, para. 135.

⁶⁶⁰Appellate Body Report, *Korea – Dairy*, para. 137.

⁶⁶¹Appellate Body Report, *Australia – Salmon*, para. 267; Appellate Body Report, *Japan – Apples*, para. 221; Appellate Body Report, *Korea – Alcoholic Beverages*, para. 164.

⁶⁶²Appellate Body Report, *EC – Asbestos*, para. 161.

⁶⁶³China's appellant's submission, para. 373 (referring to Panel Reports, para. 7.297). (emphasis added by China omitted)

⁶⁶⁴China's appellant's submission, para. 373 (quoting Panel Reports, para. 7.351).

⁶⁶⁵China's appellant's submission, para. 373 (referring to Panel Reports, paras. 7.348 and 7.351).

⁶⁶⁶Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 894.

possible to 'relieve or prevent' it through an export restriction applied on a temporary basis".⁶⁶⁷ Instead, the Panel's statement to which China refers contains a hypothetical. It reads as follows: "if there is no possibility for an existing shortage ever to cease to exist, it will not be possible to 'relieve or prevent' it through an export restriction applied on a temporary basis."⁶⁶⁸ The Panel did not make such a finding but employed a hypothetical and did not, as China alleges, make two internally inconsistent findings. Therefore, the Panel did not fail to conduct an objective assessment of the matter pursuant to Article 11 of the DSU.

344. For the above reasons, we *uphold* the Panel's conclusion that China did not demonstrate that its export quota on refractory-grade bauxite was "temporarily applied", within the meaning of Article XI:2(a) of the GATT 1994, to either prevent or relieve a "critical shortage"⁶⁶⁹, and we dismiss China's allegation that the Panel acted inconsistently with its duty to conduct an objective assessment of the matter as required by Article 11 of the DSU.

VIII. Article XX(g) of the GATT 1994

345. China alleges that the Panel erred in interpreting the phrase "made effective in conjunction with" in Article XX(g) to mean that restrictions on domestic production or consumption must "be applied jointly with the challenged export restrictions", and that "the purpose of those export restrictions must be to ensure the effectiveness of those domestic restrictions".⁶⁷⁰

A. *The Panel's Findings and Arguments on Appeal*

346. The Panel found that China's export quota on refractory-grade bauxite is inconsistent with Article XI:1 of the GATT 1994. China sought to justify this export quota pursuant to Article XX(g) of the GATT 1994, arguing that refractory-grade bauxite is an exhaustible natural resource that is scarce and requires protection.⁶⁷¹

347. The Panel first addressed the question of whether China's export quota relates to the conservation of refractory-grade bauxite. Based on its review of the evidence and arguments before

China)
⁶⁶⁷China's appellant's submission, para. 373 (quoting Panel Reports, para. 7.297). (emphasis added by China)
⁶⁶⁸Panel Reports, para. 7.297. (emphasis added)
⁶⁶⁹Panel Reports, para. 7.355. China also refers to paragraphs 7.257, 7.258, 7.297-7.302, 7.305, 7.306, 7.346, 7.349, 7.351, and 7.354 of the Panel Reports. (See China's appellant's submission, paras. 299 and 388)
⁶⁷⁰Panel Reports, para. 7.397.
⁶⁷¹See Panel Reports, para. 7.356.

it, the Panel found this not to be the case.⁶⁷² The Panel nevertheless continued its analysis in order to determine whether the export quota on refractory-grade bauxite was "made effective in conjunction with" restrictions on domestic production or consumption, as required under Article XX(g) of the GATT 1994.

348. The Panel considered that, in order for a measure to be justified under Article XX(g), the measure must satisfy two conditions: (i) it must relate to the conservation of an exhaustible natural resource; and (ii) it must be made effective in conjunction with restrictions on domestic production or consumption. With respect to the first requirement, the Panel stated that the words "relate to ... conservation" have been interpreted by the Appellate Body to require a substantial relationship between the trade measure and conservation, so that the trade measure would be "primarily aimed at" the conservation of exhaustible natural resources.⁶⁷³ The Panel further noted that the term "conservation" is defined as "the act of preserving and maintaining the existing state of something, in this case 'natural resources' covered by Article XX(g)".⁶⁷⁴

349. With respect to the requirement that conservation measures in the sense of Article XX(g) be "made effective in conjunction with" restrictions on domestic production, the Panel referred to a statement of the GATT panel in *Canada – Herring and Salmon*, that a measure can only be considered to be "made effective in conjunction with" restrictions on domestic production, if it is "primarily aimed at rendering effective these restrictions".⁶⁷⁵ The Panel also quoted the Appellate Body's statement in *US – Gasoline* that the phrase "if such measures are made effective in conjunction with restrictions on domestic products or consumption" is appropriately read as a requirement that the measures concerned impose restrictions, not just in respect of imported [products], but also with respect to domestic [products].⁶⁷⁶ The Panel then found that "restrictions on domestic production or consumption must not only be applied jointly with the challenged export restrictions but, in addition, the purpose of those export restrictions must be to ensure the effectiveness of those domestic restrictions."⁶⁷⁷

⁶⁷²Panel Reports, para. 7.435.

⁶⁷³Panel Reports, para. 7.370 (quoting Appellate Body Report, *US – Gasoline*, p. 18, DSR 1996:1. 3, at 17).

⁶⁷⁴Panel Reports, para. 7.372.

⁶⁷⁵Panel Reports, para. 7.395 (quoting GATT Panel Report, *Canada – Herring and Salmon*, para. 4.6). (emphasis added by the Panel omitted)

⁶⁷⁶Panel Reports, para. 7.396 (quoting Appellate Body Report, *US – Gasoline*, p. 20, DSR 1996:1. 3, at 19).

⁶⁷⁷Panel Reports, para. 7.397 (referring to GATT Panel Report, *Canada – Herring and Salmon*, para. 4.6).

350. China alleges that the Panel erred in its interpretation of the phrase "made effective in conjunction with" in Article XX(g) of the GATT 1994. China maintains that the Panel read this phrase to mean that, in order to be justified under Article XX(g), a challenged measure must satisfy two cumulative conditions: first, it must "be applied jointly" with restrictions on domestic production or consumption; and, second, the "purpose" of the challenged measure must be to make effective restrictions on domestic production or consumption. China argues that the first element of this interpretation is consistent with the ordinary meaning of the phrase "made effective in conjunction with", but that the second is not. China requests the Appellate Body to reverse the erroneous second element of the Panel's interpretation.⁶⁷⁸ China does not, however, appeal the Panel's ultimate conclusion that China's export quota on refractory-grade bauxite is inconsistent with Article XI of the GATT 1994 and not justified under Article XX(g).⁶⁷⁹

351. China submits that the Appellate Body's interpretation of the term "in conjunction with" in *US – Gasoline* corresponds to the first element of the meaning that the Panel attributed to that term, namely, that the challenged measures "be applied jointly with" restrictions on domestic production or consumption.⁶⁸⁰ China submits, however, that nothing in the phrase "made effective in conjunction with" suggests that the "purpose" of a challenged measure must be to ensure the effectiveness of domestic restrictions.⁶⁸¹ In particular, China argues that Article XX(g) does not require that each set of measures must have, as a separate and independent purpose, the goal of ensuring the effectiveness of the other set of measures. For China, it suffices that the challenged measure is related to the conservation of a natural resource, and that it operates together with domestic restrictions on the production or consumption of the same resource.⁶⁸²

352. By contrast, the United States and Mexico request the Appellate Body to uphold the Panel's reasoning. They submit that *US – Gasoline* did not involve the particular interpretive question of how the operation of the challenged measure should be conjoined with the operation of domestic restrictions, and that the present case was the first instance since the GATT panel proceeding in *Canada – Herring and Salmon* that a respondent asserted Article XX(g) as a defence where the challenged measure was distinct from the restrictions on domestic production or consumption.⁶⁸³ Therefore, the United States and Mexico argue that the Panel appropriately drew upon the *Canada –*

⁶⁷⁸China's appellant's submission, para. 391.

⁶⁷⁹China's appellant's submission, para. 392.

⁶⁸⁰China's appellant's submission, paras. 405 and 406.

⁶⁸¹China's appellant's submission, para. 407.

⁶⁸²China's appellant's submission, para. 411.

⁶⁸³The United States and Mexico further submit that the Appellate Body report in *US – Shrimp* also did not involve this question. (Joint appellees' submission of the United States and Mexico, para. 215)

Herring and Salmon panel's reasoning.⁶⁸⁴ The European Union also supports the Panel's reasoning, arguing that the GATT panel rightly stated that a measure can only be made effective "in conjunction with" domestic restrictions on production if it is primarily aimed at rendering effective these restrictions.

B. Analysis

353. Article XX of the GATT 1994 provides, in relevant part:

General Exceptions

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:

...
(g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption[.]

354. Article XX of the GATT 1994 contemplates a two-tiered analysis of a measure that a Member seeks to justify under that provision.⁶⁸⁵ A respondent must first demonstrate that the challenged measure falls within the scope of one of the subparagraphs of Article XX. Where this is the case, a respondent must further establish that the measure at issue satisfies the requirements of the chapeau of Article XX.

355. In order to fall within the ambit of subparagraph (g) of Article XX, a measure must "relat[e] to the conservation of exhaustible natural resources". The term "relat[e] to" is defined as "hav[ing] some connection with, be[ing] connected to".⁶⁸⁶ The Appellate Body has found that, for a measure to relate to conservation in the sense of Article XX(g), there must be "a close and genuine relationship of

⁶⁸⁴Joint appellees' submission of the United States and Mexico, para. 220.

⁶⁸⁵Appellate Body Report, *US – Shrimp*, paras. 118, 119, and 147. See also Appellate Body Report, *US – Gasoline*, p. 22, DSR 1996:1, 3, at 20; and Appellate Body Report, *US – Gambling*, para. 292.

⁶⁸⁶*Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 2, p. 2519.

ends and means".⁶⁸⁷ The word "conservation", in turn, means "the preservation of the environment, especially of natural resources".⁶⁸⁸

356. Article XX(g) further requires that conservation measures be "made effective in conjunction with restrictions on domestic production or consumption". The word "effective" as relating to a legal instrument is defined as "in operation at a given time".⁶⁸⁹ We consider that the term "made effective", when used in connection with a legal instrument, describes measures brought into operation, adopted, or applied. The Spanish and French equivalents of "made effective"—namely "*se aplican*" and "*sont appliquées*"—confirm this understanding of "made effective". The term "in conjunction" is defined as "together, jointly, (with)".⁶⁹⁰ Accordingly, the trade restriction must operate jointly with the restrictions on domestic production or consumption. Article XX(g) thus permits trade measures relating to the conservation of exhaustible natural resources when such trade measures work together with restrictions on domestic production or consumption, which operate so as to conserve an exhaustible natural resource. By its terms, Article XX(g) does not contain an additional requirement that the conservation measure be primarily aimed at making effective the restrictions on domestic production or consumption.

357. The Appellate Body addressed Article XX(g) in *US – Gasoline*.⁶⁹¹ The Appellate Body noted Venezuela's and Brazil's argument that, to be deemed as "made effective in conjunction with restrictions on domestic production or consumption", a measure must be "primarily aimed at" both conservation of exhaustible natural resources and making effective certain restrictions on domestic production or consumption. The Appellate Body, however, found that:

... "made effective" when used in connection with a measure—a governmental act or regulation—may be seen to refer to such measure being "operative", as "in force", or as having "come into effect." Similarly, the phrase "in conjunction with" may be read quite plainly as "together with" or "jointly with." Taken together, the second clause of Article XX(g) appears to us to refer to governmental measures like the baseline establishment rules being promulgated or brought into effect together with restrictions on domestic production or consumption of natural resources. Put in a slightly different manner, we believe that the clause "if such measures are made

⁶⁸⁷ Appellate Body Report, *US – Shrimp*, para. 136.

⁶⁸⁸ *Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 1, p. 496.

⁶⁸⁹ *Black's Law Dictionary*, 9th edn, B.A. Garner (ed.) (West Group, 2009), p. 592.

⁶⁹⁰ *Shorter Oxford English Dictionary*, 6th edn, W.R. Trumble, A. Stevenson (eds) (Oxford University Press, 2007), Vol. 1, p. 492.

⁶⁹¹ Appellate Body Report, *US – Gasoline*, pp. 19-22, DSR 1996:1, 3, at 18-20.

effective in conjunction with restrictions on domestic production or consumption" is appropriately read as a requirement that the measures concerned impose restrictions, not just in respect of imported gasoline but also with respect to domestic gasoline. The clause is a requirement of even-handedness in the imposition of restrictions, in the name of conservation, upon the production or consumption of exhaustible natural resources.⁶⁹²

358. Accordingly, in assessing whether the baseline establishment rules at issue in *US – Gasoline* were "made effective in conjunction with" restrictions on domestic production or consumption, the Appellate Body relied on the fact that those rules were promulgated or brought into effect "together with" restrictions on domestic production or consumption of natural resources. However, even though Brazil and Venezuela had presented arguments suggesting that it was necessary that the purpose of the baseline establishment rules be to ensure the effectiveness of restrictions on domestic production, the Appellate Body did *not* consider this to be necessary. In particular, the Appellate Body did not consider that, in order to be justified under Article XX(g), measures "relating to the conservation of exhaustible natural resources" must be primarily aimed at rendering effective restrictions on domestic production or consumption. Instead, the Appellate Body read the terms "in conjunction with", "quite plainly", as "together with" or "jointly with"⁶⁹³, and found no additional requirement that the conservation measure be primarily aimed at making effective certain restrictions on domestic production or consumption.

359. As noted above, the Panel in the present case appears to have considered that, in order to prove that a measure is "made effective in conjunction with" restrictions on domestic production or consumption in the sense of Article XX(g), it must be established, first, that the measure is applied jointly with restrictions on domestic production or consumption, and, second, that the purpose of the challenged measure is to make effective restrictions on domestic production or consumption. In particular, the Panel's use of the words "not only ... but, in addition", as well as the reference at the end of the sentence to the GATT panel report in *Canada – Herring and Salmon*, indicate that the Panel did in fact consider that two separate conditions have to be met for a measure to be considered "made effective in conjunction with" in the sense of Article XX(g).

360. As explained above, we see nothing in the text of Article XX(g) to suggest that, in addition to being "made effective in conjunction with restrictions on domestic production or consumption", a trade restriction must be aimed at ensuring the effectiveness of domestic restrictions, as the Panel

⁶⁹² Appellate Body Report, *US – Gasoline*, p. 20, DSR 1996:1, 3, at 19.

⁶⁹³ Appellate Body Report, *US – Gasoline*, p. 20, DSR 1996:1, 3, at 19.

found. Instead, we have found above that Article XX(g) permits trade measures relating to the conservation of exhaustible natural resources if such trade measures work together with restrictions on domestic production or consumption, which operate so as to conserve an exhaustible natural resource.

361. Based on the foregoing, we *find* that the Panel erred in interpreting the phrase "made effective in conjunction with" in Article XX(g) of the GATT 1994 to require a separate showing that the purpose of the challenged measure must be to make effective restrictions on domestic production or consumption. Accordingly, we *reverse* this interpretation by the Panel in paragraph 7.397 of the Panel Reports.

IX. Findings and Conclusions in the Appellate Body Report WT/DS394/AB/R

362. In the appeal of the Panel Report in *China – Measures Related to the Exportation of Various Raw Materials* (complaint by the United States, WT/DS394/R) (the "US Panel Report"), for the reasons set out in this Report, the Appellate Body:

- (a) finds that the Panel erred under Article 6.2 of the DSU in making findings regarding claims allegedly identified in Section III of the United States' panel request; and therefore declares moot and of no legal effect the Panel findings in paragraph 8.4(a)-(d) in respect of claims concerning export quota administration and allocation; in paragraph 8.5(a)-(b) in respect of claims concerning export licensing requirements; in paragraph 8.6(a)-(b) in respect of claims concerning a minimum export price requirement; and in paragraph 8.4(e) of the US Panel Report in respect of claims concerning fees and formalities in connection with exportation.
- (b) finds that the Panel did not err in recommending, in paragraph 8.8 of the US Panel Report, that China bring its measures into conformity with its WTO obligations such that the "series of measures" do not operate to bring about a WTO-inconsistent result;
- (c) finds that the Panel did not err, in paragraph 7.159 of the US Panel Report, in finding that there is no basis in China's Accession Protocol to allow the application of Article XX of the GATT 1994 to China's obligations in Paragraph 11.3 of China's Accession Protocol; and therefore upholds the Panel's conclusion, in paragraph 8.2(b) of the US Panel Report, that China may not seek to justify the application of export duties to certain forms of fluorspar pursuant to Article XX(g) of the GATT 1994 and the Panel's conclusion, in paragraph 8.2(c) of the US Panel Report, that China may not seek to justify the application of export duties to certain forms of magnesium, manganese and zinc pursuant to Article XX(b) of the GATT 1994;
- (d) with respect to Article XI:2(a) of the GATT 1994:
 - (i) upholds the Panel's conclusion, in paragraph 7.355 of the US Panel Report, that China had not demonstrated that its export quota on refractory-grade bauxite was "temporarily applied", within the meaning of Article XI:2(a) of the GATT 1994, to either prevent or relieve a "critical shortage";

(ii) finds that China has not demonstrated that the Panel acted inconsistently with its duty to conduct an objective assessment of the matter as required by Article 11 of the DSU; and

(e) finds that the Panel erred in interpreting the phrase "made effective in conjunction with", in Article XX(g) of the GATT 1994, to require that the purpose of the export restriction must be to ensure the effectiveness of restrictions on domestic production and consumption, and therefore reverses this interpretation by the Panel in paragraph 7.397 of the US Panel Report.

363. The Appellate Body recommends that the DSB request China to bring its measures, found in this Report and in the US Panel Report, as modified by this Report, to be inconsistent with China's Accession Protocol and the GATT 1994, into conformity with China's obligations thereunder, such that the "series of measures" do not operate to bring about a WTO-inconsistent result.

Signed in the original in Geneva this 10th day of January 2012 by:

Ricardo Ramirez-Hernández
Presiding Member

Jennifer Hillman
Member

Shotaro Oshima
Member

IX. Findings and Conclusions in the Appellate Body Report WT/DS395/AB/R

362. In the appeal of the Panel Report in *China – Measures Related to the Exportation of Various Raw Materials* (complaint by the European Union, WT/DS395/R) (the "EU Panel Report"), for the reasons set out in this Report, the Appellate Body:

(a) finds that the Panel erred under Article 6.2 of the DSU in making findings regarding claims allegedly identified in Section III of the European Union's panel request; and therefore declares moot and of no legal effect the Panel findings in paragraph 8.11(a)-(e) in respect of claims concerning export quota administration and allocation; in paragraph 8.12(a)-(b) in respect of claims concerning export licensing requirements; and in paragraph 8.13(a)-(b) of the EU Panel Report in respect of claims concerning a minimum export price requirement;

(b) finds that the Panel did not err in recommending, in paragraph 8.15 of the EU Panel Report, that China bring its measures into conformity with its WTO obligations such that the "series of measures" do not operate to bring about a WTO-inconsistent result;

(c) finds that the Panel did not err, in paragraph 7.159 of the EU Panel Report, in finding that there is no basis in China's Accession Protocol to allow the application of Article XX of the GATT 1994 to China's obligations in Paragraph 11.3 of China's Accession Protocol; and therefore upholds the Panel's conclusion, in paragraph 8.9(b) of the EU Panel Report, that China may not seek to justify the application of export duties to certain forms of fluorspar pursuant to Article XX(g) of the GATT 1994 and the Panel's conclusion, in paragraph 8.9(c) of the EU Panel Report, that China may not seek to justify the application of export duties to certain forms of magnesium, manganese and zinc pursuant to Article XX(b) of the GATT 1994;

(d) with respect to Article XI:2(a) of the GATT 1994:

(i) upholds the Panel's conclusion, in paragraph 7.355 of the EU Panel Report, that China had not demonstrated that its export quota on refractory-grade bauxite was "temporarily applied", within the meaning of Article XI:2(a) of the GATT 1994, to either prevent or relieve a "critical shortage";

(ii) finds that China has not demonstrated that the Panel acted inconsistently with its duty to conduct an objective assessment of the matter as required by Article 11 of the DSU; and

(c) finds that the Panel erred in interpreting the phrase "made effective in conjunction with", in Article XX(g) of the GATT 1994, to require that the purpose of the export restriction must be to ensure the effectiveness of restrictions on domestic production and consumption, and therefore reverses this interpretation by the Panel in paragraph 7.397 of the EU Panel Report.

363. The Appellate Body recommends that the DSB request China to bring its measures, found in this Report and in the EU Panel Report, as modified by this Report, to be inconsistent with China's Accession Protocol and the GATT 1994, into conformity with China's obligations thereunder, such that the "series of measures" do not operate to bring about a WTO-inconsistent result.

Signed in the original in Geneva this 10th day of January 2012 by:

Ricardo Ramirez-Hernández
Presiding Member

Jennifer Hillman
Member

Shotaro Oshima
Member

IX. Findings and Conclusions in the Appellate Body Report WT/DS398/AB/R

362. In the appeal of the Panel Report in *China – Measures Related to the Exportation of Various Raw Materials* (complaint by Mexico, WT/DS398/R) (the "Mexico Panel Report"), for the reasons set out in this Report, the Appellate Body:

(a) finds that the Panel erred under Article 6.2 of the DSU in making findings regarding claims allegedly identified in Section III of Mexico's panel request; and therefore declares moot and of no legal effect the Panel findings in paragraph 8.18(a)-(d) in respect of claims concerning export quota administration and allocation; in paragraph 8.19(a)-(b) in respect of claims concerning export licensing requirements; in paragraph 8.20(a)-(b) in respect of claims concerning a minimum export price requirement; and in paragraph 8.18(e) of the Mexico Panel Report in respect of claims concerning fees and formalities in connection with exportation;

(b) finds that the Panel did not err in recommending, in paragraph 8.22 of the Mexico Panel Report, that China bring its measures into conformity with its WTO obligations such that the "series of measures" do not operate to bring about a WTO-inconsistent result;

(c) finds that the Panel did not err, in paragraph 7.159 of the Mexico Panel Report, in finding that there is no basis in China's Accession Protocol to allow the application of Article XX of the GATT 1994 to China's obligations in Paragraph 11.3 of China's Accession Protocol; and therefore upholds the Panel's conclusion, in paragraph 8.16(b) of the Mexico Panel Report, that China may not seek to justify the application of export duties to certain forms of fluorspar pursuant to Article XX(g) of the GATT 1994 and the Panel's conclusion, in paragraph 8.16(c) of the Mexico Panel Report, that China may not seek to justify the application of export duties to certain forms of magnesium, manganese and zinc pursuant to Article XX(b) of the GATT 1994;

(d) with respect to Article XI:2(a) of the GATT 1994:

(i) upholds the Panel's conclusion, in paragraph 7.355 of the Mexico Panel Report, that China had not demonstrated that its export quota on refractory-grade bauxite was "temporarily applied", within the meaning of Article XI:2(a) of the GATT 1994, to either prevent or relieve a "critical shortage";

(ii) finds that China has not demonstrated that the Panel acted inconsistently with its duty to conduct an objective assessment of the matter as required by Article 11 of the DSU; and

(e) finds that the Panel erred in interpreting the phrase "made effective in conjunction with", in Article XX(g) of the GATT 1994, to require that the purpose of the export restriction must be to ensure the effectiveness of restrictions on domestic production and consumption, and therefore reverses this interpretation by the Panel in paragraph 7.397 of the Mexico Panel Report.

363. The Appellate Body recommends that the DSB request China to bring its measures, found in this Report and in the Mexico Panel Report, as modified by this Report, to be inconsistent with China's Accession Protocol and the GATT 1994, into conformity with China's obligations thereunder, such that the "series of measures" do not operate to bring about a WTO-inconsistent result.

Signed in the original in Geneva this 10th day of January 2012 by:

Ricardo Ramirez-Hernández
Presiding Member

Jennifer Hillman
Member

Shotaro Oshima
Member

ANNEX I

WORLD TRADE ORGANIZATION

WT/DS394/7
9 November 2009
(09-5564)

Original: English

CHINA – MEASURES RELATED TO THE EXPORTATION OF VARIOUS RAW MATERIALS

Request for the Establishment of a Panel by the United States

The following communication, dated 4 November 2009, from the delegation of the United States to the Chairman of the Dispute Settlement Body, is circulated pursuant to Article 6.2 of the DSU.

On 23 June 2009, the United States requested consultations with the Government of the People's Republic of China ("China") pursuant to Articles 1 and 4 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Article XXII of the *General Agreement on Tariffs and Trade 1994* ("GATT 1994") with respect to China's restraints on the exportation from China of various forms of bauxite¹, coke², fluorspar³, magnesium⁴, manganese⁵,

¹ Bauxite includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes, as listed in Attachment I of Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009) ("2009 Export Licensing List") and/or the following eight-digit HS numbers as listed in Table 7 of Notice Regarding the 2009 Tariff Implementation Program (State Council Tariff Policy Commission, shuweihui (2008) No. 40, January 1, 2009) ("2009 Export Duty List"): 2508300000/25083000, 2606000000/26060000, 26204000.

² Coke includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2704001000/27040010.

³ Fluorspar includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2529210000/25292100, 2529220000/25292200.

⁴ Magnesium includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 81041100, 81041900, 81042000.

⁵ Manganese includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 26020000, 8111001010/81110010, 8111001090/81110010.

silicon carbide⁶, silicon metal⁷, yellow phosphorus⁸, and zinc⁹ (the "materials"). The United States held consultations with China on 31 July 2009, and 1-2 September 2009. Those consultations unfortunately did not resolve the dispute.

I. Export Quotas

China subjects the exportation of bauxite, coke, fluorspar, silicon carbide, and zinc to quantitative restrictions such as quotas.

The United States understands that these Chinese measures are reflected in, among others:

- Foreign Trade Law of the People's Republic of China (adopted at the 8th Session of the Standing Committee of the Tenth National People's Congress on April 6, 2004, promulgated on July 1, 2004)
- Regulation of the People's Republic of China on the Administration of the Import and Export of Goods (passed at the forty-sixth executive meeting of the State Council on October 31, 2001, January 1, 2002)
- Measures for the Administration of License for the Export of Goods (Order of the Ministry of Commerce (2008) No. 11, July 1, 2008)
- Measures for the Administration of Export Commodities Quotas (Order of the Ministry of Foreign Trade and Economic Cooperation No. 12, adopted on December 20, 2001, January 1, 2002)
- Measures of Quota Bidding for Export Commodities (Decree of the Ministry of Foreign Trade and Economic Cooperation No. 11, adopted on December 20, 2001, January 1, 2002)
- Measures for the Administration of the Organs for Issuing the Licenses of Import and Export Commodities (Ministry of Foreign Trade and Economic Cooperation, waijingmaopeiguanhanzi (1999) No. 68, September 21, 1999)
- Implementation Rules of Export Quota Bidding for Industrial Products (Ministry of Foreign Trade and Economic Cooperation, November 8, 2001)

⁶ Silicon carbide includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2849200000, 3824909910.

⁷ Silicon metal includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 28046900.

⁸ Yellow phosphorus includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 28047010.

⁹ Zinc includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2608000001/260800000, 2608000090/260800000, 790111110000/7901111100, 7901119000/79011190, 7901120000/79011200, 7901200000/79012000, 79020000, 26201100, 26201900.

- Working Rules on Issuing Export Licenses (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)
- Rules on the Administration of Import and Export License Certificates (Ministry of Foreign Trade and Economic Cooperation, waijingmaopeizi (1999) No. 87, December 6, 1999)
- Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2008) No. 83, January 1, 2009)
- Notice Regarding Passing Down the 2009 First Batch Regular Trade Coke Export Quota (Ministry of Commerce, shangmaohan (2008) No. 140, January 1, 2009)
- 2009 Coke Export Quota Declaration Conditions and Declaration Procedures (Ministry of Commerce, Notice (2008) No. 76, October 13, 2008)
- Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009)
- Announcement of the Ministry of Commerce Issuing the "2009 Graded License-Issuing List of Commodities Subject to Export License Administration" (Ministry of Commerce, Notice (2008) No. 124, January 1, 2009)
- Announcement Regarding Printing "Working Rules on Issuing Export Licenses" (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)
- Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009 (Ministry of Commerce, Announcement (2008) No. 85, October 30, 2008)
- Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009 (Ministry of Commerce, Announcement (2009) No. 42, June 9, 2009)
- Circular of the Ministry of Foreign Trade and Economic Cooperation on Distribution of the "Implementation Rules of Export Quota Bidding for Industrial Products" (Ministry of Foreign Trade and Economic Cooperation, issued on November 8, 2001)
- Quotas of Fluorspar Lump (Powder) of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Quotas of Bauxite of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 10, 2008)
- Quotas of Silicon Carbide of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)

- Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009 (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Quotas of Silicon Carbide of 2009, Second Round (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Notice Regarding Passing Down the 2009 Second Batch Regular Trade Coke and Rare Earth Export Quota (Ministry of Commerce, shangzhihan (2009) No. 73, September 8, 2009)
- Notice Regarding Announcement of the 2010 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2009) No. 88, October 29, 2009)
- as well as any amendments or extensions; related measures; replacement measures; renewal measures; and implementing measures.

The United States considers that these measures are inconsistent with Article XI:1 of the GATT 1994 as well as China's obligations under the provisions of paragraph 1.2 of Part I of the *Protocol on the Accession of the People's Republic of China* (WT/L/432) ("Accession Protocol"), which incorporates commitments in paragraphs 162 and 165 of the *Working Party Report on the Accession of China* (WT/MIN(01)/3) ("Working Party Report").

II. Export Duties

China subjects the materials to export duties.

China imposes export duty rates, "temporary" export duty rates, and/or "special" export duty rates of various magnitudes on bauxite, coke, fluorspar, magnesium, silicon metal, yellow phosphorus, and zinc. These export duties are imposed either on materials that are not listed in Annex 6 of the Accession Protocol, or on materials that are listed in Annex 6 of the Accession Protocol, but at rates that exceed the maximum rates designated in Annex 6.

In addition, as discussed in Section III below, China allocates the quotas¹⁰ imposed on the exportation of bauxite, fluorspar, and silicon carbide through a bidding system. In connection with the administration of this bidding system, China requires enterprises to pay a charge in order to export these materials. However, bauxite, fluorspar, and silicon carbide are not listed in Annex 6 of the Accession Protocol.

The United States understands that these Chinese measures are reflected in, among others:

- Customs Law of the People's Republic of China (adopted at the 19th Meeting of the Standing Committee of the Sixth National People's Congress on January 22, 1987, amended July 8, 2000)

- Regulations of the People's Republic of China on Import and Export Duties (Order of the State Council (2003) No. 392, adopted at the 26th executive meeting of the State Council on October 29, 2003, January 1, 2004)
- Notice Regarding the 2009 Tariff Implementation Program (State Council Tariff Policy Commission, shuiweihui (2008) No. 40, January 1, 2009)
- Foreign Trade Law of the People's Republic of China (adopted at the 8th Session of the Standing Committee of the Tenth National People's Congress on April 6, 2004, promulgated on July 1, 2004)
- Regulation of the People's Republic of China on the Administration of the Import and Export of Goods (passed at the forty-sixth executive meeting of the State Council on October 31, 2001, January 1, 2002)
- Measures for the Administration of License for the Export of Goods (Order of the Ministry of Commerce (2008) No. 11, July 1, 2008)
- Measures of Quota Bidding for Export Commodities (Decree of the Ministry of Foreign Trade and Economic Cooperation No. 11, adopted on December 20, 2001, January 1, 2002)
- Implementation Rules of Export Quota Bidding for Industrial Products (Ministry of Foreign Trade and Economic Cooperation, November 8, 2001)
- Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2008) No. 83, January 1, 2009)
- Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009)
- Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009 (Ministry of Commerce, Announcement (2008) No. 85, October 30, 2008)
- Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009 (Ministry of Commerce, Announcement (2009) No. 42, June 9, 2009)
- Circular of the Ministry of Foreign Trade and Economic Cooperation on Distribution of the "Implementation Rules of Export Quota Bidding for Industrial Products" (Ministry of Foreign Trade and Economic Cooperation, issued on November 8, 2001)
- Quotas of Fluorspar Lump (Powder) of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Quotas of Bauxite of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 10, 2008)

¹⁰ Discussed in Section I above.

- Quotas of Silicon Carbide of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009 (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Quotas of Silicon Carbide of 2009, Second Round (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Notice Regarding Announcement of the 2010 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2009) No. 88, October 29, 2009)
- as well as any amendments or extensions; related measures; replacement measures; renewal measures; and implementing measures.

The United States considers that these measures are inconsistent with paragraph 11.3 of Part I of the Accession Protocol, as well as China's obligations under the provisions of paragraph 1.2 of Part I of the Accession Protocol, which incorporates commitments referred to in paragraph 342 of the Working Party Report.

657 III. Additional Restraints Imposed on Exportation

In addition to the export quotas and export duties discussed in Sections I and II above, China imposes other restraints on the exportation of the materials, administers its measures in a manner that is not uniform, impartial, and reasonable, imposes excessive fees and formalities on exportation, and does not publish certain measures pertaining to requirements, restrictions, or prohibitions on exports.

China administers the export quotas imposed on bauxite, coke, fluorspar, silicon carbide, and zinc discussed in Section I above, through its ministries and other organizations under the State Council as well as chambers of commerce and industry associations, in a manner that restricts exports and is not uniform, impartial and reasonable. In connection with the administration of the quotas for these materials, China imposes restrictions on the right of Chinese enterprises as well as foreign enterprises and individuals to export.

China allocates the export quotas imposed on bauxite, fluorspar, and silicon carbide discussed in Section I above, through a bidding system. China administers the requirements and procedures for this bidding system through its ministries and other organizations under the State Council as well as chambers of commerce and industry associations, in a manner that restricts exports and is not uniform, impartial and reasonable. In connection with the administration of this bidding system, China also requires foreign-invested enterprises to satisfy certain criteria in order to export these materials that Chinese enterprises need not satisfy. Further, China requires enterprises to pay a charge in order to export these materials that is excessive and imposes excessive formalities on the exportation of these materials.

China does not publish the amount for the export quota for zinc or any conditions or procedures for applying entities to qualify to export zinc.

In addition, China restricts the exportation of bauxite, coke, fluorspar, manganese, silicon carbide, and zinc by subjecting these materials to non-automatic licensing. China imposes the non-automatic export licensing for bauxite, coke, fluorspar, silicon carbide, and zinc in connection with the administration of the export quotas discussed in Section I, as an additional restraint on the exportation of those materials.

China also imposes quantitative restrictions on the exportation of the materials by requiring that prices for the materials meet or exceed a minimum price before they may be exported. Further, through its ministries and other organizations under the State Council as well as chambers of commerce and industry associations, China administers the price requirements in a manner that restricts exports and is not uniform, impartial, and reasonable. China also does not publish certain measures relating to these requirements in a manner that enables governments and traders to become acquainted with them.

The United States understands that these Chinese measures are reflected in, among others:

- Foreign Trade Law of the People's Republic of China (adopted at the 8th Session of the Standing Committee of the Tenth National People's Congress on April 6, 2004, promulgated on July 1, 2004)
- Regulation of the People's Republic of China on the Administration of the Import and Export of Goods (passed at the forty-sixth executive meeting of the State Council on October 31, 2001, January 1, 2002)
- Measures for the Administration of License for the Export of Goods (Order of the Ministry of Commerce (2008) No. 11, July 1, 2008)
- Measures for the Administration of Export Commodities Quotas (Order of the Ministry of Foreign Trade and Economic Cooperation No. 12, adopted on December 20, 2001, January 1, 2002)
- Measures of Quota Bidding for Export Commodities (Decree of the Ministry of Foreign Trade and Economic Cooperation No. 11, adopted on December 20, 2001, January 1, 2002)
- Measures for the Administration of the Organs for Issuing the Licenses of Import and Export Commodities (Ministry of Foreign Trade and Economic Cooperation, wajingmaopeiguanhanzi (1999) No. 68, September 21, 1999)
- Working Rules on Issuing Export Licenses (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)
- Rules on the Administration of Import and Export License Certificates (Ministry of Foreign Trade and Economic Cooperation, wajingmaopeizi (1999) No. 87, December 6, 1999)
- Implementation Rules of Export Quota Bidding for Industrial Products (Ministry of Foreign Trade and Economic Cooperation, November 8, 2001)

- Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2008) No. 83, January 1, 2009)
- Notice Regarding Passing Down the 2009 First Batch Regular Trade Coke Export Quota (Ministry of Commerce, shangmaohan (2008) No. 140, January 1, 2009)
- 2009 Coke Export Quota Declaration Conditions and Declaration Procedures (Ministry of Commerce, Notice (2008) No. 76, October 13, 2008)
- Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009)
- Announcement of the Ministry of Commerce Issuing the "2009 Graded License-Issuing List of Commodities Subject to Export License Administration" (Ministry of Commerce, Notice (2008) No. 124, January 1, 2009)
- Announcement Regarding Printing "Working Rules on Issuing Export Licenses" (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)
- Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009 (Ministry of Commerce, Announcement (2008) No. 85, October 30, 2008)
- Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009 (Ministry of Commerce, Announcement (2009) No. 42, June 9, 2009)
- Circular of the Ministry of Foreign Trade and Economic Cooperation on Distribution of the "Implementation Rules of Export Quota Bidding for Industrial Products" (Ministry of Foreign Trade and Economic Cooperation, issued on November 8, 2001)
- Quotas of Fluorspar Lump (Powder) of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Quotas of Bauxite of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 10, 2008)
- Quotas of Silicon Carbide of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009 (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Quotas of Silicon Carbide of 2009, Second Round (Committee for the Invitation for Bid for Export Commodity Quotas, September 16, 2009)

- Notice Regarding Passing Down the 2009 Second Batch Regular Trade Coke and Rare Earth Export Quota (Ministry of Commerce, ShangZiHan (2009) No. 73, September 8, 2009)
- Notice Regarding Announcement of the 2010 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2009) No. 88, October 29, 2009)
- Charter of the China Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters
- Charter of the China Coking Industry Association
- Measures for the Administration over Foreign Trade and Economic Social Organizations (Ministry of Foreign Trade and Economic Cooperation, February 26, 1991)
- Notice Regarding Printing and Distribution of Several Regulations for Personnel Management of Chambers of Commerce for Importers and Exporters (Ministry of Foreign Trade and Economic Cooperation, September 23, 1994)
- Interim Regulations of the Ministry of Foreign Trade and Economic Cooperation on Punishment for Conduct at Exporting at Lower-than-Normal Price (Ministry of Foreign Trade and Economic Cooperation, March 20, 1996)
- Notice Regarding Rules for Contract Declaration for Chemicals-Related Verification and Stamp Products (China Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters Petroleum and Chemicals Products Department, December 30, 2003)
- Online Verification and Certification Operating Steps (China Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters)
- Rules for Coordination with Respect to Customs Price Review of Export Products, (Ministry of Foreign Trade and Economic Cooperation guanzonghanzi No. 21, 1997)
- Notice of the Rules on Price Reviews of Export Products by the Customs, (Ministry of Foreign Trade and Economic Cooperation guanzonghanzi No. 21, 1997)
- Notice on the Issuance of "Various Provisions on the Strengthening of Export Product Coordination and Management" (Ministry of Foreign Economic Relations and Trade, jinshufa (1991) No. 52, February 22, 1991)
- "Various Provisions on the Strengthening of Export Product Coordination and Management" (Ministry of Foreign Economic Relations and Trade, jinshufa (1991) No. 52, February 22, 1991)
- Decision of the State Council on Various Questions on the Further Reform and Improvement of the Foreign Trade System (State Council, guofa (1990) No. 70, January 1, 1991)

- as well as any amendments or extensions; related measures; replacement measures; renewal measures; and implementing measures.

The United States considers that these measures are inconsistent with Article VIII:1(a) and VIII:4, Article X:1 and X:3(a), and Article XI:1 of the GATT 1994 and paragraphs 2(A)2, 5.1, 5.2 and 8.2 of Part I of the Accession Protocol, as well as China's obligations under the provisions of paragraph 1.2 of Part I of the Accession Protocol, which incorporates commitments in paragraphs 83, 84, 162, and 165 of the Working Party Report.

* * * * *

Accordingly, the United States respectfully requests that, pursuant to Article 6 of the DSU, the Dispute Settlement Body establish a panel to examine this matter, with the standard terms of reference as set out in Article 7.1 of the DSU.

ANNEX II

**WORLD TRADE
ORGANIZATION**

WT/DS395/7
9 November 2009
(09-5567)

Original: English

**CHINA – MEASURES RELATED TO THE EXPORTATION
OF VARIOUS RAW MATERIALS**

Request for the Establishment of a Panel by the European Communities

The following communication, dated 4 November 2009, from the delegation of the European Communities to the Chairman of the Dispute Settlement Body, is circulated pursuant to Article 6.2 of the DSU.

On 23 June 2009, the European Communities requested consultations with the Government of the People's Republic of China ("China") pursuant to Articles 1 and 4 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Article XXII of the *General Agreement on Tariffs and Trade 1994* ("GATT 1994") with respect to China's restraints on the exportation from China of various forms of bauxite¹, coke², fluorspar³, magnesium⁴, manganese⁵,

¹ Bauxite includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes, as listed in Attachment I of Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009) ("2009 Export Licensing List") and/or the following eight-digit HS numbers as listed in Table 7 of Notice Regarding the 2009 Tariff Implementation Program (State Council Tariff Policy Commission, shuweihui (2008) No. 40, January 1, 2009) ("2009 Export Duty List"): 2508300000/25083000, 2606000000/26060000, 26204000.

² Coke includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2704001000/27040010.

³ Fluorspar includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2529210000/25292100, 2529220000/25292200.

⁴ Magnesium includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 81041100, 81041900, 81042000.

⁵ Manganese includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 26020000, 8111001010/81110010, 8111001090/81110010.

silicon carbide⁶, silicon metal⁷, yellow phosphorus⁸, and zinc⁹ (the "materials"). The European Communities held consultations with China on July 31, 2009, and September 1-2, 2009. Those consultations unfortunately did not resolve the dispute.

I. Export Quotas

China subjects the exportation of bauxite, coke, fluorspar, silicon carbide, and zinc to quantitative restrictions such as quotas.

The European Communities understands that these Chinese measures are reflected in, among others:

- Foreign Trade Law of the People's Republic of China (adopted at the 8th Session of the Standing Committee of the Tenth National People's Congress on April 6, 2004, promulgated on July 1, 2004)
- Regulation of the People's Republic of China on the Administration of the Import and Export of Goods (passed at the forty-sixth executive meeting of the State Council on October 31, 2001, January 1, 2002)
- Measures for the Administration of License for the Export of Goods (Order of the Ministry of Commerce (2008) No. 11, July 1, 2008)
- Measures for the Administration of Export Commodities Quotas (Order of the Ministry of Foreign Trade and Economic Cooperation No. 12, adopted on December 20, 2001, January 1, 2002)
- Measures of Quota Bidding for Export Commodities (Decree of the Ministry of Foreign Trade and Economic Cooperation No. 11, adopted on December 20, 2001, January 1, 2002)
- Measures for the Administration of the Organs for Issuing the Licenses of Import and Export Commodities (Ministry of Foreign Trade and Economic Cooperation, wajingmaopeiguanhanzi (1999) No. 68, September 21, 1999)
- Implementation Rules of Export Quota Bidding for Industrial Products (Ministry of Foreign Trade and Economic Cooperation, November 8, 2001)

⁶ Silicon carbide includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2849200000, 3824909910.

⁷ Silicon metal includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 28046900.

⁸ Yellow phosphorus includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 28047010.

⁹ Zinc includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2608000001/26080000, 2608000090/26080000, 790111111000/7901111100, 7901119000/79011190, 7901120000/79011200, 7901200000/79012000, 79020000, 26201100, 26201900.

- Working Rules on Issuing Export Licenses (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)
- Rules on the Administration of Import and Export License Certificates (Ministry of Foreign Trade and Economic Cooperation, wajingmaopeizi (1999) No. 87, December 6, 1999)
- Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2008) No. 83, January 1, 2009)
- Notice Regarding Passing Down the 2009 First Batch Regular Trade Coke Export Quota (Ministry of Commerce, shangmaohan (2008) No. 140, January 1, 2009)
- 2009 Coke Export Quota Declaration Conditions and Declaration Procedures (Ministry of Commerce, Notice (2008) No. 76, October 13, 2008)
- Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009)
- Announcement of the Ministry of Commerce Issuing the "2009 Graded License-Issuing List of Commodities Subject to Export License Administration" (Ministry of Commerce, Notice (2008) No. 124, January 1, 2009)
- Announcement Regarding Printing "Working Rules on Issuing Export Licenses" (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)
- Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009 (Ministry of Commerce, Announcement (2008) No. 85, October 30, 2008)
- Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009 (Ministry of Commerce, Announcement (2009) No. 42, June 9, 2009)
- Circular of the Ministry of Foreign Trade and Economic Cooperation on Distribution of the "Implementation Rules of Export Quota Bidding for Industrial Products" (Ministry of Foreign Trade and Economic Cooperation, issued on November 8, 2001)
- Quotas of Fluorspar Lump (Powder) of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Quotas of Bauxite of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 10, 2008)
- Quotas of Silicon Carbide of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)

- Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009 (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Quotas of Silicon Carbide of 2009, Second Round (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Notice Regarding Passing Down the 2009 Second Batch Regular Trade Coke and Rare Earth Export Quota (Ministry of Commerce, shangzhihan (2009) No. 73, September 8, 2009)
- Notice Regarding Announcement of the 2010 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2009) No. 88, October 29, 2009)
- as well as any amendments or extensions; related measures; replacement measures; renewal measures; and implementing measures.

The European Communities considers that these measures are inconsistent with Article XI:1 of the GATT 1994 as well as China's obligations under the provisions of paragraph 1.2 of Part I of the *Protocol on the Accession of the People's Republic of China* (WT/L/432) ("Accession Protocol"), which incorporates commitments in paragraphs 162 and 165 of the *Working Party Report on the Accession of China* (WT/MIN(01)/3) ("Working Party Report").

II. Export Duties

China subjects the materials to export duties.

China imposes export duty rates, "temporary" export duty rates, and/or "special" export duty rates of various magnitudes on bauxite, coke, fluorspar, magnesium, manganese, silicon metal, yellow phosphorus, and zinc. These export duties are imposed either on materials that are not listed in Annex 6 of the Accession Protocol, or on materials that are listed in Annex 6 of the Accession Protocol, but at rates that exceed the maximum rates designated in Annex 6.

In addition, China allocates the quotas¹⁰ imposed on the exportation of bauxite, fluorspar, and silicon carbide through a bidding system. In connection with the administration of this bidding system, China requires enterprises to pay a charge in order to export these materials. However, bauxite, fluorspar, and silicon carbide are not listed in Annex 6 of the Accession Protocol.

The European Communities understands that these Chinese measures are reflected in, among others:

- Customs Law of the People's Republic of China (adopted at the 19th Meeting of the Standing Committee of the Sixth National People's Congress on January 22, 1987, amended July 8, 2000)

- Regulations of the People's Republic of China on Import and Export Duties (Order of the State Council (2003) No. 392, adopted at the 26th executive meeting of the State Council on October 29, 2003, January 1, 2004)
- Notice Regarding the 2009 Tariff Implementation Program (State Council Tariff Policy Commission, shuiweihui (2008) No. 40, January 1, 2009)
- Foreign Trade Law of the People's Republic of China (adopted at the 8th Session of the Standing Committee of the Tenth National People's Congress on April 6, 2004, promulgated on July 1, 2004)
- Regulation of the People's Republic of China on the Administration of the Import and Export of Goods (passed at the forty-sixth executive meeting of the State Council on October 31, 2001, January 1, 2002)
- Measures for the Administration of License for the Export of Goods (Order of the Ministry of Commerce (2008) No. 11, July 1, 2008)
- Measures of Quota Bidding for Export Commodities (Decree of the Ministry of Foreign Trade and Economic Cooperation No. 11, adopted on December 20, 2001, January 1, 2002)
- Implementation Rules of Export Quota Bidding for Industrial Products (Ministry of Foreign Trade and Economic Cooperation, November 8, 2001)
- Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2008) No. 83, January 1, 2009)
- Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009)
- Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009 (Ministry of Commerce, Announcement (2008) No. 85, October 30, 2008)
- Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009 (Ministry of Commerce, Announcement (2009) No. 42, June 9, 2009)
- Circular of the Ministry of Foreign Trade and Economic Cooperation on Distribution of the "Implementation Rules of Export Quota Bidding for Industrial Products" (Ministry of Foreign Trade and Economic Cooperation, issued on November 8, 2001)
- Quotas of Fluorspar Lump (Powder) of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Quotas of Bauxite of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 10, 2008)

¹⁰ Discussed in Section I above.

- Quotas of Silicon Carbide of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009 (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Quotas of Silicon Carbide of 2009, Second Round (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Notice Regarding Announcement of the 2010 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2009) No. 88, October 29, 2009)
- as well as any amendments or extensions; related measures; replacement measures; renewal measures; and implementing measures.

The European Communities considers that these measures are inconsistent with paragraph 11.3 of Part I of the Accession Protocol, as well as China's obligations under the provisions of paragraph 1.2 of Part I of the Accession Protocol, which incorporates commitments referred to in paragraph 342 of the Working Party Report.

III. Additional Restraints Imposed on Exportation

In addition to the export quotas and export duties discussed in Sections I and II above, China imposes other restraints on the exportation of the materials, administers its measures in a manner that is not uniform, impartial, and reasonable, imposes excessive fees and formalities on exportation, and does not publish certain measures pertaining to requirements, restrictions, or prohibitions on exports.

China administers the export quotas imposed on bauxite, coke, fluorspar, silicon carbide, and zinc discussed in Section I above, through its ministries and other organisations under the State Council as well as chambers of commerce and industry associations, in a manner that restricts exports and is not uniform, impartial and reasonable. In connection with the administration of the quotas for these materials, China imposes restrictions on the right of Chinese enterprises as well as foreign enterprises and individuals to export.

China allocates the export quotas imposed on bauxite, fluorspar, and silicon carbide discussed in Section I above, through a bidding system. China administers the requirements and procedures for this bidding system through its ministries and other organisations under the State Council as well as chambers of commerce and industry associations, in a manner that restricts exports and is not uniform, impartial and reasonable. In connection with the administration of this bidding system, China also requires foreign-invested enterprises to satisfy certain criteria in order to export these materials that Chinese enterprises need not satisfy.

China does not publish the amount for the export quota for zinc or any conditions or procedures for applying entities to qualify to export zinc.

In addition, China restricts the exportation of bauxite, coke, fluorspar, manganese, silicon carbide, and zinc by subjecting these materials to non-automatic licensing. China imposes the non-automatic export licensing for bauxite, coke, fluorspar, silicon carbide, and zinc in connection with

the administration of the export quotas discussed in Section I, as an additional restraint on the exportation of those materials.

China also imposes quantitative restrictions on the exportation of the materials by requiring that prices for the materials meet or exceed a minimum price before they may be exported. Further, through its ministries and other organisations under the State Council as well as chambers of commerce and industry associations, China administers the price requirements in a manner that restricts exports and is not uniform, impartial, and reasonable. China also does not publish certain measures relating to these requirements in a manner that enables governments and traders to become acquainted with them.

China also imposes excessive fees and formalities in relation to the exportation of the materials.

The European Communities understands that these Chinese measures are reflected in, among others:

- Foreign Trade Law of the People's Republic of China (adopted at the 8th Session of the Standing Committee of the Tenth National People's Congress on April 6, 2004, promulgated on July 1, 2004)
- Regulation of the People's Republic of China on the Administration of the Import and Export of Goods (passed at the forty-sixth executive meeting of the State Council on October 31, 2001, January 1, 2002)
- Measures for the Administration of License for the Export of Goods (Order of the Ministry of Commerce (2008) No. 11, July 1, 2008)
- Measures for the Administration of Export Commodities Quotas (Order of the Ministry of Foreign Trade and Economic Cooperation No. 12, adopted on December 20, 2001, January 1, 2002)
- Measures of Quota Bidding for Export Commodities (Decree of the Ministry of Foreign Trade and Economic Cooperation No. 11, adopted on December 20, 2001, January 1, 2002)
- Measures for the Administration of the Organs for Issuing the Licenses of Import and Export Commodities (Ministry of Foreign Trade and Economic Cooperation, wajingmaopeiguanhanzi (1999) No. 68, September 21, 1999)
- Working Rules on Issuing Export Licenses (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)
- Rules on the Administration of Import and Export License Certificates (Ministry of Foreign Trade and Economic Cooperation, wajingmaopeizi (1999) No. 87, December 6, 1999)
- Implementation Rules of Export Quota Bidding for Industrial Products (Ministry of Foreign Trade and Economic Cooperation, November 8, 2001)

- Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2008) No. 83, January 1, 2009)
- Notice Regarding Passing Down the 2009 First Batch Regular Trade Coke Export Quota (Ministry of Commerce, shangmaohan (2008) No. 140, January 1, 2009)
- 2009 Coke Export Quota Declaration Conditions and Declaration Procedures (Ministry of Commerce, Notice (2008) No. 76, October 13, 2008)
- Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009)
- Announcement of the Ministry of Commerce Issuing the "2009 Graded License-Issuing List of Commodities Subject to Export License Administration" (Ministry of Commerce, Notice (2008) No. 124, January 1, 2009)
- Announcement Regarding Printing "Working Rules on Issuing Export Licenses" (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)
- Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009 (Ministry of Commerce, Announcement (2008) No. 85, October 30, 2008)
- Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009 (Ministry of Commerce, Announcement (2009) No. 42, June 9, 2009)
- Circular of the Ministry of Foreign Trade and Economic Cooperation on Distribution of the "Implementation Rules of Export Quota Bidding for Industrial Products" (Ministry of Foreign Trade and Economic Cooperation, issued on November 8, 2001)
- Quotas of Fluorspar Lump (Powder) of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Quotas of Bauxite of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 10, 2008)
- Quotas of Silicon Carbide of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009 (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Quotas of Silicon Carbide of 2009, Second Round (Committee for the Invitation for Bid for Export Commodity Quotas, September 16, 2009)

- Notice Regarding Passing Down the 2009 Second Batch Regular Trade Coke and Rare Earth Export Quota (Ministry of Commerce, ShangZiHan (2009) No. 73, September 8, 2009)
- Notice Regarding Announcement of the 2010 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2009) No. 88, October 29, 2009)
- Charter of the China Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters
- Charter of the China Coking Industry Association
- Measures for the Administration over Foreign Trade and Economic Social Organizations (Ministry of Foreign Trade and Economic Cooperation, February 26, 1991)
- Notice Regarding Printing and Distribution of Several Regulations for Personnel Management of Chambers of Commerce for Importers and Exporters (Ministry of Foreign Trade and Economic Cooperation, September 23, 1994)
- Interim Regulations of the Ministry of Foreign Trade and Economic Cooperation on Punishment for Conduct at Exporting at Lower-than-Normal Price (Ministry of Foreign Trade and Economic Cooperation, March 20, 1996)
- Notice Regarding Rules for Contract Declaration for Chemicals-Related Verification and Stamp Products (China Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters Petroleum and Chemicals Products Department, December 30, 2003)
- Online Verification and Certification Operating Steps (China Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters)
- Rules for Coordination with Respect to Customs Price Review of Export Products, (Ministry of Foreign Trade and Economic Cooperation guanzonghanzi No. 21, 1997)
- Notice of the Rules on Price Reviews of Export Products by the Customs, (Ministry of Foreign Trade and Economic Cooperation guanzonghanzi No. 21, 1997)
- Notice on the Issuance of "Various Provisions on the Strengthening of Export Product Coordination and Management" (Ministry of Foreign Economic Relations and Trade, jinchufa (1991) No. 52, February 22, 1991)
- "Various Provisions on the Strengthening of Export Product Coordination and Management" (Ministry of Foreign Economic Relations and Trade, jinchufa (1991) No. 52, February 22, 1991)
- Decision of the State Council on Various Questions on the Further Reform and Improvement of the Foreign Trade System (State Council, guofa (1990) No. 70, January 1, 1991)

- as well as any amendments or extensions; related measures; replacement measures; renewal measures; and implementing measures.

The European Communities considers that these measures are inconsistent with Article VIII:1 and VIII:4, Article X:1 and X:3(a), and Article XI:1 of the GATT 1994 and paragraphs 2(A)2, 5.1, 5.2 and 8.2 of Part I of the Accession Protocol, as well as China's obligations under the provisions of paragraph 1.2 of Part I of the Accession Protocol, which incorporates commitments in paragraphs 83, 84, 162, and 165 of the Working Party Report.

* * * * *

Accordingly, the European Communities respectfully requests that, pursuant to Article 6 of the DSU, the Dispute Settlement Body establish a panel to examine this matter, with the standard terms of reference as set out in Article 7.1 of the DSU.

The European Communities asks that this request be placed on the agenda for the meeting of the Dispute Settlement Body to be held on 19 November 2009.

ANNEX III

WORLD TRADE ORGANIZATION

WT/DS398/6
9 November 2009
(09-5568)

Original: English

CHINA – MEASURES RELATED TO THE EXPORTATION OF VARIOUS RAW MATERIALS

Request for the Establishment of a Panel by Mexico

The following communication, dated 4 November 2009, from the delegation of Mexico to the Chairman of the Dispute Settlement Body, is circulated pursuant to Article 6.2 of the DSU.

On 21 August 2009, Mexico requested consultations with the Government of the People's Republic of China ("China") pursuant to Articles 1 and 4 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Article XXII of the *General Agreement on Tariffs and Trade 1994* ("GATT 1994") with respect to China's restraints on the exportation from China of various forms of bauxite¹, coke², fluorspar³, magnesium⁴, manganese⁵, silicon carbide⁶, silicon metal⁷, yellow phosphorus⁸, and zinc⁹ (the "materials"). Mexico held

¹ Bauxite includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes, as listed in Attachment 1 of Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009) ("2009 Export Licensing List") and/or the following eight-digit HS numbers as listed in Table 7 of Notice Regarding the 2009 Tariff Implementation Program (State Council Tariff Policy Commission, shuweiwei (2008) No. 40, January 1, 2009) ("2009 Export Duty List"): 2508300000/25083000, 2606000000/260600000, 26204000.

² Coke includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2704001000/27040010.

³ Fluorspar includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2529210000/25292100, 2529220000/25292200.

⁴ Magnesium includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 81041100, 81041900, 81042000.

⁵ Manganese includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 26020000, 8111001010/81110010, 8111001090/81110010.

⁶ Silicon carbide includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2849200000, 3824909910.

consultations with China on September 1-2, 2009. Those consultations unfortunately did not resolve the dispute.

I. Export Quotas

China subjects the exportation of bauxite, coke, fluorspar, silicon carbide, and zinc to quantitative restrictions such as quotas.

Mexico understands that these Chinese measures are reflected in, among others:

- Foreign Trade Law of the People's Republic of China (adopted at the 8th Session of the Standing Committee of the Tenth National People's Congress on April 6, 2004, promulgated on July 1, 2004)
- Regulation of the People's Republic of China on the Administration of the Import and Export of Goods (passed at the forty-sixth executive meeting of the State Council on October 31, 2001, January 1, 2002)
- Measures for the Administration of License for the Export of Goods (Order of the Ministry of Commerce (2008) No. 11, July 1, 2008)
- Measures for the Administration of Export Commodities Quotas (Order of the Ministry of Foreign Trade and Economic Cooperation No. 12, adopted on December 20, 2001, January 1, 2002)
- Measures of Quota Bidding for Export Commodities (Decree of the Ministry of Foreign Trade and Economic Cooperation No. 11, adopted on December 20, 2001, January 1, 2002)
- Measures for the Administration of the Organs for Issuing the Licenses of Import and Export Commodities (Ministry of Foreign Trade and Economic Cooperation, wajingmaopeiguanhanzi (1999) No. 68, September 21, 1999)
- Implementation Rules of Export Quota Bidding for Industrial Products (Ministry of Foreign Trade and Economic Cooperation, November 8, 2001)
- Working Rules on Issuing Export Licenses (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)

⁷ Silicon metal includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 28046900.

⁸ Yellow phosphorus includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 28047010.

⁹ Zinc includes but is not limited to items falling under the following ten-digit Chinese Commodity Codes as listed in the 2009 Export Licensing List and/or the eight-digit HS numbers as listed in the 2009 Export Duty List: 2608000001/260800000, 2608000090/260800000, 790111111000/7901111100, 7901119000/79011190, 7901120000/79011200, 7901200000/79012000, 79020000, 26201100, 26201900.

- Rules on the Administration of Import and Export License Certificates (Ministry of Foreign Trade and Economic Cooperation, wajingmaopeizi (1999) No. 87, December 6, 1999)
- Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2008) No. 83, January 1, 2009)
- Notice Regarding Passing Down the 2009 First Batch Regular Trade Coke Export Quota (Ministry of Commerce, shangmaohan (2008) No. 140, January 1, 2009)
- 2009 Coke Export Quota Declaration Conditions and Declaration Procedures (Ministry of Commerce, Notice (2008) No. 76, October 13, 2008)
- Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009)
- Announcement of the Ministry of Commerce Issuing the "2009 Graded License-Issuing List of Commodities Subject to Export License Administration" (Ministry of Commerce, Notice (2008) No. 124, January 1, 2009)
- Announcement Regarding Printing "Working Rules on Issuing Export Licenses" (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)
- Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009 (Ministry of Commerce, Announcement (2008) No. 85, October 30, 2008)
- Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009 (Ministry of Commerce, Announcement (2009) No. 42, June 9, 2009)
- Circular of the Ministry of Foreign Trade and Economic Cooperation on Distribution of the "Implementation Rules of Export Quota Bidding for Industrial Products" (Ministry of Foreign Trade and Economic Cooperation, issued on November 8, 2001)
- Quotas of Fluorspar Lump (Powder) of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Quotas of Bauxite of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 10, 2008)
- Quotas of Silicon Carbide of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009 (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)

- Quotas of Silicon Carbide of 2009, Second Round (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Notice Regarding Passing Down the 2009 Second Batch Regular Trade Coke and Rare Earth Export Quota (Ministry of Commerce, shangzhizhan (2009) No. 73, September 8, 2009)
- Notice Regarding Announcement of the 2010 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2009) No. 88, October 29, 2009)
- As well as any amendments or extensions; related measures; replacement measures; renewal measures; and implementing measures.

Mexico considers that these measures are inconsistent with Article XI:1 of the GATT 1994 as well as China's obligations under the provisions of paragraph 1.2 of Part I of the *Protocol on the Accession of the People's Republic of China* (WT/L/432) ("Accession Protocol"), which incorporates commitments in paragraphs 162 and 165 of the *Working Party Report on the Accession of China* (WT/MIN(01)/3) ("Working Party Report").

II. Export Duties

China subjects the materials to export duties.

China imposes export duty rates, "temporary" export duty rates, and/or "special" export duty rates of various magnitudes on bauxite, coke, fluorspar, magnesium, manganese, silicon metal, yellow phosphorus, and zinc. These export duties are imposed either on materials that are not listed in Annex 6 of the Accession Protocol, or on materials that are listed in Annex 6 of the Accession Protocol, but at rates that exceed the maximum rates designated in Annex 6.

In addition, as discussed in Section III below, China allocates the quotas¹⁰ imposed on the exportation of bauxite, fluorspar, and silicon carbide through a bidding system. In connection with the administration of this bidding system, China requires enterprises to pay a charge in order to export these materials. However, bauxite, fluorspar, and silicon carbide are not listed in Annex 6 of the Accession Protocol.

Mexico understands that these Chinese measures are reflected in, among others:

- Customs Law of the People's Republic of China (adopted at the 19th Meeting of the Standing Committee of the Sixth National People's Congress on January 22, 1987, amended July 8, 2000)
- Regulations of the People's Republic of China on Import and Export Duties (Order of the State Council (2003) No. 392, adopted at the 26th executive meeting of the State Council on October 29, 2003, January 1, 2004)
- Notice Regarding the 2009 Tariff Implementation Program (State Council Tariff Policy Commission, shuiweihui (2008) No. 40, January 1, 2009)

- Foreign Trade Law of the People's Republic of China (adopted at the 8th Session of the Standing Committee of the Tenth National People's Congress on April 6, 2004, promulgated on July 1, 2004)
- Regulation of the People's Republic of China on the Administration of the Import and Export of Goods (passed at the forty-sixth executive meeting of the State Council on October 31, 2001, January 1, 2002)
- Measures for the Administration of License for the Export of Goods (Order of the Ministry of Commerce (2008) No. 11, July 1, 2008)
- Measures of Quota Bidding for Export Commodities (Decree of the Ministry of Foreign Trade and Economic Cooperation No. 11, adopted on December 20, 2001, January 1, 2002)
- Implementation Rules of Export Quota Bidding for Industrial Products (Ministry of Foreign Trade and Economic Cooperation, November 8, 2001)
- Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2008) No. 83, January 1, 2009)
- Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009)
- Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009 (Ministry of Commerce, Announcement (2008) No. 85, October 30, 2008)
- Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009 (Ministry of Commerce, Announcement (2009) No. 42, June 9, 2009)
- Circular of the Ministry of Foreign Trade and Economic Cooperation on Distribution of the "Implementation Rules of Export Quota Bidding for Industrial Products" (Ministry of Foreign Trade and Economic Cooperation, issued on November 8, 2001)
- Quotas of Fluorspar Lump (Powder) of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Quotas of Bauxite of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 10, 2008)
- Quotas of Silicon Carbide of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009 (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)

¹⁰ Discussed in Section I above.

- Quotas of Silicon Carbide of 2009, Second Round (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Notice Regarding Announcement of the 2010 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2009) No. 88, October 29, 2009)
- As well as any amendments or extensions; related measures; replacement measures; renewal measures; and implementing measures.

Mexico considers that these measures are inconsistent with paragraph 11.3 of Part I of the Accession Protocol, as well as China's obligations under the provisions of paragraph 1.2 of Part I of the Accession Protocol, which incorporates commitments referred to in paragraph 342 of the Working Party Report.

III. Additional Restraints Imposed on Exportation

In addition to the export quotas and export duties discussed in Sections I and II above, China imposes other restraints on the exportation of the materials, administers its measures in a manner that is not uniform, impartial, and reasonable, imposes excessive fees and formalities on exportation, and does not publish certain measures pertaining to requirements, restrictions, or prohibitions on exports.

China administers the export quotas imposed on bauxite, coke, fluorspar, silicon carbide, and zinc discussed in Section I above, through its ministries and other organizations under the State Council as well as chambers of commerce and industry associations, in a manner that restricts exports and is not uniform, impartial and reasonable. In connection with the administration of the quotas for these materials, China imposes restrictions on the right of Chinese enterprises as well as foreign enterprises and individuals to export.

China allocates the export quotas imposed on bauxite, fluorspar, and silicon carbide discussed in Section I above, through a bidding system. China administers the requirements and procedures for this bidding system through its ministries and other organizations under the State Council as well as chambers of commerce and industry associations, in a manner that restricts exports and is not uniform, impartial and reasonable. In connection with the administration of this bidding system, China also requires foreign-invested enterprises to satisfy certain criteria in order to export these materials that Chinese enterprises need not satisfy. Further, China requires enterprises to pay a charge in order to export these materials that is excessive and imposes excessive formalities on the exportation of these materials.

China does not publish the amount for the export quota for zinc or any conditions or procedures for applying entities to qualify to export zinc.

In addition, China restricts the exportation of bauxite, coke, fluorspar, manganese, silicon carbide, and zinc by subjecting these materials to non-automatic licensing. China imposes the non-automatic export licensing for bauxite, coke, fluorspar, silicon carbide, and zinc in connection with the administration of the export quotas discussed in Section I, as an additional restraint on the exportation of those materials.

China also imposes quantitative restrictions on the exportation of the materials by requiring that prices for the materials meet or exceed a minimum price before they may be exported. Further, through its ministries and other organizations under the State Council as well as chambers of commerce and industry associations, China administers the price requirements in a manner that restricts exports and is not uniform, impartial, and reasonable. China also does not publish certain measures relating to these requirements in a manner that enables governments and traders to become acquainted with them.

Mexico understands that these Chinese measures are reflected in, among others:

- Foreign Trade Law of the People's Republic of China (adopted at the 8th Session of the Standing Committee of the Tenth National People's Congress on April 6, 2004, promulgated on July 1, 2004)
- Regulation of the People's Republic of China on the Administration of the Import and Export of Goods (passed at the forty-sixth executive meeting of the State Council on October 31, 2001, January 1, 2002)
- Measures for the Administration of License for the Export of Goods (Order of the Ministry of Commerce (2008) No. 11, July 1, 2008)
- Measures for the Administration of Export Commodities Quotas (Order of the Ministry of Foreign Trade and Economic Cooperation No. 12, adopted on December 20, 2001, January 1, 2002)
- Measures of Quota Bidding for Export Commodities (Decree of the Ministry of Foreign Trade and Economic Cooperation No. 11, adopted on December 20, 2001, January 1, 2002)
- Measures for the Administration of the Organs for Issuing the Licenses of Import and Export Commodities (Ministry of Foreign Trade and Economic Cooperation, wajingmaopeiguanhanzi (1999) No. 68, September 21, 1999)
- Working Rules on Issuing Export Licenses (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)
- Rules on the Administration of Import and Export License Certificates (Ministry of Foreign Trade and Economic Cooperation, wajingmaopeizi (1999) No. 87, December 6, 1999)
- Implementation Rules of Export Quota Bidding for Industrial Products (Ministry of Foreign Trade and Economic Cooperation, November 8, 2001)
- Notice Regarding 2009 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2008) No. 83, January 1, 2009)
- Notice Regarding Passing Down the 2009 First Batch Regular Trade Coke Export Quota (Ministry of Commerce, shangmaohan (2008) No. 140, January 1, 2009)

- 2009 Coke Export Quota Declaration Conditions and Declaration Procedures (Ministry of Commerce, Notice (2008) No. 76, October 13, 2008)
- Notice "2009 Export Licensing Management Commodities List" (Ministry of Commerce and General Administration of Customs, Notice (2008) No. 100, January 1, 2009)
- Announcement of the Ministry of Commerce Issuing the "2009 Graded License-Issuing List of Commodities Subject to Export License Administration" (Ministry of Commerce, Notice (2008) No. 124, January 1, 2009)
- Announcement Regarding Printing "Working Rules on Issuing Export Licenses" (Ministry of Commerce, shangpeifa (2008) No. 398, October 9, 2008)
- Announcement of Ministry of Commerce on Matters regarding the First Bidding for Export Quotas of Industrial Products in 2009 (Ministry of Commerce, Announcement (2008) No. 85, October 30, 2008)
- Announcement of Ministry of Commerce on the Notice for the Second Invitation for the Bidding for Industrial Product Export Quotas in 2009 (Ministry of Commerce, Announcement (2009) No. 42, June 9, 2009)
- Circular of the Ministry of Foreign Trade and Economic Cooperation on Distribution of the "Implementation Rules of Export Quota Bidding for Industrial Products" (Ministry of Foreign Trade and Economic Cooperation, issued on November 8, 2001)
- Quotas of Fluorspar Lump (Powder) of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Quotas of Bauxite of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 10, 2008)
- Quotas of Silicon Carbide of 2009 (Committee for the Invitation for bid for Export Commodity Quotas, December 11, 2008)
- Announcement on the Second Invitation for the Bidding of Select Industrial Product Export Quotas in 2009 (Committee for the Invitation for bid for Export Commodity Quotas, September 16, 2009)
- Quotas of Silicon Carbide of 2009, Second Round (Committee for the Invitation for Bid for Export Commodity Quotas, September 16, 2009)
- Notice Regarding Passing Down the 2009 Second Batch Regular Trade Coke and Rare Earth Export Quota (Ministry of Commerce, ShangZiHan (2009) No. 73, September 8, 2009)
- Notice Regarding Announcement of the 2010 Export Quota Amounts for Agricultural and Industrial Products (Ministry of Commerce, Notice (2009) No. 88, October 29, 2009)

- Charter of the China Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters
 - Charter of the China Coking Industry Association
 - Measures for the Administration over Foreign Trade and Economic Social Organizations (Ministry of Foreign Trade and Economic Cooperation, February 26, 1991)
 - Notice Regarding Printing and Distribution of Several Regulations for Personnel Management of Chambers of Commerce for Importers and Exporters (Ministry of Foreign Trade and Economic Cooperation, September 23, 1994)
 - Interim Regulations of the Ministry of Foreign Trade and Economic Cooperation on Punishment for Conduct at Exporting at Lower-than-Normal Price (Ministry of Foreign Trade and Economic Cooperation, March 20, 1996)
 - Notice Regarding Rules for Contract Declaration for Chemicals-Related Verification and Stamp Products (China Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters Petroleum and Chemicals Products Department, December 30, 2003)
 - Online Verification and Certification Operating Steps (China Chamber of Commerce of Metals, Minerals and Chemicals Importers and Exporters)
 - Rules for Coordination with Respect to Customs Price Review of Export Products, (Ministry of Foreign Trade and Economic Cooperation guanzonghanzi No. 21, 1997)
 - Notice of the Rules on Price Reviews of Export Products by the Customs, (Ministry of Foreign Trade and Economic Cooperation guanzonghanzi No. 21, 1997)
 - Notice on the Issuance of "Various Provisions on the Strengthening of Export Product Coordination and Management" (Ministry of Foreign Economic Relations and Trade, jinchufa (1991) No. 52, February 22, 1991)
 - "Various Provisions on the Strengthening of Export Product Coordination and Management" (Ministry of Foreign Economic Relations and Trade, jinchufa (1991) No. 52, February 22, 1991)
 - Decision of the State Council on Various Questions on the Further Reform and Improvement of the Foreign Trade System (State Council, guofa (1990) No. 70, January 1, 1991)
 - As well as any amendments or extensions; related measures; replacement measures; renewal measures; and implementing measures.
- Mexico considers that these measures are inconsistent with Article VIII:1(a) and VIII:4, Article X:1 and X:3(a), and Article XI:1 of the GATT 1994 and paragraphs 2(A)2, 5.1, 5.2 and 8.2 of Part I of the Accession Protocol, as well as China's obligations under the provisions of paragraph 1.2

of Part I of the Accession Protocol, which incorporates commitments in paragraphs 83, 84, 162, and 165 of the Working Party Report.

Accordingly, Mexico respectfully requests that, pursuant to Article 6 of the DSU, the Dispute Settlement Body establish a panel to examine this matter, with the standard terms of reference as set out in Article 7.1 of the DSU.

ANNEX IV

**WORLD TRADE
ORGANIZATION**

WT/DS394/11
WT/DS395/11
WT/DS398/10
2 September 2011
(11-4301)

Original: English

**CHINA – MEASURES RELATED TO THE EXPORTATION
OF VARIOUS RAW MATERIALS**

Notification of an Appeal by China under Article 16.4 and Article 17
of the Understanding on Rules and Procedures Governing the
Settlement of Disputes (DSU), and under Rule 20(1)
of the *Working Procedures for Appellate Review*

The following notification, dated 31 August 2011, from the Delegation of the People's Republic of China, is being circulated to Members.

1. Pursuant to Articles 16.4 and 17 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 20 of the *Working Procedures for Appellate Review* (WT/AB/WP/6, 16 August 2010), the People's Republic of China ("China") hereby notifies the Dispute Settlement Body ("DSB") of its decision to appeal certain issues of law and legal interpretations in the Panel Reports in *China – Measures Related to the Exportation of Various Raw Materials* (WT/DS394, WT/DS395, WT/DS398) ("Panel Report"). As set out in this notice of appeal, and pursuant to Article 17.13 of the DSU, China requests that the Appellate Body reverse or modify various legal findings and conclusions of the Panel, as a result of the errors identified below.
2. Pursuant to Rule 20(2)(d)(iii) of the *Working Procedures for Appellate Review*, this notice of appeal includes an indicative list of the paragraphs of the Panel Report containing the alleged errors, without prejudice to China's ability to refer to other paragraphs of the Panel Report in the context of its appeal.
- I. **APPEAL OF THE PANEL'S FINDING THAT SECTION III OF THE COMPLAINANTS' PANEL REQUESTS "PRESENTS THE PROBLEM CLEARLY" BY PROVIDING SUFFICIENT CONNECTIONS BETWEEN THE 37 LISTED MEASURES AND THE 13 LISTED TREATY PROVISIONS**
3. The Panel erred in its interpretation and application of Article 6.2 of the DSU, in finding, in paragraph 77 of its Second Preliminary Ruling of 1 October 2010 and paragraph 7.3(b) of the Panel

Report, that Section III of the Complainants' Panel Requests¹ complies with the requirement to "provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly".

4. China requests that the Appellate Body reverse this finding, and find that Section III of the Panel Requests does not comply with Article 6.2 of the DSU, with the exception of the Complainants' claims under Article X:1 of the GATT 1994 regarding non-publication of measures concerning zinc.

5. As a consequence of this reversal, China also requests that the Appellate Body reverse the Panel findings regarding claims purportedly made by the Complainants on the basis of Section III of the Panel Requests, including the findings in paragraphs 7.669; 7.670; 7.678; 7.756; 7.807; 7.958; 7.1082; 7.1102; 7.1103; 8.4(a)-(b); 8.5(b); 8.6 (a)-(b); 8.11(a), (c), (e) and (f); 8.12(b); 8.13(a)-(b); 8.18(a)-(b); 8.19(b) and 8.20(a)-(b) of the Panel Report.

II. APPEAL OF THE PANEL'S DECISION TO MAKE RECOMMENDATIONS WITH RESPECT TO THE "SERIES OF MEASURES" THAT HAVE AN ONGOING EFFECT THROUGH ANNUAL REPLACEMENT MEASURES

6. China appeals the Panel's recommendations in paragraphs 8.8; 8.15 and 8.22 of the Panel Report that China must bring its export duty and quota measures into conformity with its WTO obligations, to the extent that the Panel's recommendations apply to annual replacement measures regarding export quotas and export duties on products at issue in these disputes.

7. In making recommendations extending to measures excluded from the dispute, the Panel acted inconsistently with Article 7.1 of the DSU; failed to make an objective assessment of the matter under Article 11 of the DSU; and, made recommendations on measures that are not part of the matter, inconsistently with Article 19.1 of the DSU.

8. China requests that the Appellate Body reverse the Panel's recommendations in paragraphs 8.8; 8.15 and 8.22 of the Panel Report to the extent that they apply to annual replacement measures.

III. APPEAL OF THE PANEL'S FINDING THAT CHINA DOES NOT HAVE THE RIGHT TO INVOKE ARTICLE XX OF THE GATT 1994 IN DEFENSE OF A CLAIM UNDER PARAGRAPH 11.3 OF CHINA'S ACCESSION PROTOCOL

9. China appeals the Panel's erroneous interpretation and application of Paragraphs 1.2 and 11.3 of China's *Accession Protocol*² and Paragraphs 170 and 342 of China's *Working Party Report*³ as not according China the right to invoke Article XX of the GATT 1994 in defense of a claim under Paragraph 11.3 of China's *Accession Protocol* and Paragraph 170 of China's *Working Party Report*.

¹China – Measures Related to the Exportation of Various Raw Materials – Request for the Establishment of a Panel by the European Communities, WT/DS395/7 (9 November 2009); China – Measures Related to the Exportation of Various Raw Materials – Request for the Establishment of a Panel by Mexico, WT/DS398/6 (9 November 2009); China – Measures Related to the Exportation of Various Raw Materials – Request for the Establishment of a Panel by the United States, WT/DS394/7 (9 November 2009).

²Protocol on the Accession of the People's Republic of China, WT/L/432 (23 November 2001) ("Accession Protocol").

³Report of the Working Party on the Accession of China, WT/MIN(01)/3 (10 November 2001) ("*Working Party Report*").

10. As a result of these errors, China requests that the Appellate Body reverse the Panel's findings, in paragraphs 7.158; 7.159; 8.2 (b)-(c); 8.9 (b)-(c) and 8.16 (b)-(c) of the Panel Report, that China may not seek to justify export duties pursuant to Article XX of the GATT 1994.

IV. APPEAL OF THE PANEL'S INTERPRETATION AND APPLICATION OF THE TERM "TEMPORARILY" AND THE PANEL'S INTERPRETATION OF THE TERM "CRITICAL SHORTAGES" IN ARTICLE XI:2(A) OF THE GATT 1994, AND THE PANEL'S ASSESSMENT OF THE MATTER, UNDER ARTICLE II OF THE DSU

11. China appeals the Panel's erroneous interpretation and application of the term "temporarily" and the Panel's erroneous interpretation of the term "critical shortages", in Article XI:2(a) of the GATT 1994. The Panel also failed to make an objective assessment of the matter, as required under Article 11 of the DSU. Specifically, the Panel failed to assess properly evidence that China's export restriction is annually reviewed and renewed, and employed internally inconsistent and incoherent reasoning in its assessment of the possibility to prevent or relieve critical shortages of exhaustible natural resources through the temporary application of export restrictions.

12. As a result of these errors, China requests that the Appellate Body reverse the Panel's interpretation and application of the term "temporarily" and the Panel's interpretation of the term "critical shortages", as set out in paragraphs 7.257-7.258; 7.297-7.302; 7.305; 7.306; 7.346; 7.349; 7.351; 7.354 and 7.355 of the Panel Report.

V. APPEAL OF THE PANEL'S INTERPRETATION OF THE PHRASE "MADE EFFECTIVE IN CONJUNCTION WITH" IN ARTICLE XX(G) OF THE GATT 1994

13. China appeals the Panel's erroneous interpretation of the phrase "... made effective in conjunction with ...", in Article XX(g) of the GATT 1994. Specifically, the Panel erred in interpreting this phrase to require a showing that the "purpose" of a challenged measure is to make effective restrictions on domestic production or consumption. As a result of this error, China requests that the Appellate Body reverse the Panel's finding in paragraph 7.397 of the Panel Report.

VI. APPEAL OF THE PANEL'S INTERPRETATION AND APPLICATION OF PARAGRAPHS 1.2 AND 5.1 OF CHINA'S ACCESSION PROTOCOL AND PARAGRAPHS 83 AND 84 OF THE WORKING PARTY REPORT IN CONNECTION WITH THE PRIOR EXPORT PERFORMANCE AND MINIMUM CAPITAL REQUIREMENTS

14. China appeals the Panel's erroneous interpretation and application of Paragraphs 1.2 and 5.1 of China's *Accession Protocol*, read in combination with Paragraphs 83(a), 83(b), 83(d), 84(a), and 84(b) of China's *Working Party Report*, to prohibit any "examination and approval system" for WTO-consistent export quotas operated subsequent to 11 December 2004, including elimination of "export performance" and "prior experience requirements" and minimum registered capital requirements. As a result of these errors, China requests that the Appellate Body reverse the Panel's findings in paragraphs 7.655; 7.665; 7.669; 7.670; 7.678; 8.4(a)-(b); 8.11(a); 8.11(c) and 8.18(a)-(b) of the Panel Report.

VII. APPEAL OF THE PANEL'S INTERPRETATION AND APPLICATION OF ARTICLE XI:1 OF THE GATT 1994, AND ITS ASSESSMENT OF THE MATTER UNDER ARTICLE 11 OF THE DSU, IN CONNECTION WITH CHINA'S EXPORT LICENSING REGIME

15. China appeals various elements of the Panel's findings under Article XI:1 of the GATT 1994 in connection with China's export licensing requirement.

16. First, the Panel erred in interpreting Article XI:1 to prohibit a measure *as such*, even where, as a matter of municipal law, the measure can always be—and has always been—interpreted and applied in a WTO-consistent manner.

17. Second, the Panel also erred in applying its erroneous interpretation of Article XI:1 to China's export licensing requirement. Specifically, the Panel erroneously found that Article 11(7) of China's *Measures for the Administration of License for the Export of Goods* and Articles 5(5) and 8(4) of China's *Working Rules on Issuing Export Licenses*, *as such*, are inconsistent with Article XI:1, because they accord discretion to request undefined or unspecified documents or materials of applicants for export licenses.

18. Third, the Panel erred in its assessment of the matter, under Article 11 of the DSU. Specifically, the Panel had no evidentiary basis on which to find that any documents requested of an applicant pursuant to Article 11(7) of China's *Measures for the Administration of License for the Export of Goods* and Articles 5(5) and 8(4) of China's *Working Rules on Issuing Export Licenses* would be of such a nature as to impose an export restriction.

19. As a result of these errors, China requests that the Appellate Body reverse the Panel's findings and recommendations, at paragraphs 7.921; 7.946; 7.948; 7.958; 8.5(b); 8.8; 8.12(b); 8.15; 8.19(b) and 8.22 of the Panel Report.

VIII. APPEAL OF THE PANEL'S INTERPRETATION AND APPLICATION OF ARTICLE X:3(A) OF THE GATT 1994, AND ITS ASSESSMENT OF THE MATTER UNDER ARTICLE 11 OF THE DSU, IN CONNECTION WITH THE "OPERATION CAPACITY" CRITERION FOR EXPORT QUOTA ADMINISTRATION

20. China appeals various elements of the Panel's findings under Article X:3(a) of the GATT 1994 in connection with the "operation capacity" criterion for export quota administration, under Article 19 of China's *Measures for the Administration of Export Commodities Quotas*.

21. First, the Panel erred in interpreting Article X:3(a) to prohibit a measure *as such*, even where, as a matter of municipal law, the measure can always be—and has always been—interpreted and applied in such a way as to avoid WTO-inconsistent administration.

22. Second, the Panel also erred in applying its erroneous interpretation of Article X:3(a) to China's "operation capacity" criterion. Specifically, the Panel erroneously found that Article 19 of China's *Measures for the Administration of Export Commodities Quotas*, *as such*, is inconsistent with Article X:3(a), because the term "operation capacity" is undefined, thus reserving the discretion for China to interpret and apply the term in such a manner as to constitute WTO-inconsistent administration.

23. Third, the Panel erred in its assessment of the matter, under Article 11 of the DSU. Specifically, the Panel had no evidentiary basis on which to find that the term "operation capacity" would be interpreted and applied in a manner that would constitute WTO-inconsistent administration.

24. As a result of these errors, China requests that the Appellate Body reverse the Panel's findings and recommendations, at paragraphs 7.708; 7.742-7.746; 7.748-7.752; 7.756; 8.11(e) and 8.15 of the Panel Report.

ANNEX V

WORLD TRADE ORGANIZATION

WT/DS394/12
12 September 2011

(11-4373)

Original: English

CHINA – MEASURES RELATED TO THE EXPORTATION OF VARIOUS RAW MATERIALS

Notification of an Other Appeal by the United States under Article 16.4 and Article 17 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), and under Rule 23(1) of the Working Procedures for Appellate Review

The following notification, dated 6 September 2011, from the Delegation of the United States, is being circulated to Members.

Pursuant to Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 23 of the *Working Procedures for Appellate Review*, the United States hereby notifies its decision to appeal to the Appellate Body certain issues of law covered in the Report of the Panel in *China – Measures Related to the Exportation of Various Raw Materials* (WT/DS394/R) ("Panel Report") and certain legal interpretations developed by the Panel.

1. The United States seeks review by the Appellate Body of the Panel's legal conclusion that China's requirement that enterprises pay a quota allocation fee (also referred to as the total award price or bid-winning price) in order to export bauxite, fluorspar, and silicon carbide under its export quota regime¹ is not inconsistent with Article VIII:1(a) of the *General Agreement on Tariffs and Trade 1994* or Paragraph 11.3 of China's Protocol of Accession to the WTO. These conclusions are in error and are based on erroneous findings on issues of law and legal interpretations of the fees and charges subject to Article VIII.² The United States requests the Appellate Body to reverse the Panel's legal interpretation and conclusion and to find that China's requirement that enterprises pay a total award price in order to export bauxite, fluorspar, and silicon carbide under its export quota regime is inconsistent with Article VIII:1(a) of the GATT 1994 and Paragraph 11.3 of China's Protocol of Accession to the WTO.

¹See Panel Report, Section VII.C.2(b). Relevant legal instruments include the *Import and Export Regulations, Quota Bidding Measures, Quota Bidding Implementation Rules, 2009 First Round Fluorspar Bidding Procedures, 2009 First Round Bauxite Bidding Procedures*, and *2009 First Round Silicon Carbide Bidding Procedures*.

²See, e.g., Panel Report, paras. 7.827-7.839, 7.844-7.851, 7.859-7.861, and 8.4(c).

2. The United States also seeks conditional review by the Appellate Body relating to the Panel's recommendations. If the Appellate Body, pursuant to China's appeal of the Panel's "recommendation with respect to the 'series of measures' that have an ongoing effect through annual replacement measures,"³ were to grant China's request to "reverse the Panel's recommendations in paragraphs 8.8, 8.15 and 8.22 of the Panel Report to the extent that they apply to replacement measures,"⁴ and if the Appellate Body were to find that no recommendation should have been made on the "series of measures" as they existed as of the date of panel establishment, then the United States would seek review of the Panel's legal interpretation⁵ and conclusion⁶ not to make a recommendation on the export quota and export duty measures that were annually recurring and in effect on the date of panel establishment, *i.e.*, December 21, 2009, but that subsequently were replaced or superseded by other legal instruments. In that event, the United States would contend that this interpretation and conclusion are in error and based on erroneous findings on issues of law and related legal interpretations of Articles 6.2, 7.1, 11, and 19.1 of the DSU. The United States would request the Appellate Body to reverse the Panel's legal conclusion and to make the recommendation provided for in DSU Article 19.1. However, the Appellate Body would not need to review this legal interpretation and conclusion if the condition precedent to this appeal is not met.

ANNEX VI

**WORLD TRADE
ORGANIZATION**

WT/DS395/12
12 September 2011

(11-4371)

Original: English

**CHINA – MEASURES RELATED TO THE EXPORTATION
OF VARIOUS RAW MATERIALS**

Notification of an Other Appeal by the European Union
under Article 16.4 and Article 17 of the Understanding on Rules
and Procedures Governing the Settlement of Disputes (DSU),
and under Rule 23(1) of the Working Procedures for Appellate Review

The following notification, dated 6 September 2011, from the Delegation of the European Union, is being circulated to Members.

Pursuant to Article 16.4 and Article 17 of the DSU, the European Union hereby notifies to the Dispute Settlement Body its decision to appeal to the Appellate Body certain issues of law covered in the Report of the Panel and certain legal interpretations developed by the Panel in its Report in the dispute *China – Measures relating to the exportation of various Raw Materials* (WT/DS395/R). Pursuant to Rule 23(1) of the *Working Procedures for Appellate Review*, the European Union simultaneously files this Notice of Other Appeal with the Appellate Body Secretariat.

For the reasons to be further elaborated in its submissions to the Appellate Body, the European Union appeals, and requests the Appellate Body to reverse and/or modify the findings, conclusions and recommendations of the Panel, with respect to the following errors of law and legal interpretations contained in the Panel Report.¹

I. THE EUROPEAN UNION NEVER REQUESTED THE PANEL "NOT TO MAKE FINDINGS OR RECOMMENDATIONS ON THE LEGAL INSTRUMENTS TAKING EFFECT ON 1 JANUARY 2010". THE EUROPEAN UNION NEVER "NARROWED THE PANEL'S TERMS OF REFERENCE DURING THE COURSE OF THE PROCEEDINGS".

¹ See China's Appellant Submission, Section III.

² China's Appellant Submission, para. 167.

³ See, e.g., Panel Report, paras. 7.26-7.32.

⁴ See, e.g., Panel Report, paras. 7.33(d), 8.8.

¹ Pursuant to Rule 23(2)(c)(ii)(C) of the *Working Procedures for Appellate Review* this Notice of Other Appeal includes an indicative list of the paragraphs of the Panel Report containing the alleged errors, without prejudice to the ability of the European Union to refer to other paragraphs of the Panel Report in the context of its appeal.

- (a) In paragraph 7.21 of its Report, the Panel found that the European Union requested the Panel not to make findings or recommendations on the legal instruments taking effect on 1 January 2010. In paragraph 7.22 of its Report, the Panel found that the European Union narrowed the Panel's terms of reference during the course of the proceedings. The Panel makes reference to these erroneous findings in various other paragraphs of its Report, such as paragraph 7.24.
- (b) In reaching these erroneous legal interpretations and findings, the Panel acted inconsistently with its obligations under Articles 7.1, 11 and 19.1 of the DSU.
- (c) The European Union appeals these erroneous Panel legal interpretations and findings and requests the Appellate Body to reverse them. The European Union also requests the Appellate Body to complete the analysis and find that the relevant measures are inconsistent with China's obligations under the covered agreements and to recommend that China brings its measures into compliance with its WTO obligations.

ANNEX VII

**WORLD TRADE
ORGANIZATION**

WT/DS398/11
12 September 2011

(11-4372)

Original: English

**CHINA – MEASURES RELATED TO THE EXPORTATION
OF VARIOUS RAW MATERIALS**

Notification of an Other Appeal by Mexico
under Article 16.4 and Article 17 of the Understanding on Rules
and Procedures Governing the Settlement of Disputes (DSU),
and under Rule 23(1) of the Working Procedures for Appellate Review

The following notification, dated 6 September 2011, from the Delegation of Mexico, is being circulated to Members.

1. Pursuant to Articles 16.4 and 17 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 23(1) of the *Working Procedures for Appellate Review*, Mexico hereby notifies its decision to appeal to the Appellate Body certain issues of law covered in the Panel Report on *China – Measures Related To The Exportation Of Various Raw Materials* (WT/DS398) ("Panel Report"), and certain legal interpretations developed by the Panel in this dispute.
2. Pursuant to Rule 23(2)(c)(ii) of the *Working Procedures for Appellate Review*, this notice of appeal includes and indicative list of the paragraphs of the Panel Report containing the alleged errors, without prejudice to Mexico's ability to refer to other paragraphs of the Panel Report in the context of this appeal.
 1. **Conditional Appeal of the Panel's Recommendations on Annual Export Quota and Export Duty Measures**
 3. Mexico also seeks conditional review by the Appellate Body relating to the Panel's recommendations. If the Appellate Body, pursuant to China's appeal of the Panel's "recommendation with respect to the 'series of measures' that have an ongoing effect through annual replacement measures,"¹ were to grant China's request to "reverse the Panel's recommendations in paragraphs 8.8, 8.15 and 8.22 of the Panel Report to the extent that they apply to replacement measures,"² and if the Appellate Body were to find that no recommendation should have been made on the "series of

¹See China's Appellant Submission, Section III.

²China's Appellant Submission, para. 167.

measures" as they existed as of the date of panel establishment, then Mexico would seek review of the Panel's legal interpretation³ and conclusion⁴ not to make a recommendation on the export quota and export duty measures that were annually recurring and in effect on the date of panel establishment, *i.e.*, December 21, 2009, but that subsequently were replaced or superseded by other legal instruments. In that event, Mexico would contend that this interpretation and conclusion are in error and based on erroneous findings on issues of law and related legal interpretations of Articles 6.2, 7.1, 11, and 19.1 of the DSU. Mexico would request the Appellate Body to reverse the Panel's legal conclusion and to make the recommendation provided for in DSU Article 19.1. However, the Appellate Body would not need to review this legal interpretation and conclusion if the condition precedent to this appeal is not met.

II. Appeal of the Panel Conclusion that China's Administration of its Export Quota through the Involvement of the CCCMC Complied With Article X:3(a) of GATT 1994

4. Mexico appeals various elements of the Panel's findings under Article X:3(a) of the GATT 1994 regarding the involvement of the China Chamber of Commerce on Metals, Minerals in the administration of export quotas.

5. Mexico addresses the following errors in the Panel's findings and conclusions concerning China's an CCCMC's administration of quotas⁵:

- a) First, the Panel erred in its interpretation of Article X:3(a) as requiring complainants to demonstrate, in an as such claim, that a challenged measure must necessarily lead to partial and/or unreasonable administration of export quotas.
 - b) Second, the Panel erred in its interpretation of Article X:3(a) requiring evidence of partiality/unreasonableness when complainants argue that a measure is inherently partial/ unreasonable. Proper interpretation of Article X:3(a) leads to the conclusion that China's delegation of authority to CCCMC is inherently partial/unreasonable.
 - c) Third, the Panel failed to make an objective assessment of the facts of the case as required by Article 11 of the DSU with respect to the role of CCCMC in the quota process. The CCCMC Secretariat's role in administering quotas is much more than purely administrative in nature. Specifically, the CCCMC gains access to confidential business information on applicants, exercises discretion in determining qualifying applicants, and is the sole verifier of certain eligibility data.
6. As a result, Mexico requests that the Appellate Body reverse the Panel's findings and conclusions at, e.g., paragraphs 7.784-7.787, 7.795-7.797, 8.18 c) and d) of the Panel Report.

³See, e.g., Panel Report, paras. 7.26-7.32.

⁴See, e.g., Panel Report, paras. 7.33(d), 8.22.

⁵See Panel Report, paras. 7.774-7.797.

World Trade Organization

**United States – Measures Affecting the Production and Sale of
Clove Cigarettes**

Report of the Appellate Body, 4 April 2012

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AB-2012-1

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Annex I Notification of an Appeal by the United States, WT/DS406/6

CASES CITED IN THIS REPORT

Short Title	Full case title and citation
<i>Australia – Salmon</i>	Appellate Body Report, <i>Australia – Measures Affecting Importation of Salmon</i> , WT/DS18/AB/R, adopted 6 November 1998, DSR 1998:VIII, 3327
<i>Border Tax Adjustments</i>	Working Party Report, <i>Border Tax Adjustments</i> , L/3464, adopted 2 December 1970, BISD 18S/97
<i>Brazil – Retreaded Tyres</i>	Appellate Body Report, <i>Brazil – Measures Affecting Imports of Retreaded Tyres</i> , WT/DS332/AB/R, adopted 17 December 2007, DSR 2007:IV, 1527
<i>Canada – Provincial Liquor Boards (US)</i>	GATT Panel Report, <i>Canada – Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies</i> , DS17/R, adopted 18 February 1992, BISD 39S/27
<i>Canada – Wheat Exports and Grain Imports</i>	Appellate Body Report, <i>Canada – Measures Relating to Exports of Wheat and Treatment of Imported Grain</i> , WT/DS276/AB/R, adopted 27 September 2004, DSR 2004:VI, 2739
<i>Chile – Alcoholic Beverages</i>	Appellate Body Report, <i>Chile – Taxes on Alcoholic Beverages</i> , WT/DS87/AB/R, WT/DS110/AB/R, adopted 12 January 2000, DSR 2000:1, 281
<i>Chile – Alcoholic Beverages</i>	Panel Report, <i>Chile – Taxes on Alcoholic Beverages</i> , WT/DS87/R, WT/DS110/R, adopted 12 January 2000, as modified by Appellate Body Report WT/DS87/AB/R, WT/DS110/AB/R, DSR 2000:1, 303
<i>Chile – Price Band System</i>	Appellate Body Report, <i>Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products</i> , WT/DS207/AB/R, adopted 23 October 2002, DSR 2002:VIII, 3045 (Corr.1, DSR 2006:XII, 5473)
<i>Chile – Price Band System (Article 21.5 – Argentina)</i>	Appellate Body Report, <i>Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products – Recourse to Article 21.5 of the DSU by Argentina</i> , WT/DS207/AB/RW, adopted 22 May 2007, DSR 2007:II, 513
<i>Dominican Republic – Import and Sale of Cigarettes</i>	Appellate Body Report, <i>Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes</i> , WT/DS302/AB/R, adopted 19 May 2005, DSR 2005:XV, 7367
<i>EC – Approval and Marketing of Biotech Products</i>	Panel Report, <i>European Communities – Measures Affecting the Approval and Marketing of Biotech Products</i> , WT/DS291/R, WT/DS292/R, WT/DS293/R, Add.1 to Add.9, and Corr.1, adopted 21 November 2006, DSR 2006:III-VIII, 847
<i>EC – Asbestos</i>	Appellate Body Report, <i>European Communities – Measures Affecting Asbestos and Asbestos-Containing Products</i> , WT/DS135/AB/R, adopted 5 April 2001, DSR 2001:VII, 3243
<i>EC – Bananas III</i>	Panel Reports, <i>European Communities – Regime for the Importation, Sale and Distribution of Bananas ("EC – Bananas III")</i> , WT/DS27/R/ECU (Ecuador) / WT/DS27/R/GTM, WT/DS27/R/HND (Guatemala and Honduras) / WT/DS27/R/MEX (Mexico) / WT/DS27/R/USA (US), adopted 25 September 1997, as modified by Appellate Body Report WT/DS27/AB/R, DSR 1997:II, 695 to DSR 1997:III, 1085

Short Title	Full case title and citation
EC – Bananas III (Article 21.5 – Ecuador II) / EC – Bananas III (Article 21.5 – US)	Appellate Body Reports, <i>European Communities – Regime for the Importation, Sale and Distribution of Bananas – Second Recourse to Article 21.5 of the DSU by Ecuador</i> , WT/DS27/AB/RW2/ECU, adopted 11 December 2008, and Corr.1 / <i>European Communities – Regime for the Importation, Sale and Distribution of Bananas – Recourse to Article 21.5 of the DSU by the United States</i> , WT/DS27/AB/RW/USA and Corr.1, adopted 22 December 2008
EC – Bed Linen (Article 21.5 – India)	Appellate Body Report, <i>European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India – Recourse to Article 21.5 of the DSU by India</i> , WT/DS141/AB/RW, adopted 24 April 2003, DSR 2003:III, 965
EC – Fasteners (China)	Appellate Body Report, <i>European Communities – Definitive Anti-Dumping Measures on Certain Iron or Steel Fasteners from China</i> , WT/DS397/AB/R, adopted 28 July 2011
EC – Hormones	Appellate Body Report, <i>EC Measures Concerning Meat and Meat Products (Hormones)</i> , WT/DS26/AB/R, WT/DS48/AB/R, adopted 13 February 1998, DSR 1998:1, 135
EC – Sardines	Appellate Body Report, <i>European Communities – Trade Description of Sardines</i> , WT/DS231/AB/R, adopted 23 October 2002, DSR 2002:VIII, 3359
EC and certain member States – Large Civil Aircraft	Appellate Body Report, <i>European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft</i> , WT/DS316/AB/R, adopted 1 June 2011
Japan – Agricultural Products II	Appellate Body Report, <i>Japan – Measures Affecting Agricultural Products</i> , WT/DS76/AB/R, adopted 19 March 1999, DSR 1999:1, 277
Japan – Alcoholic Beverages II	Panel Report, <i>Japan – Taxes on Alcoholic Beverages</i> , WT/DSS8/R, WT/DS10/R, WT/DS11/R, adopted 1 November 1996, as modified by Appellate Body Report WT/DSS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, DSR 1996:1, 125
Japan – Alcoholic Beverages II	Appellate Body Report, <i>Japan – Taxes on Alcoholic Beverages</i> , WT/DSS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, DSR 1996:1, 97
Japan – Apples	Appellate Body Report, <i>Japan – Measures Affecting the Importation of Apples</i> , WT/DS245/AB/R, adopted 10 December 2003, DSR 2003:IX, 4391
Korea – Various Measures on Beef	Appellate Body Report, <i>Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef</i> , WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, DSR 2001:1, 5
Mexico – Taxes on Soft Drinks	Appellate Body Report, <i>Mexico – Tax Measures on Soft Drinks and Other Beverages</i> , WT/DS308/AB/R, adopted 24 March 2006, DSR 2006:1, 3
Philippines – Distilled Spirits	Appellate Body Reports, <i>Philippines – Taxes on Distilled Spirits</i> , WT/DS396/AB/R / WT/DS403/AB/R, adopted 20 January 2012
Philippines – Distilled Spirits	Panel Reports, <i>Philippines – Taxes on Distilled Spirits</i> , WT/DS396/R / WT/DS403/R, adopted 20 January 2012, as modified by Appellate Body Reports WT/DS396/AB/R / WT/DS403/AB/R
Thailand – Cigarettes (Philippines)	Appellate Body Report, <i>Thailand – Customs and Fiscal Measures on Cigarettes from the Philippines</i> , WT/DS371/AB/R, adopted 15 July 2011

Short Title	Full case title and citation
US – Carbon Steel	Appellate Body Report, <i>United States – Countervailing Duties on Certain Corrosion-Resistant Carbon Steel Flat Products from Germany</i> , WT/DS213/AB/R and Corr.1, adopted 19 December 2002, DSR 2002:IX, 3779
US – Clove Cigarettes	Panel Report, <i>United States – Measures Affecting the Production and Sale of Clove Cigarettes</i> , WT/DS406/R, circulated to WTO Members 2 September 2011
US – Gasoline	Panel Report, <i>United States – Standards for Reformulated and Conventional Gasoline</i> , WT/DS2/R, adopted 20 May 1996, as modified by Appellate Body Report WT/DS2/AB/R, DSR 1996:1, 29
US – Section 337 Tariff Act	GATT Panel Report, <i>United States Section 337 of the Tariff Act of 1930</i> , L/6439, adopted 7 November 1989, BISD 36S/345
US – Stainless Steel (Mexico)	Appellate Body Report, <i>United States – Final Anti-Dumping Measures on Stainless Steel from Mexico</i> , WT/DS344/AB/R, adopted 20 May 2008, DSR 2008:II, 513
US – Steel Safeguards	Appellate Body Report, <i>United States – Definitive Safeguard Measures on Imports of Certain Steel Products</i> , WT/DS248/AB/R, WT/DS249/AB/R, WT/DS251/AB/R, WT/DS252/AB/R, WT/DS253/AB/R, WT/DS254/AB/R, WT/DS258/AB/R, WT/DS259/AB/R, adopted 10 December 2003, DSR 2003:VII, 3117
US – Tuna (II) (Mexico)	Panel Report, <i>United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products</i> , WT/DS381/R, circulated to WTO Members 15 September 2011
US – Tuna II (Mexico)	Panel Report, <i>United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products</i> , WT/DS381/R, circulated to WTO Members 15 September 2011 [appeal in progress]
US – Upland Cotton (Article 21.5 – Brazil)	Appellate Body Report, <i>United States – Subsidies on Upland Cotton – Recourse to Article 21.5 of the DSU by Brazil</i> , WT/DS267/AB/RW, adopted 20 June 2008, DSR 2008:III, 809
US – Wheat Gluten	Appellate Body Report, <i>United States – Definitive Safeguard Measures on Imports of Wheat Gluten from the European Communities</i> , WT/DS166/AB/R, adopted 19 January 2001, DSR 2001:II, 717
US – Wool Shirts and Blouses	Appellate Body Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/AB/R, adopted 23 May 1997, and Corr.1, DSR 1997:1, 323

ABBREVIATIONS USED IN THIS REPORT

WORLD TRADE ORGANIZATION
APPELLATE BODY

Abbreviation	Description
Doha Ministerial Decision	Doha Ministerial Decision on Implementation-Related Issues and Concerns, Decision of 14 November 2011, WT/MIN(01)/17
DSB	Dispute Settlement Body
DSU	<i>Understanding on Rules and Procedures Governing the Settlement of Disputes</i>
FDA	United States Food and Drug Administration
FDA Guidance	Guidance for Industry and FDA Staff, "General Questions and Answers on the Ban of Cigarettes that Contain Characterizing Flavors (Edition 2)", 23 December 2009 (Panel Exhibit IND-41)
FFDCA	United States Federal Food, Drug and Cosmetic Act, <i>United States Code</i> , Title 21, Chapter 9
FSPTCA	United States Family Smoking Prevention and Tobacco Control Act, Public Law No. 111-31, 123 Stat. 1776 (22 June 2009) (Panel Exhibit US-7)
GATT 1994	<i>General Agreement on Tariffs and Trade 1994</i>
House Report	House Energy and Commerce Committee Report, H.R. No. 111-58, Pt. 1 (2009) (Panel Exhibits IND-2 and US-67)
ILC	International Law Commission
March 2011 TPSAC Report	Report by the Tobacco Products Scientific Advisory Committee to the FDA, March 2011 available at <http://www.fda.gov/downloads/AdvisoryCommittees/CommitteesMeetingMaterials/TobaccoProductsScientificAdvisoryCommittee/UCM247689.pdf>
Panel Report	Panel Report, <i>United States – Measures Affecting the Production and Sale of Clove Cigarettes</i> , WT/DS406/R
Section 907(a)(1)(A)	Section 907(a)(1)(A) of the FFDCA (as amended by the FSPTCA), codified at <i>United States Code</i> , Title 21, Chapter 9, section 387g(a)(1)(A)
TBT Agreement	<i>Agreement on Technical Barriers to Trade</i>
Vienna Convention	<i>Vienna Convention on the Law of Treaties</i> , done at Vienna, 23 May 1969, 1155 UNTS, 8 International Legal Materials 679
WHO	World Health Organization
Working Procedures	<i>Working Procedures for Appellate Review</i> , WT/AB/WP/6, 16 August 2010
WTO	World Trade Organization
WTO Agreement	<i>Marrakesh Agreement Establishing the World Trade Organization</i>

United States – Measures Affecting the Production and Sale of Clove Cigarettes

AB-2012-1

Present:

United States, *Appellant*
Indonesia, *Appellee*

Oshima, Presiding Member
Ramirez-Hernández, Member
Van den Bossche, Member

Brazil, *Third Participant*
Colombia, *Third Participant*
Dominican Republic, *Third Participant*
European Union, *Third Participant*
Guatemala, *Third Participant*
Mexico, *Third Participant*
Norway, *Third Participant*
Turkey, *Third Participant*

I. Introduction

1. The United States appeals certain issues of law and legal interpretations developed in the Panel Report, *United States – Measures Affecting the Production and Sale of Clove Cigarettes*¹ (the "Panel Report"). The Panel was established on 20 July 2010 to consider a complaint by Indonesia with respect to a measure adopted by the United States that prohibits cigarettes with characterizing flavours, other than tobacco or menthol.

2. Before the Panel, Indonesia claimed that the United States acted inconsistently with its substantive and procedural obligations under the *Agreement on Technical Barriers to Trade* (the "TBT Agreement") and the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994"). In particular, Indonesia claimed that Section 907(a)(1)(A) of the United States Federal Food, Drug and Cosmetic Act² (the "FFDCA")—as amended by the Family Smoking Prevention and Tobacco Control Act³ (the "FSPTCA")—was inconsistent with Articles 2.1, 2.2, 2.5, 2.8, 2.9, 2.10, 2.12, and 12.3 of the *TBT Agreement*. Alternatively, Indonesia claimed that Section 907(a)(1)(A) was inconsistent with Article III:4 of the GATT 1994⁴, and could not be justified under Article XX(b) thereof.⁵

¹WT/DS406/R, 2 September 2011.

²Codified at *United States Code*, Title 21, Chapter 9, section 387g(a)(1)(A).

³United States Family Smoking Prevention and Tobacco Control Act, Public Law No. 111-31, 123 Stat. 1776 (22 June 2009) (Panel Exhibit US-7).

⁴Panel Report, para. 3.1.

⁵Panel Report, para. 7.299 (referring to Indonesia's first written submission to the Panel, paras. 114-127).

3. The Panel Report was circulated to Members of the World Trade Organization (the "WTO") on 2 September 2011. The Panel found that Section 907(a)(1)(A) was inconsistent with Article 2.1 of the *TBT Agreement* because it accorded to imported clove cigarettes less favourable treatment than that accorded to like menthol cigarettes of national origin.⁶ Having found that Section 907(a)(1)(A) was inconsistent with Article 2.1 of the *TBT Agreement*, the Panel declined to rule on Indonesia's alternative claim under Article III:4 of the GATT 1994 and on the United States' related defence under Article XX(b) of the GATT 1994.⁷

4. The Panel further found that the United States acted inconsistently with Article 2.9.2 of the *TBT Agreement* by failing to notify to WTO Members, through the Secretariat, the products to be covered by the proposed Section 907(a)(1)(A), together with a brief indication of its objective and rationale, at an appropriate early stage when amendments and comments were still possible.⁸ The Panel also found that the United States acted inconsistently with Article 2.12 of the *TBT Agreement* by not allowing an interval of no less than six months between the publication and the entry into force of Section 907(a)(1)(A).⁹

5. Conversely, the Panel rejected Indonesia's claims under Articles 2.2, 2.5, 2.8, 2.9.3, 2.10, and 12.3 of the *TBT Agreement*. More specifically, the Panel found that Indonesia failed to demonstrate that Section 907(a)(1)(A) was inconsistent with Article 2.2 of the *TBT Agreement* to the extent that its ban on clove cigarettes was more trade restrictive than necessary to fulfil the legitimate objective of reducing youth smoking, taking account of the risks non-fulfilment would create.¹⁰ The Panel also concluded that Indonesia failed to demonstrate that the United States had acted inconsistently with Article 2.5 of the *TBT Agreement*, because Indonesia did not request the United States to explain the justification for Section 907(a)(1)(A) "in terms of Articles 2.2 and 2.4 of the *TBT Agreement*".¹¹ Similarly, the Panel found that Indonesia failed to demonstrate that it would be "appropriate" to formulate the technical regulation in Section 907(a)(1)(A) in terms of "performance" rather than design or descriptive characteristics, within the meaning of Article 2.8 of the *TBT Agreement*.¹²

6. The Panel further found that Indonesia failed to demonstrate that the United States had acted inconsistently with Article 2.9.3 of the *TBT Agreement*, because Indonesia did not request the

⁶Panel Report, paras. 7.293 and 8.1(b).

⁷Panel Report, paras. 7.294, 7.310, 8.3, and 8.4.

⁸Panel Report, paras. 7.550 and 8.1(f).

⁹Panel Report, paras. 7.595 and 8.1(h).

¹⁰Panel Report, paras. 7.432 and 8.1(c).

¹¹Panel Report, paras. 7.461, 7.463, and 8.1(d).

¹²Panel Report, paras. 7.497, 7.498, and 8.1(e).

United States to provide particulars or copies of Section 907(a)(1)(A) while it was still in draft form.¹³ The Panel also found that, in the absence of any evidence or arguments that "urgent problems of safety, health, environmental protection or national security" arose or threatened to arise upon adoption of Section 907(a)(1)(A), Article 2.10 of the *TBT Agreement* would not be applicable to the present dispute.¹⁴ Finally, the Panel found that Indonesia failed to demonstrate that the United States had acted inconsistently with Article 12.3 of the *TBT Agreement* by failing to take account of the special development, financial, and trade needs of Indonesia in the preparation and application of Section 907(a)(1)(A).¹⁵

7. Accordingly, the Panel recommended that the Dispute Settlement Body (the "DSB") request the United States to bring Section 907(a)(1)(A) into conformity with its obligations under Articles 2.1, 2.9.2, and 2.12 of the *TBT Agreement*.¹⁶

8. On 5 January 2012, the United States notified the DSB of its intention to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, pursuant to Articles 16.4 and 17 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), and filed a Notice of Appeal¹⁷ and an appellant's submission pursuant to Rules 20 and 21, respectively, of the *Working Procedures for Appellate Review*¹⁸ (the "*Working Procedures*"). On 23 January 2012, Indonesia filed an appellee's submission.¹⁹ On 26 January 2012, Brazil, Colombia, the European Union, Mexico, Norway, and Turkey each filed a third participant's submission.²⁰ On the same date, the Dominican Republic and Guatemala notified their intention to appear at the oral hearing as third participants.²¹

9. On appeal, the United States claims that the Panel erred in finding that the United States acted inconsistently with Article 2.1 of the *TBT Agreement*. In particular, the United States claims that the Panel erred in finding that imported clove cigarettes and domestic menthol cigarettes were like products within the meaning of Article 2.1. The United States also challenges the Panel's finding that Section 907(a)(1)(A) accords to imported clove cigarettes less favourable treatment than that accorded to domestic like products. The United States claims further that the Panel acted inconsistently with Article 11 of the DSU in reaching these findings. The United States also claims that the Panel erred in finding that the United States acted inconsistently with Article 2.12 of the *TBT Agreement* by not

¹³Panel Report, paras. 7.549, 7.551, and 8.1(g).

¹⁴Panel Report, para. 7.507.

¹⁵Panel Report, paras. 7.649 and 8.1(f).

¹⁶Panel Report, para. 8.6.

¹⁷WT/DS406/6 (attached as Annex 1 to this Report).

¹⁸WT/AB/WP/6, 16 August 2010.

¹⁹Pursuant to Rule 22 of the *Working Procedures*.

²⁰Pursuant to Rule 24(1) of the *Working Procedures*.

²¹Pursuant to Rule 24(2) of the *Working Procedures*.

allowing an interval of no less than six months between the publication and the entry into force of Section 907(a)(1)(A). The United States conditionally appeals the Panel's reliance on the jurisprudence developed under Article XX(b) of the GATT 1994 in its assessment of Indonesia's claims under Article 2.2, should Indonesia appeal the Panel's finding that the United States did not act inconsistently with Article 2.2 of the *TBT Agreement*. Indonesia did not raise an other appeal of any issues under Article 2.2 of the *TBT Agreement*. Therefore, the condition on which the United States bases its appeal of the Panel's findings under Article 2.2 is not met.

10. Two *amicus curiae* briefs were received by the Appellate Body in relation to this appeal: on 24 January 2012 from the Campaign for Tobacco-Free Kids, the American Academy of Pediatrics, the American Cancer Society, the American Cancer Society Cancer Action Network, the American Lung Association, the American Medical Association, and the American Public Health Association; and on 26 January 2012 from the O'Neill Institute for National and Global Health Law at the Georgetown University Law Center. The Appellate Body Division hearing the appeal gave the participants and third participants an opportunity to express their views on the *amicus curiae* briefs referred to above. The Division did not find it necessary to rely on these *amicus curiae* briefs in rendering its decision.

11. On 25 January 2012, the Presiding Member of the Division received a letter from the Director-General of the World Health Organization (the "WHO") expressing interest and offering technical assistance in this appeal in areas covered by the WHO's mandate. The Division thanked the WHO Director-General for her letter, and indicated that it would reflect on the need for such assistance. The Division asked the participants and third participants to comment on the letter from the WHO. Of the participants, the United States submitted comments, and of the third participants, the European Union commented. In the light of the fact that the parties had placed a considerable amount of materials regarding WHO legal instruments and the WHO's work in the area of tobacco control on the Panel record, and mindful of its mandate on appeal under Article 17.6 of the DSU, the Division did not deem it necessary to request assistance from the WHO.

12. The oral hearing in this appeal was held on 9 and 10 February 2012. The participants and six of the third participants (Brazil, Colombia, Guatemala, Mexico, Norway, and Turkey) made oral opening statements. The participants and third participants subsequently responded to questions posed by the Members of the Division hearing the appeal.

II. Arguments of the Participants and the Third Participants

A. *Claims of Error by the United States – Appellant*

1. Article 2.1 of the *TBT Agreement* – "Like Products"

13. The United States claims on appeal that the Panel erred in its interpretation and specific application of the term "like products" under Article 2.1 of the *TBT Agreement*, and requests the Appellate Body to reverse the Panel's findings in this respect. In particular, while agreeing with the overall approach adopted by the Panel in its like product analysis—that is, one that determines likeness based on the traditional "likeness" criteria, and in the light of the legal provision at issue and of the public health nature of the measure being challenged²²—the United States contends that the Panel conducted an "incomplete and flawed" analysis with respect to two of the traditional "likeness" criteria, namely, end-uses and consumer tastes and habits.²³

(a) End-Uses

14. The United States claims that the Panel erred by failing to perform a complete analysis of the different end-uses of clove and menthol cigarettes and by concluding that the end-use for both products is "to be smoked".²⁴ In the United States' view, the Panel improperly dismissed the possible different end-uses presented by the United States—that is, satisfying an addiction to nicotine, and creating a pleasurable experience associated with the taste of the cigarette and aroma of the smoke²⁵—and erroneously based its ultimate conclusion on an "overly narrow analysis".²⁶

15. The United States submits that a panel, when conducting an end-use analysis, must consider the different uses of the products in question and not just the use that is a "common denominator" between the products. In this regard, the United States relies on statements of the Appellate Body in *EC – Asbestos* that "a panel must also examine the other, *different* end-uses for products" and that "[i]t is only by forming a complete picture of the various end-uses of a product that a panel can assess the significance of the fact that products share a limited number of end-uses."²⁷ According to the United States, it is undisputed that both clove and menthol cigarettes are used for smoking, but the Panel improperly limited its analysis to considering only such common use between the products while ignoring other relevant end-uses. Menthol cigarettes, the United States posits, are used to

²²United States' appellant's submission, paras. 37 and 41.

²³United States' appellant's submission, para. 42.

²⁴United States' appellant's submission, para. 43 (quoting Panel Report, para. 7.199).

²⁵United States' appellant's submission, para. 44.

²⁶United States' appellant's submission, para. 45.

²⁷United States' appellant's submission, para. 45 (quoting Appellate Body Report, *EC – Asbestos*, para. 119 (original emphasis)).

"satisfy the nicotine addictions of millions of smokers in the United States", whereas clove cigarettes are primarily used "for experimentation and special social settings" and generally are not smoked to satisfy nicotine addiction in the US market.²⁸

16. The United States further takes issue with the Panel's rejection of the different end-uses of clove and menthol cigarettes based on the argument that these end-uses are related to the reasons why a person might smoke a cigarette, and maintains that the Panel erred in finding that end-uses and consumer tastes and habits are "mutually exclusive concepts".²⁹ Referring to the Appellate Body report in *EC – Asbestos*, the United States notes that, although consumer tastes and habits constitute a "likeness" criterion separate from end-uses, consumer preferences are nonetheless relevant to how products are capable of being used.³⁰ However, the United States contends that the Panel incorrectly considered end-uses "absent the relevant, real-world context"³¹ of how the products at issue are used in the relevant market. Clove and menthol cigarettes have different and "multi-faceted" end-uses—that is, "habitual use and satisfying addiction versus occasional, experimental use"³²—which cannot, in the United States' view, be reduced to the simple, undisputed fact that both types of cigarettes are used for smoking. This is particularly true, the United States adduces, where the public health context relates to the different ways in which cigarettes are used in the relevant market. According to the United States, the Panel erred by failing to consider the "complete picture" and by disregarding evidence relating to such differences in use.³³

(b) Consumer Tastes and Habits

17. The United States claims that the Panel failed to perform a complete analysis of consumer tastes and habits related to clove and menthol cigarettes. In the United States' view, the Panel first made a legal error by excluding the tastes and habits of current adult consumers from its analysis. The United States further contends that the Panel acted inconsistently with Article 11 of the DSU by refusing to examine evidence on how consumers in the relevant market use clove and menthol cigarettes.³⁴

18. First, the United States maintains that the Panel erred in determining that it need not examine the tastes and habits of current adult consumers as part of its analysis. In the United States' view, by disregarding how current consumers perceive and use the products at issue, the Panel erroneously

²⁸United States' appellant's submission, para. 46.

²⁹United States' appellant's submission, para. 48.

³⁰United States' appellant's submission, para. 47 (quoting Appellate Body Report, *EC – Asbestos*, para. 102).

³¹United States' appellant's submission, para. 48.

³²United States' appellant's submission, para. 49.

³³United States' appellant's submission, para. 49.

³⁴United States' appellant's submission, para. 50.

limited the scope of consumer tastes and habits to one aspect of the public health basis for Section 907(a)(1)(A) of the FDCA—use by young people—and failed to capture the other aspect—use by adult smokers—thereby nullifying consumer tastes and habits as a meaningful criterion.³⁵ Consistent with the principle stated by the Appellate Body in *EC – Asbestos*, the Panel was required to examine evidence related to each of the criteria set forth in the GATT Working Party report in *Border Tax Adjustments*, and to weigh "all of the relevant evidence".³⁶ Accordingly, the United States claims that the Panel committed a fundamental error in excluding, *a priori*, an essential element from the analysis of consumer tastes and habits.³⁷

19. Moreover, the United States posits that, given the particular nature of this dispute, the tastes and habits of current adult consumers are highly relevant. First, Section 907(a)(1)(A) draws regulatory distinctions among cigarettes based not only on their appeal to potential smokers, but based on their uses by current adult smokers as well. Banning cigarettes that are used by adults on a regular basis entails a risk of "straining the healthcare system or exacerbating the illicit market".³⁸ Second, clove and other banned flavoured cigarettes are used in very small numbers and almost exclusively by young people, thus being "trainer" or "starter" cigarettes, whereas menthol cigarettes are consumed by 20 to 26 per cent of adult smokers in the United States.³⁹ Consequently, the United States argues, the products at issue pose different public health challenges: clove cigarettes present a unique risk to young, uninitiated smokers, while menthol cigarettes also have a significant impact on adults.⁴⁰ Finally, the particular flavour matters, in the sense that adult smokers seldom use clove-flavoured cigarettes and do not perceive them to be like menthol cigarettes.⁴¹

20. The United States further claims that the exclusion of current adult consumer tastes and habits cannot be justified by the Panel's finding on the declared legitimate objective of Section 907(a)(1)(A) to prevent new young smokers from becoming addicted to cigarettes.⁴² Albeit agreeing with the Panel that the characteristics of the products at issue must be examined in the light of the public health basis of the measure at issue⁴³, the United States contends that there is no textual basis in Article 2.1 of the *TBT Agreement* to limit the consideration of the public health distinctions to the immediate

³⁵United States' appellant's submission, para. 58.

³⁶United States' appellant's submission, para. 56 (quoting Appellate Body Report, *EC – Asbestos*, paras. 109 (in turn referring to GATT Working Party Report, *Border Tax Adjustments*) and 113 (original emphasis)).

³⁷United States' appellant's submission, para. 53.

³⁸United States' appellant's submission, para. 54.

³⁹United States' appellant's submission, para. 58 (referring to Panel Report, paras. 2.24, 2.25, and 7.391).

⁴⁰United States' appellant's submission, para. 55.

⁴¹United States' appellant's submission, para. 58.

⁴²United States' appellant's submission, para. 59 (referring to Panel Report, paras. 7.116, 7.119, 7.201, and 7.206).

⁴³United States' appellant's submission, para. 59 (referring to Panel Report, paras. 7.245-7.249).

objective of the measure.⁴⁴ Rather, technical regulations inevitably reflect a balancing of other considerations relevant to public welfare—in this case, the additional health concerns associated with heavily used cigarettes, such as possible increases in unregulated black market cigarettes or strain on the healthcare system.⁴⁵ The United States submits that the Panel based its exclusion of current adult consumers on a narrow view of the measure's objective, which was actually targeting a group of tobacco products "that *uniquely* appeal to youth" without precluding access by adults to those cigarettes that are "most heavily used in the U.S. market".⁴⁶ Even assuming that the Panel was correct to limit its assessment of the product distinctions on the basis of the primary legitimate objective of Section 907(a)(1)(A)—that is, the "reduction of youth smoking"—the United States contends that, precisely because of the measure's distinction between adult and youth smoking behaviour, the Panel was required to take into account the comparative patterns of use in the relevant market.⁴⁷

21. Second, the United States claims that the Panel acted inconsistently with Article 11 of the DSU by disregarding critical evidence on how consumers use and perceive the products⁴⁸, and thereby came to a "fatally flawed" conclusion on consumer tastes and habits.⁴⁹ In the United States' view, the Panel improperly disregarded critical survey evidence submitted by both parties on the basis that it was not clear and that the information presented therein was "not directly comparable", without duly examining such evidence according to its probative force.⁵⁰ According to the United States, the survey data were particularly relevant because the data provided evidence on how consumers and potential consumers "used and perceived different cigarettes in the *United States*".⁵¹ In addition, the United States argues that the Panel based its conclusions entirely on speculation and conjecture, without any evidentiary support on the record, and ultimately concluded that, for potential consumers, arguably, "any cigarette would likely be fine to start smoking".⁵² However, the United States submits, the reports used as evidence by the Panel "do not tell the whole story", because they focus on cigarettes with characterizing flavours, but do not present the whole picture as to how cigarettes actually are used and perceived in the United States, the relevant market in this dispute.⁵³ According

⁴⁴United States' appellant's submission, para. 60 (referring to Panel Report, para. 7.116).

⁴⁵United States' appellant's submission, para. 61.

⁴⁶United States' appellant's submission, para. 61. (original emphasis)

⁴⁷United States' appellant's submission, para. 63.

⁴⁸United States' appellant's submission, para. 64.

⁴⁹United States' appellant's submission, para. 68.

⁵⁰United States' appellant's submission, para. 67 (quoting Panel Report, para. 7.210). The United States also stresses that, in the section of the Panel Report devoted to its analysis under Article 2.2 of the *TBT Agreement*, the Panel did rely upon the information provided in the surveys on market share. (*Ibid.*, para. 66)

⁵¹United States' appellant's submission, para. 67. (original emphasis)

⁵²United States' appellant's submission, para. 68 (quoting Panel Report, para. 7.214).

⁵³United States' appellant's submission, para. 69 (referring to United States' response to Panel Question 44, para. 110; and Indonesia's response to Panel Question 44, para. 97).

to the United States, the handling of the evidence by the Panel falls short of an objective assessment of the facts and is therefore incompatible with the Panel's duty under Article 11 of the DSU.⁵⁴

2. Article 2.1 of the *TBT Agreement* – "Treatment No Less Favourable"

22. The United States claims that the Panel erred in finding that Section 907(a)(1)(A) of the FFDCA accords to imported clove cigarettes less favourable treatment than that accorded to like domestic products, and requests the Appellate Body to reverse this finding. The United States also requests the Appellate Body to find that the Panel acted inconsistently with Article 11 of the DSU when it found: (i) that there were no domestic cigarettes with characterizing flavours other than menthol at the time of the ban; and (ii) that Section 907(a)(1)(A) imposes no costs on any US entity.

23. First, the United States argues that the Panel erroneously limited the scope of the products to be compared for the purposes of its less favourable treatment analysis to one banned imported product—Indonesian clove cigarettes—and one non-banned like domestic product—menthol cigarettes—thereby reaching the "flawed conclusion" that Indonesian clove cigarettes are treated less favourably than like domestic products.⁵⁵ Referring to the Appellate Body report in *EC – Asbestos*, the United States posits that "the relevant analysis is how the measure treats like imported products, as a group, and like domestic products, as a group".⁵⁶ Accordingly, the Panel was required to consider the "treatment of all domestic and imported cigarettes with characterizing flavors".⁵⁷ However, in the United States' view, the Panel improperly excluded, with respect to like domestic products, the treatment accorded by the measure to domestic cigarettes with other characterizing flavours and, with respect to like imported products, the treatment accorded to menthol cigarettes from other countries.⁵⁸ According to the United States, a proper less favourable treatment analysis that considers all cigarettes that meet the criteria of "like products" demonstrates that Section 907(a)(1)(A) bans only products comprising "a very small market segment in the United States", and "does not alter the conditions of competition" as between like imported products, as a group, and like domestic products, as a group.⁵⁹

24. For the United States, the reference to treatment accorded to the products imported from the territory of "any other Member" in Article 2.1 does not compel the conclusion that only the treatment

⁵⁴United States' appellant's submission, para. 69 (quoting Appellate Body Report, *EC – Hormones*, para. 133).

⁵⁵United States' appellant's submission, para. 74.

⁵⁶United States' appellant's submission, para. 75 (referring to Appellate Body Report, *EC – Asbestos*, para. 100). See also Panel Report, *US – Tuna II (Mexico)*, para. 7.295.

⁵⁷United States' appellant's submission, para. 77. (original underlining) Albeit disagreeing with the Panel's conclusion that clove and menthol cigarettes are like products, the United States stresses that "other cigarettes with characterizing flavors ... would meet the Panel's criteria and thus belong to the category of cigarettes deemed by the Panel to be like products." (*Ibid.*, para. 78 (referring to Panel Report, para. 7.247))

⁵⁸United States' appellant's submission, para. 79.

⁵⁹United States' appellant's submission, paras. 80 and 81. (original underlining)

accorded to the complaining Member's products are relevant.⁶⁰ In the United States' view, the main purpose of a *de facto* less favourable treatment analysis is to assess whether Section 907(a)(1)(A) legitimately draws distinctions among like products or whether it creates "a proxy for singling out the like products of the complaining Member for less favorable treatment".⁶¹ In order to make such an assessment, the analysis should consider the entire range of like products addressed by the measure. The question of less favourable treatment is not answered by the sole fact that clove cigarettes were banned while a single like domestic product (menthol cigarettes) was not. In this case, the United States contends that the ban affected some imported and domestic products, but "did not affect other domestic and imported like products".⁶²

25. In addition, to the extent that the Panel took the view that it was limited by its terms of reference to consider only the products mentioned in Indonesia's request for the establishment of a panel⁶³, the United States claims that the Panel erred in concluding that Indonesia, as the complaining party, "set the field of products to be compared"⁶⁴—that is, "imported clove cigarettes *versus* domestic menthol cigarettes".⁶⁵ While defining which measures and claims a panel may consider, the terms of reference do not define the scope of the relevant products to analyze with respect to a discrimination claim, nor do they limit which defences a responding party may invoke.⁶⁶ The United States notes that the question of which products should be compared in the less favourable treatment analysis was a point of argument between the parties in the present dispute, and stresses that the complainant cannot *a priori* limit the scope of the comparison by its selection of products in its panel request.

26. Second, the United States takes issue with the Panel's statement that, "at the time of the ban, there were no domestic cigarettes with characterizing flavours other than menthol."⁶⁷ The United States submits that such a statement reflects a "mis-application of the legal standard" under Article 2.1 of the *TBT Agreement*.⁶⁸ The Panel "improperly restrict[ed] the legal analysis" when it limited the comparison to only products that were on the market at the time the ban went into effect, without regard to the years preceding or forthcoming. Article 2.1 of the *TBT Agreement* does not contain any "rigid temporal limitation" to the evidence a panel may consider in conducting a less

⁶⁰United States' appellant's submission, para. 84 (referring to Panel Report, para. 7.275).

⁶¹United States' appellant's submission, para. 84.

⁶²United States' appellant's submission, para. 85. (original underlining)

⁶³Request for the Establishment of a Panel by Indonesia, WT/DS406/2.

⁶⁴United States' appellant's submission, para. 87.

⁶⁵United States' appellant's submission, para. 86 (quoting Panel Report, para. 7.147 (original emphasis)).

⁶⁶United States' appellant's submission, para. 87.

⁶⁷United States' appellant's submission, para. 90 (quoting Panel Report, para. 7.289).

⁶⁸United States' appellant's submission, para. 91.

favourable treatment analysis.⁶⁹ Therefore, the Panel should have taken into account the fact that there were domestic cigarettes with characterizing flavours other than menthol in the years preceding the effective date of the ban.⁷⁰ Moreover, the Panel incorrectly dismissed the fact that Section 907(a)(1)(A) was enacted specifically "to respond to an *emerging* trend of products" that US producers "were actively exploring".⁷¹ In that respect, the United States stresses that the focus of Section 907(a)(1)(A) was "primarily U.S. production", and that it is not unusual that producers will stop investing in products "even before the ban goes into effect". This should not be construed, however, as evidence that US production "was not affected".⁷²

27. Third, the United States claims that the Panel failed to make an objective assessment of the facts, in violation of Article 11 of the DSU, by ignoring unrebutted evidence showing that cigarettes with characterizing flavours other than menthol were marketed in the United States at the time of the ban. The facts on record do not support the Panel's finding that there were no domestically produced flavoured cigarettes—other than menthol—at the time of the ban. In particular, the United States recalls that the Panel had already found that: (i) there was at least one domestically produced brand of clove cigarettes on the market prior to the ban⁷³; (ii) the list of cigarettes authorized for sale in 2008 and 2009 in several US states included at least 20 different brands of domestic flavoured cigarettes other than menthol; and (iii) by 2008, just one year before the ban went into effect, at least four US companies were producing flavoured cigarettes.⁷⁴

28. Fourth, the United States claims that the Panel erred in concluding that any detriment to the competitive conditions for clove cigarettes in the US market could not be explained by factors unrelated to the foreign origin of the products. Even assuming *arguendo* that the Panel had properly identified the like imported and domestic products to be compared, its analysis of whether the less favourable treatment accorded to clove cigarettes was related to the origin of the imported products was in error.⁷⁵

⁶⁹United States' appellant's submission, para. 91.

⁷⁰United States' appellant's submission, para. 92 (referring to Indonesia's first written submission to the Panel, footnote 29 to para. 22; United States' first written submission to the Panel, para. 51; ACNielsen 2008 Data on Flavoured Cigarettes in the United States (Panel Exhibit US-52); Examples of Cigarettes Certified for Sale in the United States as of 2009 (Panel Exhibit US-62); New York List of Fire-Safe Certified Cigarettes as of 20 January 2009 (Panel Exhibit US-63); and Maine List of Fire-Safe Certified Cigarettes as of 29 July 2009 (Panel Exhibit US-64)).

⁷¹United States' appellant's submission, para. 93. (original emphasis)

⁷²United States' appellant's submission, para. 94.

⁷³United States' appellant's submission, para. 97 (referring to Panel Report, para. 2.27).

⁷⁴United States' appellant's submission, paras. 97 and 98 (quoting Panel Report, paras. 2.27, 2.28, and footnote 524 to para. 7.289, in turn quoting Panel Exhibits US-52 and US-62 (*supra*, footnote 70)).

⁷⁵United States' appellant's submission, para. 99.

29. For the United States, under Article 2.1 of the *TBT Agreement*, a technical regulation may impose costs or burdens associated with imported products as compared to like domestic products without necessarily according less favourable treatment to the imported product, where these burdens are explained by a factor or circumstance other than the origin of the products.⁷⁶ In this regard, the United States stresses that there are a number of prior WTO reports in which a detrimental effect on an imported product was not related to its origin, but rather to other factors—such as the products' particular market share or import profile, a difference in the real or perceived safety of the products at issue, or the choices of the producers themselves, as private actors.⁷⁷ According to the United States, the Panel failed to consider any arguments or evidence bearing upon other relevant factors (unrelated to origin) that could have explained the detriment to the competitive situation of imported clove cigarettes.⁷⁸

30. In the United States' view, in finding that the reason for excluding menthol cigarettes from the ban under Section 907(a)(1)(A) related to "the costs that might be incurred by the United States were it to ban menthol cigarettes"⁷⁹, the Panel failed to examine whether the detriment to the competitive situation of clove cigarettes was related to their origin.⁸⁰ Besides the fact that "it is unclear" what the Panel meant by "costs", the United States submits that the text of Article 2.1 requires panels to focus on the comparative treatment of products. Therefore, Article 2.1 contains "no basis" for a comparison of costs imposed on foreign producers with those avoided by "any U.S. entity".⁸¹ In any case, the United States posits, the Panel's finding does not show that any detrimental effect to the competitive conditions for clove cigarettes compared to menthol cigarettes was related to the national origin of imported products. In fact, the costs incurred by the United States if it were to ban menthol cigarettes—that is, "the potential impact on the health care system and the potential development of a black market and smuggling of menthol cigarettes"⁸²—would remain unaltered regardless of where menthol cigarettes were produced, and even if all menthol cigarettes were imported.⁸³

⁷⁶United States' appellant's submission, para. 101 (referring to Panel Report, para. 7.269; Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 96; and United States' second written submission to the Panel, paras. 137-144).

⁷⁷United States' appellant's submission, para. 102 (referring to Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 96; Panel Report, *EC – Approval and Marketing of Biotech Products*, para. 7.2514; Panel Report, *US – Tuna II (Mexico)*, paras. 7.331, 7.332, and 7.340; and United States' second written submission to the Panel, paras. 138 and 140).

⁷⁸United States' appellant's submission, paras. 103 and 104.

⁷⁹United States' appellant's submission, para. 105 (quoting Panel Report, para. 7.289).

⁸⁰United States' appellant's submission, para. 105.

⁸¹United States' appellant's submission, para. 106.

⁸²United States' appellant's submission, para. 107 (quoting Panel Report, para. 7.289).

⁸³United States' appellant's submission, para. 107.

31. In addition, the United States claims that the Panel acted inconsistently with its duties under Article 11 of the DSU by finding, without an appropriate evidentiary basis⁸⁴, that Section 907(a)(1)(A) does not impose "any costs on any U.S. entity".⁸⁵ The United States recalls that Article 11 requires a panel to refrain from issuing "affirmative findings that lack a basis in the evidence contained in the panel record".⁸⁶ In this dispute, the United States posits, there was no basis for the Panel to conclude that the measure avoids costs to any US entity, as underscored by the fact that the Panel "barely cited the record".⁸⁷ According to the United States, the Panel ignored the fact that the United States Food and Drug Administration (the "FDA") was charged with enforcing the measure, thereby incurring "costs" as a US entity.⁸⁸ Moreover, the Panel did not take into account that the effect of the measure on US production was "pre-emptive and closed off a potential market that U.S. producers were actively exploring", nor did it consider that, by reducing youth smoking, Section 907(a)(1)(A) reduces demand for all cigarettes and thus "shrinks the U.S. adult cigarette market".⁸⁹

3. Article 2.12 of the TBT Agreement – "Reasonable Interval"

32. The United States claims that the Panel's analysis under Article 2.12 of the *TBT Agreement* contains three errors that led it to find, incorrectly, that the United States acted inconsistently with Article 2.12. First, the United States argues that the Panel attributed an incorrect "interpretative value" to the Doha Ministerial Decision on Implementation-Related Issues and Concerns⁹⁰ (the "Doha Ministerial Decision") in interpreting the meaning of Article 2.12. Second, the United States argues that the Panel incorrectly found that Indonesia had established a *prima facie* case of inconsistency with Article 2.12. Lastly, the United States argues that, regardless of whether the Panel was correct in finding that Indonesia had established a *prima facie* case of inconsistency with Article 2.12, the Panel incorrectly determined that the United States did not rebut Indonesia's arguments.⁹¹

33. The United States first claims that the Panel attributed an incorrect "interpretative value" to paragraph 5.2 of the Doha Ministerial Decision by treating paragraph 5.2 as though it were an authoritative interpretation adopted by the Ministerial Conference pursuant to Article IX:2 of the *Marrakesh Agreement Establishing the World Trade Organization* (the "*WTO Agreement*"), despite not having found that it has this legal status. The United States further argues that the legal value of

⁸⁴United States' appellant's submission, para. 113.

⁸⁵United States' appellant's submission, para. 109; (original emphasis)

⁸⁶United States' appellant's submission, para. 110 (quoting Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 181).

⁸⁷United States' appellant's submission, para. 110.

⁸⁸United States' appellant's submission, para. 110.

⁸⁹United States' appellant's submission, para. 111.

⁹⁰Decision of 14 November 2011, WT/MIN(01)/17.

⁹¹United States' appellant's submission, para. 123.

paragraph 5.2 of the Doha Ministerial Decision is, at most, a "means of supplemental interpretation" under Article 32 of the *Vienna Convention on the Law of Treaties*⁹² (the "*Vienna Convention*").⁹³ Therefore, while paragraph 5.2 of the Doha Ministerial Decision may be used to confirm the meaning of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*, it may not be applied as a "rule" that can be relied upon as the exclusive basis for concluding that the term "reasonable interval" means "not less than six months".⁹⁴

34. According to the United States, the Doha Ministerial Decision "preceded by several months"⁹⁵ a TBT Committee decision that took note of paragraph 5.2 of the Doha Ministerial Decision and, therefore, the Ministerial Conference could not have acted on a recommendation of the Council for Trade in Goods, as Article IX:2 of the *WTO Agreement* requires for the adoption of multilateral interpretations of agreements contained in Annex 1 to the *WTO Agreement*.

35. Second, the United States claims that the Panel incorrectly found that Indonesia had established a *prima facie* case of inconsistency with Article 2.12 where it did not establish that the interval period was unreasonable in the light of the impact on the ability of exporting Members to adapt to the requirements of Section 907(a)(1)(A) of the FFDCA.⁹⁶ The United States submits that Indonesia never provided any evidence or legal argument that demonstrates that the three-month period allowed by the United States prejudiced the ability of any foreign producer, including Indonesian producers, to adapt to the requirements of Section 907(a)(1)(A).⁹⁷

36. The United States argues further that, "[e]ven assuming *arguendo* that the Panel was correct in deciding that the elements of the *prima facie* case could be drawn exclusively from paragraph 5.2", the Panel erred in finding that Indonesia had succeeded in establishing a *prima facie* case under the terms of that paragraph⁹⁸, because Indonesia would have had to establish "with evidence and argument" that Section 907(a)(1)(A) presents a "normal" situation and does not constitute one of the non-urgent cases where it would be reasonable to have a shorter interval.⁹⁹ The United States submits that Indonesia would also have had to establish that "allowing an interval period of at least six months would not render the fulfillment of the objective pursued by Section 907(a)(1)(A) ineffective".¹⁰⁰

⁹²Done at Vienna, 23 May 1969, 1155 UNTS 331; 8 International Legal Materials 679.

⁹³United States' appellant's submission, para. 126.

⁹⁴United States' appellant's submission, para. 126 (quoting Panel Report, para. 7.559). (footnote omitted)

⁹⁵United States' appellant's submission, para. 125.

⁹⁶United States' appellant's submission, para. 131.

⁹⁷United States' appellant's submission, para. 133.

⁹⁸United States' appellant's submission, para. 135.

⁹⁹United States' appellant's submission, paras. 135 and 138.

¹⁰⁰United States' appellant's submission, para. 136.

37. According to the United States, the Panel based its finding that Indonesia had established a *prima facie* case entirely on a "single" statement made by Indonesia that "neither the Act itself nor any other statement by the United States indicates that having [Section 907(a)(1)(A)] enter into force 90 days after signing was necessary to fulfill the objectives of the Act".¹⁰¹ According to the United States, "Indonesia's assertion does not demonstrate what the Panel claimed Indonesia needed to prove—that a six month interval period would be effective in fulfilling the legitimate objective of Section 907(a)(1)(A)".¹⁰²

38. Third, the United States claims that, even if Indonesia did establish a *prima facie* case, the Panel improperly found that the United States did not rebut that *prima facie* case. According to the United States, "no matter what weight"¹⁰³ is attributed to the Doha Ministerial Decision, Indonesia was required to establish a *prima facie* case under the terms of Article 2.12 of the *TBT Agreement*. In the United States' view, the evidence and argument before the Panel on whether the interval period chosen allowed time for Indonesian producers to adapt their products to the requirements of Section 907(a)(1)(A) showed that "the difference between the three and six month interval periods had no impact on Indonesian producers".¹⁰⁴ According to the United States, the fact that "Indonesian producers, even 16 months after the enactment of the FSPTCA, had not adjusted their product lines to produce tobacco or menthol-flavoured cigarettes"¹⁰⁵ is sufficient evidence to rebut the *prima facie* case that the Panel found Indonesia to have established. Accordingly, the Panel committed legal error in finding that "the United States has not rebutted" Indonesia's *prima facie* case.¹⁰⁶

B. *Arguments of Indonesia – Appellee*

I. Article 2.1 of the TBT Agreement – "Like Products"

39. Indonesia requests the Appellate Body to reject the United States' appeal against the Panel's finding that clove and menthol cigarettes are like products within the meaning of Article 2.1 of the *TBT Agreement*. In Indonesia's view, the United States' objection is not about the legal findings of the Panel, but about the appropriate weight to give to certain evidence and findings of fact. According to Indonesia, in many of its claims, the United States is simply attempting to disguise its disagreement with the Panel's findings of fact as legal error.¹⁰⁷ Indonesia also recalls that the United States did not

¹⁰¹United States' appellant's submission, para. 147 (quoting Panel Report, para. 7.587, in turn quoting Indonesia's first written submission to the Panel, para. 145).

¹⁰²United States' appellant's submission, para. 149. (footnote omitted)

¹⁰³United States' appellant's submission, para. 132.

¹⁰⁴United States' appellant's submission, para. 152. (original emphasis)

¹⁰⁵United States' appellant's submission, para. 152 (quoting Panel Report, para. 7.583).

¹⁰⁶United States' appellant's submission, para. 153 (quoting Panel Report, para. 7.594).

¹⁰⁷Indonesia's appellee's submission, para. 65.

appeal the Panel's conclusion that clove and menthol cigarettes share similar physical characteristics.¹⁰⁸

(a) End-Uses

40. Indonesia takes issue with the United States' contention that the Panel "over-simplified" its analysis in finding that the end-use of both products at issue is "to be smoked".¹⁰⁹ In Indonesia's view, the United States' claim that clove and menthol cigarettes have different end-uses because clove cigarettes are smoked only occasionally while menthol cigarettes are used regularly by addicted smokers has no merit and should be rejected by the Appellate Body. At the outset, Indonesia recalls that, in *Philippines – Distilled Spirits*, the United States correctly noted that "there is no support for the [] proposition that a product consumed on special occasions cannot be in competition with a routinely purchased product".¹¹⁰

41. Indonesia first submits that the Panel examined end-uses pursuant to prior guidance from the Appellate Body. In particular, in accordance with the Appellate Body's guidance in *EC – Asbestos*, the Panel noted that the definition of "end-uses" is "the extent to which two products are capable of performing the same function".¹¹¹ According to Indonesia, in its finding with respect to end-uses, the Panel also properly gave special consideration to the fact that Section 907(a)(1)(A) of the FFDCA is a public health measure aimed at addressing youth smoking. In Indonesia's view, moreover, even assuming *arguendo* that the end-uses put forward by the United States were pertinent ones, the United States presented no evidence showing that clove and menthol cigarettes were not both capable of performing the end-uses of satisfying a nicotine addiction and creating a pleasurable experience.¹¹² In addition, Indonesia contends that the Panel did not dismiss out-of-hand the possibility that products may have more than one end-use, but rather simply concluded that the products at issue in the present case did not have the specific end-uses suggested by the United States.¹¹³

42. Second, Indonesia submits that the Panel did not ignore the alternative end-uses for the products at issue proposed by the United States, but rather went to great lengths to consider the evidence regarding end-uses, including those additional end-uses put forth by the United States. According to Indonesia, the Panel addressed the question of whether "regular use" is different from "occasional use", and carefully laid out in its Report the United States' argument that delivering

¹⁰⁸Indonesia's appellee's submission, para. 66.

¹⁰⁹Indonesia's appellee's submission, para. 67.

¹¹⁰Indonesia's appellee's submission, para. 68 (quoting Appellate Body Reports, *Philippines – Distilled Spirits*, para. 71).

¹¹¹Indonesia's appellee's submission, para. 71 (referring to Panel Report, para. 7.191, in turn referring to Appellate Body Report, *EC – Asbestos*, para. 117), (original emphasis)

¹¹²Indonesia's appellee's submission, para. 73.

¹¹³Indonesia's appellee's submission, para. 74 (referring to Panel Report, para. 7.198).

nicotine to addicted smokers must be considered as a separate end-use. However, the Panel eventually found that the United States' argument on end-uses was "circular".¹¹⁴ Indeed, Indonesia argues, the Panel simply was not persuaded by the merits of the argument of the United States¹¹⁵ and proceeded to conclude—based on evidence showing that both clove and menthol cigarettes were capable of delivering nicotine¹¹⁶—that the end-use of both types of cigarettes was "to be smoked".¹¹⁷ Although the United States asserted that there was an "occasional"-use cigarette market, it provided little evidence in support of this claim.¹¹⁸ Accordingly, Indonesia submits that the Panel did not commit errors of law or fail to make an objective assessment of the evidence, and requests the Appellate Body to uphold the Panel's conclusion that clove and menthol cigarettes share the same end-use of "being smoked".¹¹⁹

(b) Consumer Tastes and Habits

43. Indonesia first submits that the Panel did not commit a legal error in its analysis of consumer tastes and habits, but rather conducted a thorough analysis, acted consistently with guidance from the Appellate Body and, after weighing all the evidence on the record, concluded that consumer tastes and habits are similar with respect to clove and menthol cigarettes. In Indonesia's view, the United States simply disagrees with the Panel's conclusion.¹²⁰ According to Indonesia, when presenting its claims of error, the United States ignored the Appellate Body's view that it is not necessary to show *actual* substitution by consumers when assessing "the extent to which consumers perceive and treat the products as alternative means of performing particular functions in order to satisfy a particular want or demand".¹²¹ Indonesia contends that the United States failed to present evidence showing that consumers, whether adult or youth, would be unwilling to substitute clove and menthol cigarettes for the end-use of smoking. Indonesia argues that the United States is wrong in presuming that consumer tastes and habits must be identical to be like, considering that the Appellate Body found that products that are close to being perfectly substitutable can be like products. Indonesia further submits that there is sufficient evidence on record supporting the fact that young smokers and pre-smoking youth view clove and menthol cigarettes "as at least close to substitutable".¹²²

¹¹⁴Indonesia's appellee's submission, para. 75.

¹¹⁵Indonesia's appellee's submission, para. 77.

¹¹⁶Indonesia's appellee's submission, para. 78 (referring to Panel Report, para. 7.196).

¹¹⁷Indonesia's appellee's submission, para. 76 (referring to Panel Report, para. 7.199).

¹¹⁸Indonesia's appellee's submission, para. 78 (referring to United States' response to Panel Question 41, paras. 104-106).

¹¹⁹Indonesia's appellee's submission, para. 79.

¹²⁰Indonesia's appellee's submission, para. 80.

¹²¹Indonesia's appellee's submission, para. 81 (quoting Appellate Body Report, *EC – Asbestos*, para. 101), (emphasis added by Indonesia omitted)

¹²²Indonesia's appellee's submission, para. 82 (referring to Appellate Body Reports, *Philippines – Distilled Spirits*, para. 149), (original emphasis)

44. Indonesia disagrees with the United States' claim that the Panel erred by failing to include addicted adult smokers in the comparison of consumer tastes and habits. In its view, the Panel's first obligation was to determine the objective of the measure, and then determine which consumers to compare "in light of the context and the object and purpose of the provision at issue" and of the measure.¹²³ Indonesia recalls that the United States initially agreed with the Panel's focus on the public health aspects of Section 907(a)(1)(A), and only subsequently took issue with the Panel's linkage "of the consideration of likeness under Article 2.1 with the objective of the measure".¹²⁴ According to Indonesia, the Panel did not fail to consider Section 907(a)(1)(A) as an integral whole. Rather, in the light of the measure's objective of reducing youth smoking, the Panel concluded that "the perception of consumers, or rather potential consumers, can only be assessed with reference to the health protection objective of the technical regulation at issue".¹²⁵

45. Indonesia further submits that, contrary to what the United States alleges, the Panel did not exclude current consumers from its analysis, since it did include current young smokers. According to Indonesia, what the Panel did was not to include the tastes and habits of adults in its analysis¹²⁶, but to lay out very carefully the basis for its decision to focus on current and pre-smoking youth.¹²⁷ Indonesia notes that the Panel established that the purpose of Section 907(a)(1)(A) was to reduce youth smoking, whereas it rejected that a second objective of the measure was to avoid the potential negative consequences or costs associated with banning products to which tens of millions of adults are chemically and psychologically addicted.¹²⁸ Accordingly, the Panel evaluated the consumer tastes and habits of youth, following the guidance set out by the Appellate Body to consider the "particular provision in which the term 'like' is encountered as well as by the context and the circumstances that prevail in any given case to which that provision may apply".¹²⁹

46. Second, Indonesia submits that, in considering evidence regarding consumer tastes and habits, the Panel did not exceed its discretion as the trier of facts, and made an objective assessment of the facts in accordance with Article 11 of the DSU. Indonesia notes, at the outset, that the United States inaccurately cited to the Panel Report when adducing that the Panel focused only on potential young

¹²³Indonesia's appellee's submission, para. 83 (quoting Appellate Body Report, *EC – Asbestos*, paras. 88 and 89). (emphasis added by Indonesia omitted)

¹²⁴Indonesia's appellee's submission, para. 84 (referring to United States' appellant's submission, para. 60).

¹²⁵Indonesia's appellee's submission, para. 86 (quoting Panel Report, para. 7.1119).

¹²⁶Indonesia's appellee's submission, para. 87 (referring to United States' appellant's submission, para. 54).

¹²⁷Indonesia's appellee's submission, para. 88 (referring to Panel Report, para. 7.1119).

¹²⁸Indonesia's appellee's submission, paras. 90 and 91.

¹²⁹Indonesia's appellee's submission, para. 92 (quoting Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 21, DSR 1996:1, 97, at 114).

smokers.¹³⁰ On the contrary, Indonesia posits, the Panel specifically identified the consumers at issue in this case as "young smokers and potential young smokers".¹³¹ In addressing the United States' specific claims, Indonesia argues that the Panel did not willfully disregard or distort evidence. Rather, in Indonesia's view, the Panel carefully reviewed the survey evidence and devoted two paragraphs and five footnotes in its Report to explain that the survey data did not provide clear guidance on comparing consumer tastes and habits, given that the research parameters varied from survey to survey.¹³² Indonesia contends that the Panel's approach to the survey evidence hardly amounts to excluding it *a priori* but, rather, that the Panel, acting within its discretion, simply did not place the same importance on the evidence concerning addicted adult smokers as did the United States.¹³³

47. Indonesia further submits that the Panel did not make affirmative findings of fact that were not grounded on evidence. In Indonesia's view, while not relying on certain evidence put forward by the United States, the Panel identified and relied on other evidence on the record proving that both clove and menthol cigarettes were "trainer" or "starter" cigarettes that appeal to youth.¹³⁴ According to Indonesia, the Panel methodically described a number of sources of evidence (the FDA, the American Lung Association, the WHO, the National Survey on Drug Use and Health, and the Tobacco Products Scientific Advisory Council) indicating that flavoured cigarettes appeal to youth and novice smokers because their characterizing flavours mask the harshness of tobacco. It was based on this evidence that the Panel concluded that all these flavoured cigarettes are perceived as vehicles to start smoking.¹³⁵

48. Lastly, Indonesia adds that the Panel did not commit an egregious error in declining to accord the same weight as the United States sought regarding the addiction rates of use of clove and menthol cigarettes by youth and adults. Referring to Appellate Body reports in *EC – Bed Linen (Article 21.5 – India)*, *Australia – Salmon*, and *Canada – Wheat Exports and Grain Imports*, Indonesia highlights that panels are given "great latitude"¹³⁶ in determining what evidence to consider in evaluating the validity of claims and that a panel's decision not to rely on some of the facts submitted by one of the parties would not by itself constitute legal error.¹³⁷ In conclusion, Indonesia requests the Appellate

¹³⁰Indonesia's appellee's submission, para. 100 (referring to United States' appellant's submission, para. 64).

¹³¹Indonesia's appellee's submission, para. 100 (quoting Panel Report, para. 7.232). (emphasis added by Indonesia)

¹³²Indonesia's appellee's submission, para. 104 (referring to Panel Report, paras. 7.209 and 7.210 and footnotes 426-430 *tereteto*).

¹³³Indonesia's appellee's submission, para. 106.

¹³⁴Indonesia's appellee's submission, para. 111.

¹³⁵Indonesia's appellee's submission, paras. 112-114.

¹³⁶Indonesia's appellee's submission, para. 116.

¹³⁷Indonesia's appellee's submission, paras. 115-117 (referring to Appellate Body Report, *EC – Bed Linen (Article 21.5 – India)*, para. 177; Appellate Body Report, *Australia – Salmon*, para. 267; and Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 186).

Body to reject the United States' claims with respect to the Panel's findings on consumer tastes and habits, and to uphold the Panel's determination that clove and menthol cigarettes are like products for purposes of Article 2.1 of the *TBT Agreement*.¹³⁸

2. Article 2.1 of the *TBT Agreement* – "Treatment No Less Favourable"

49. Indonesia claims that the Panel did not err in finding that, under Section 907(a)(1)(A) of the FFDCA, imported clove cigarettes are treated less favourably than domestic menthol cigarettes for the purposes of Article 2.1 of the *TBT Agreement*. In particular, Indonesia contends that the Panel did not commit error in identifying the products to be compared for its less favourable treatment analysis, and properly found that the less favourable treatment accorded to clove cigarettes cannot be explained by factors unrelated to their foreign origin. Indonesia further maintains that the Panel did not fail to make an objective assessment of the facts in evaluating the evidence before it, thereby acting consistently with Article 11 of the DSU.

50. First, Indonesia argues that the United States misinterprets the Appellate Body report in *EC – Asbestos* and the panel report in *US – Tuna II (Mexico)* as requiring the Panel to have included treatment of cigarettes with characterizing flavours other than clove and menthol in its less favourable treatment analysis.¹³⁹ While the panels in both of the above disputes had conducted an initial like product analysis of a group of products¹⁴⁰, the scope of the like products to be considered in evaluating less favourable treatment was limited to the imported and domestic products at issue, and did not extend to "other potentially like' products in general".¹⁴¹ Since the products at issue in this dispute had been identified as being imported clove cigarettes and domestically produced menthol cigarettes in the United States, the Panel correctly assessed likeness only as between these two categories of products and, as a consequence, properly identified those products for comparison in its less favourable treatment analysis.¹⁴² Moreover, because neither party argued before the Panel that clove cigarettes were like cigarettes with other characterizing flavours, had the Panel included cigarettes with characterizing flavours other than clove and menthol in its analysis, it would have made a finding on a claim that was not before it, thus acting inconsistently with Article 11 of the DSU.¹⁴³

¹³⁸Indonesia's appellee's submission, para. 118.

¹³⁹Indonesia's appellee's submission, para. 121 (referring to United States' appellant's submission, para. 77).

¹⁴⁰Indonesia's appellee's submission, para. 126.

¹⁴¹Indonesia's appellee's submission, para. 130.

¹⁴²Indonesia's appellee's submission, para. 139 (referring to Panel Report, para. 7.277).

¹⁴³Indonesia's appellee's submission, paras. 140 and 141; see also para. 142 (quoting Appellate Body Report, *Chile – Price Band System*, para. 173).

51. Indonesia further rejects the United States' contention that the Panel incorrectly narrowed the scope of products to be compared on the basis of its terms of reference. Indonesia dismisses this argument as speculative and emphasizes that the Panel referred to its terms of reference in the context of its like products analysis.¹⁴⁴ The Panel never contemplated that flavoured cigarettes other than clove and menthol cigarettes could be included in the like products analysis, which would be consistent with its terms of reference. Moreover, Indonesia's panel request and its subsequent submissions demonstrate that Indonesia raised no claims and made no arguments with respect to cigarettes with characterizing flavours other than clove or menthol.¹⁴⁵ Accordingly, the question of whether the Panel's terms of reference "could have allowed a finding of likeness" between clove cigarettes and other flavoured cigarettes "is moot".¹⁴⁶ Indonesia considers that, "absent a finding of likeness between clove and cigarettes with other characterizing flavors", the Panel could not have included these other flavoured cigarettes in its less favourable treatment analysis.¹⁴⁷

52. Second, Indonesia argues that the Panel did not exceed its discretion when considering the effect of Section 907(a)(1)(A) on those products that existed at the time the measure went into effect. Indonesia characterizes the United States' argument in this respect as "irrelevant"¹⁴⁸, and adds that the Panel acted within the limits of its discretion in determining the time period for which a comparison was to be made. While Indonesia agrees that there is "no rigid temporal limitation"¹⁴⁹ on the timeframe for analyzing less favourable treatment, neither is there a mandate to consider any specific timeframe for this analysis.¹⁵⁰ Moreover, Indonesia submits that the United States is arguing that the Panel should have assessed the treatment of the imported product—clove cigarettes—and a domestic product that had not been found to be like—other flavoured cigarettes. However, the "relevant comparison" had to be whether the measure at issue modified the conditions of competition "to the detriment of imported clove cigarettes as compared to menthol cigarettes, which were not banned".¹⁵¹

53. Third, Indonesia disagrees with the United States' claim that the Panel acted inconsistently with Article 11 of the DSU by failing to consider evidence demonstrating that cigarettes with characterizing flavours other than clove or menthol were being sold in the United States at the time the measure went into effect. According to Indonesia, because the appropriate products for

¹⁴⁴Indonesia's appellee's submission, paras. 147 and 148 (referring to United States' appellant's submission, para. 86; and Panel Report, paras. 7.124-7.127).

¹⁴⁵Indonesia's appellee's submission, paras. 149 and 150 (referring to Indonesia's panel request, pp. 1-2; and Indonesia's responses to Panel Questions 27 and 85).

¹⁴⁶Indonesia's appellee's submission, para. 150.

¹⁴⁷Indonesia's appellee's submission, para. 151.

¹⁴⁸Indonesia's appellee's submission, para. 151.

¹⁴⁹Indonesia's appellee's submission, para. 152 (quoting United States' appellant's submission, para. 89).

¹⁵⁰Indonesia's appellee's submission, para. 152; see also para. 154 (quoting Panel Report, *US – Tuna II (Mexico)*, paras. 7.299 and 7.300).

¹⁵¹Indonesia's appellee's submission, para. 157.

comparison in the less favourable treatment analysis were clove and menthol cigarettes, the existence of other flavoured cigarettes at the time the ban was imposed is immaterial. Furthermore, Indonesia submits that the Panel did consider and weigh the evidence submitted by the United States regarding the availability of other flavoured cigarettes, but eventually did not find it compelling.¹⁵² Indonesia also points out that evidence on the record showed that the domestically produced brand of clove cigarettes "accounted for a negligible share of all clove cigarettes sold in the United States".¹⁵³ In Indonesia's view, the fact that the Panel did not place the same weight on such evidence as did the United States does not amount to a violation of Article 11 of the DSU.

54. Fourth, Indonesia takes issue with the United States' claim that the Panel applied the incorrect legal framework in determining whether the less favourable treatment accorded to clove cigarettes could be explained by factors unrelated to their foreign origin. Indonesia observes that the Appellate Body jurisprudence regarding Article III:4 of the GATT 1994 provides useful guidance in the present dispute¹⁵⁴ and that, under that provision, a less favourable treatment analysis only involves determining whether a measure has the effect of modifying the conditions of competition to the detriment of imported products.¹⁵⁵ According to Indonesia, the United States' claim that no less favourable treatment exists when the detrimental effect on an imported product is not attributable to its foreign origin, but to some other factor, is based on a "misreading" of the Appellate Body report in *Dominican Republic – Import and Sale of Cigarettes*.¹⁵⁶ On this basis, Indonesia posits, the United States is "attempt[ing] to create a new criterion" when it suggests that a finding of less favourable treatment under Article 2.1 of the *TBT Agreement* would be possible only if a measure's detrimental effects are tied to the foreign origin of the imported product at issue.¹⁵⁷ In fact, no panel or Appellate Body report has ever required under Article III:4 of the GATT 1994 "both 'a less favourable treatment' test and a second test 'based on national origin'".¹⁵⁸ In other words, Indonesia contends that the Panel's conclusion that imported clove cigarettes are treated less favourably than

¹⁵²Indonesia's appellee's submission, paras. 158 and 162 (referring to Panel Report, footnote 524 to para. 7.289).

¹⁵³Indonesia's appellee's submission, para. 164 (referring to Panel Report, paras. 2.26 and 2.27; and letter dated 25 March 2008 from the President of the Tobacco Merchants Association, Inc. (Panel Exhibit IND-12)).

¹⁵⁴Indonesia's appellee's submission, para. 169 (referring to Panel Report, para. 7.269, in turn referring to Appellate Body Report, *Korea – Various Measures on Beef*, para. 137; and Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 96).

¹⁵⁵Indonesia's appellee's submission, para. 172 (referring to Indonesia's opening statement at the first panel meeting, paras. 26 and 58; Indonesia's response to Panel Question 52; and Indonesia's second written submission to the Panel, para. 99).

¹⁵⁶Indonesia's appellee's submission, para. 173 (referring to Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 96).

¹⁵⁷Indonesia's appellee's submission, para. 174 (referring to Brazil's oral statement at the Panel meeting with the third parties, para. 11; and Indonesia's second written submission to the Panel, para. 98).

¹⁵⁸Indonesia's appellee's submission, paras. 179-181 (quoting Appellate Body Report, *Korea – Various Measures on Beef*, para. 135; and Appellate Body Report, *Thailand – Cigarettes (Philippines)*, paras. 128 and 134; and referring to Panel Report, *Mexico – Taxes on Soft Drinks*, paras. 8.114-8.122).

domestic menthol cigarettes—because the former are banned from the US market, whereas the latter are not—is *per se* sufficient to make a finding that the United States acted inconsistently with Article 2.1 of the *TBT Agreement*.¹⁵⁹

55. In addition, Indonesia disagrees with the United States' claim that the Panel failed to make an objective assessment of the facts as required by Article 11 of the DSU when it found that Section 907(a)(1)(A) did not impose any costs on any US entity without an adequate evidentiary basis. Indonesia contends that there was evidence on the record demonstrating that: (i) the exception for menthol cigarettes under the measure at issue was the result of a political compromise with the US tobacco industry and an effort to protect domestic jobs¹⁶⁰; and (ii) that the sole reason for excluding menthol cigarettes from the ban was to spare the United States from the costs it might otherwise incur.¹⁶¹ In evaluating and weighing such evidence, the Panel assessed the facts within the limits of its discretion, and thus did not act inconsistently with Article 11 of the DSU.

3. Article 2.12 of the TBT Agreement – "Reasonable Interval"

56. Indonesia submits that the Panel assigned the correct interpretative value to paragraph 5.2 of the Doha Ministerial Decision, and properly found that Indonesia established a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement*, which the United States failed to rebut.¹⁶²

57. First, Indonesia contends that the United States incorrectly claims that the Panel declined to formally determine whether paragraph 5.2 of the Doha Ministerial Decision is an "authoritative interpretation" adopted by the Ministerial Conference pursuant to Article IX:2 of the *WTO Agreement*. According to Indonesia, the Panel "clearly concluded" that paragraph 5.2 of the Doha Ministerial Decision is "a binding interpretation".¹⁶³ Moreover, Indonesia disagrees with the United States that the Ministerial Conference, in adopting paragraph 5.2, did not act upon the recommendation of the Council for Trade in Goods, as Article IX:2 of the *WTO Agreement* requires. According to Indonesia, the preamble of the Doha Ministerial Decision indicates that the Decision and the interpretations contained therein were adopted on the basis of discussions carried out within the General Council and the WTO subsidiary bodies.

¹⁵⁹Indonesia's appellee's submission, para. 172.

¹⁶⁰Indonesia's appellee's submission, para. 187 (referring to Indonesia's second written submission to the Panel, para. 118; S. Saul, "Cigarette Bill Treats Menthol with Leniency", *New York Times*, 13 May 2008 (Panel Exhibit IND-87); and S. Saul, "Bill to Regulate Tobacco Moves Forward", *New York Times*, 3 April 2008 (Panel Exhibit IND-88)).

¹⁶¹Indonesia's appellee's submission, para. 189 (referring to Panel Report, para. 7.289, in turn quoting United States' first written submission to the Panel, paras. 23-25; and United States' response to Panel Questions 40, 89, and 109).

¹⁶²Indonesia's appellee's submission, para. 195.

¹⁶³Indonesia's appellee's submission, para. 196 (referring to Panel Report, para. 7.575).

58. In response to the United States' argument that the Doha Ministerial Decision is "at most"¹⁶⁴ a supplementary means of interpretation within the meaning of Article 32 of the *Vienna Convention*, Indonesia submits that the Panel properly determined that paragraph 5.2 of the Doha Ministerial Decision is a "subsequent agreement between the parties" within the meaning of Article 31(3)(a) of the *Vienna Convention*.¹⁶⁵ Moreover, Indonesia argues that the Panel did not err in its interpretation of the term "normally" in paragraph 5.2 of the Doha Ministerial Decision. According to Indonesia, the Panel correctly concluded that the term "normally" must be interpreted as meaning "under normal or usual conditions; as a rule".¹⁶⁶

59. Second, Indonesia submits that the Panel did not err in finding that Indonesia had established a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement*. According to Indonesia, the United States incorrectly argues that the Panel based its finding that Indonesia had established a *prima facie* case "exclusively" on the basis of the text of paragraph 5.2 of the Doha Ministerial Decision.¹⁶⁷ Indonesia contends that the Panel Report clearly shows that the Panel considered both Article 2.12 of the *TBT Agreement* and paragraph 5.2 of the Doha Ministerial Decision.¹⁶⁸ Indonesia contends that this is "categorically stated" by the Panel when it noted that "Indonesia ha[d] persuaded the Panel that, in the light of Article 2.12 of the *TBT Agreement* and paragraph 5.2 of the Doha Ministerial Decision, an interval of less than six months was not reasonable in the circumstances of this case".¹⁶⁹

60. In response to the United States' argument that Indonesia provided no evidence or argumentation that the three-month interval prejudiced the ability of Indonesian producers to adapt to the requirements of Section 907(a)(1)(A) of the FFDCA, Indonesia contends that it adduced sufficient argument and evidence to establish a presumption that the United States had acted inconsistently with its obligation under Article 2.12.¹⁷⁰ According to Indonesia, it did "establish[] a *prima facie* case that the 90-day interval provided by the United States was significantly shorter than the 6 months" normally required.¹⁷¹ Indonesia submits that, following the elements stipulated in Article 2.12 of the *TBT Agreement*, as well as in the binding interpretation of the term "reasonable interval" in paragraph 5.2 of the Doha Ministerial Decision, Indonesia set forth in its written and oral submissions, as well as in its Panel exhibits, legal arguments and evidence to raise the presumption

¹⁶⁴Indonesia's appellee's submission, para. 205 (quoting United States' appellant's submission, para. 126).

¹⁶⁵Indonesia's appellee's submission, para. 206.

¹⁶⁶Indonesia's appellee's submission, paras. 220 and 221.

¹⁶⁷Indonesia's appellee's submission, para. 223 (referring to United States' appellant's submission, para. 128).

¹⁶⁸Indonesia's appellee's submission, para. 227.

¹⁶⁹Indonesia's appellee's submission, para. 230 (quoting Panel Report, para. 7.594).

¹⁷⁰Indonesia's appellee's submission, para. 233.

¹⁷¹Indonesia's appellee's submission, para. 237.

that its claim against the United States under Article 2.12 was true.¹⁷² Accordingly, Indonesia submits that the Panel did not commit a legal error in finding that Indonesia had established a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement*.

61. Third, with regard to the United States' claim that, even assuming that the Panel correctly found that Indonesia had established a *prima facie* case, the Panel committed legal error in finding that the United States had not rebutted Indonesia's *prima facie* case, Indonesia responds that, since it had made out a *prima facie* case, the onus shifted to the United States "to bring forward evidence and arguments to disprove the claim".¹⁷³ Since the 90-day interval provided by the United States was significantly shorter than the six months normally required, the burden shifted to the United States to refute the claimed inconsistency. According to Indonesia, the Panel correctly stressed that the United States had failed to explain why it deemed that allowing a longer interval period between the publication and the entry into force of Section 907(a)(1)(A) would not have been effective in fulfilling the objective pursued by the measure, while a three-month interval was.¹⁷⁴ Indonesia also posits that the United States did not explain why six months would have been ineffective, especially taking into account that it did not notify Section 907(a)(1)(A) as an urgent measure pursuant to Article 2.10 of the *TBT Agreement*.¹⁷⁵

62. According to Indonesia, the Panel weighed and balanced the evidence and arguments on the record and, while it was "convinced of the validity of the claim advanced by Indonesia", it "was not convinced by the rebuttal arguments" presented by the United States.¹⁷⁶ In Indonesia's view, therefore, the Panel acted consistently with its duties since, "in the absence of effective refutation by the defending party, a panel, as a matter of law, is required to rule in favor of the complaining party presenting the *prima facie* case".¹⁷⁷

C. Arguments of the Third Participants

I. Brazil

63. Brazil generally agrees with the views expressed by the Panel concerning the legal standard for the assessment of likeness under Article 2.1 of the *TBT Agreement*. For Brazil, the absence of a provision similar to Article III:1 of the GATT 1994, combined with the sixth recital of the preamble

¹⁷²Indonesia's appellee's submission, para. 234.

¹⁷³Indonesia's appellee's submission, para. 240 (quoting Appellate Body Report, *US – Wool Shirts and Blouses*, pp. 16-17, DSR 1997:1, 323, at 338).

¹⁷⁴Indonesia's appellee's submission, para. 240 (referring to Panel Report, para. 7.593).

¹⁷⁵Indonesia's appellee's submission, para. 241 (referring to Panel Report, para. 7.593).

¹⁷⁶Indonesia's appellee's submission, para. 242. (underlining omitted)

¹⁷⁷Indonesia's appellee's submission, para. 243 (referring to Panel Report, para. 7.591, in turn referring to Appellate Body Report, *EC – Hormones*, para. 104; Appellate Body Report, *Japan – Agricultural Products II*, paras. 98 and 136; and Appellate Body Report, *Japan – Apples*, para. 159).

of the *TBT Agreement*, seems to indicate that the objectives of a technical regulation should play an important role in ascertaining the characteristics of products alleged to be like.¹⁷⁸ Despite there being no direct reference in Article 2.1 of the *TBT Agreement* to the legitimate objectives of the technical regulation, Brazil notes that the use of an overarching analytical concept to inform all paragraphs of a provision is an issue that has already been accepted in WTO jurisprudence.¹⁷⁹ In Brazil's view, the objective pursued by a Member adopting a technical regulation is a central element of the likeness analysis under Article 2.1, given its context and object and purpose.¹⁸⁰ However, Brazil posits, it does not seem reasonable to require a panel to examine the intentions of the regulator and its implications that go beyond the explicit legitimate objective of a measure. The objectives pursued through technical regulations must be assessed as objectively as possible¹⁸¹, looking at the measure's structure, architecture, and design.¹⁸² Once the legitimate objectives pursued by a Member are properly revealed, Brazil is of the view that they should inform the likeness analysis under Article 2.1 of the *TBT Agreement*.

64. Brazil further notes that the United States pursues an interpretation of the term "treatment no less favourable" that would require evidence of origin-based detrimental effects to the imported product as a prerequisite for showing *de facto* discrimination.¹⁸³ Accordingly, Brazil explains, the United States considers that if any factor, other than the foreign origin of the product, were found to be the basis for the discrimination, there would be no violation of Article 2.1 of the *TBT Agreement*. In Brazil's view, both under Article III:4 of the GATT 1994 and under Article 2.1 of the *TBT Agreement*, a key question is to what extent the application of a measure results in less favourable treatment to the like imported product, regardless of the measure's stated objective.¹⁸⁴ The difference between these two provisions is that, while under Article 2.1 of the *TBT Agreement* the measure's objectives are relevant in defining whether the products at issue are like, under Article III:4 of the GATT 1994, likeness is assessed from a competition perspective.¹⁸⁵ Under both provisions, Brazil contends, once the imported and domestic products are found to be like, the manner in which the measure is applied and the prevailing circumstances of the relevant market for the affected products are more important in a less favourable treatment determination than the measure's

¹⁷⁸Brazil's third participant's submission, para. 8.

¹⁷⁹Brazil's third participant's submission, para. 11 (referring to Appellate Body Report, *EC – Asbestos*, para. 98; and Appellate Body Reports, *Philippines – Distilled Spirits*, para. 119).

¹⁸⁰Brazil's third participant's submission, para. 14.

¹⁸¹Brazil's third participant's submission, para. 17.

¹⁸²Brazil's third participant's submission, para. 20 (referring to Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 29, DSR 1996:1, 97, at 120; Appellate Body Report, *Chile – Alcoholic Beverages*, paras. 61 and 62; and Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 112).

¹⁸³Brazil's third participant's submission, para. 23 (referring to United States' appellant's submission, paras. 101-106).

¹⁸⁴Brazil's third participant's submission, para. 28 (referring to Appellate Body Report, *Japan – Alcoholic Beverages II*, p. 28, DSR 1996:1, 97, at 119).

¹⁸⁵Brazil's third participant's submission, para. 29.

objectives. According to Brazil, this conclusion is even more relevant in the context of an analysis of a *de facto* discrimination.¹⁸⁶

2. Colombia

65. Colombia submits that the Panel erred in its legal interpretation of paragraph 5.2 of the Doha Ministerial Decision. In its view, the Panel decided to give the Doha Ministerial Decision the status of an authoritative interpretation because it was agreed by all WTO Members meeting in the form of the Ministerial Conference, the highest ranking body of the WTO.¹⁸⁷ According to Colombia, however, this legal conclusion is incorrect. Colombia notes that the Ministerial Conference did not act on the basis of a recommendation by the Council overseeing the functioning of the *TBT Agreement* as mandated by Article IX:2 of the *WTO Agreement*, and, consequently, the first condition of Article IX:2 was not present in this case.¹⁸⁸ Furthermore, the Panel dismissed this condition on the basis that it was only a formal requirement. Colombia considers such reasoning to be in error: first, because the procedural nature of a condition does not mean that it can be overlooked¹⁸⁹; and, second, because the fact that all Members agreed on a certain interpretation is not sufficient to conclude that such interpretation was adopted pursuant to Article IX:2 of the *WTO Agreement*. With respect to the latter point, Colombia submits that neither the Ministerial Conference nor the General Council have the authority to disregard the previously given consent by all WTO Members embodied in the covered agreements.¹⁹⁰ Colombia further is of the view that the Appellate Body should clarify whether the Doha Ministerial Decision could be considered to constitute, pursuant to Article 31(3)(a) of the *Vienna Convention*, a "subsequent agreement between the parties" on the interpretation of Article 2.12 of the *TBT Agreement*.¹⁹¹

3. European Union

66. The European Union first submits that the term "like product" appears to be used by the parties and the Panel in two different ways. The first use relates to the "comparison between the import and domestic sides" (the "horizontal line")¹⁹², while the second use concerns the "relationship among the things that are to be considered together" as a product on both the import and domestic sides (the "vertical line")¹⁹³. In the European Union's view, the "horizontal line" comparison requires the import and domestic categories to be described in terms that are identical in all respects, otherwise

¹⁸⁶Brazil's third participant's submission, para. 30.

¹⁸⁷Colombia's third participant's submission, para. 6 (quoting Panel Report, para. 7.576).

¹⁸⁸Colombia's third participant's submission, para. 10.

¹⁸⁹Colombia's third participant's submission, para. 14.

¹⁹⁰Colombia's third participant's submission, para. 15.

¹⁹¹Colombia's third participant's submission, para. 19.

¹⁹²European Union's third participant's submission, para. 17. (original underlining)

¹⁹³European Union's third participant's submission, para. 18. (original underlining)

one cannot meaningfully test for *de facto* discrimination.¹⁹⁴ The "vertical line" comparison, on the other hand, does not require that all things within the set of a "product" be identical in all respects because the comparison is made on the basis of a market definition (that is, by reference to cross-elasticity of supply and demand), hence quite heterogeneous things can be taken together as a single product.¹⁹⁵ The European Union is of the view that, to determine whether there is *de facto* discrimination, it is necessary to consider whether the regulatory distinction is related to the foreign origin of the product.¹⁹⁶ For this reason, the European Union contends that even if clove and menthol cigarettes would be reasonably grouped together as part of a "product", this does not mean that the situation in respect of menthol cigarettes and youth smoking, and clove cigarettes and youth smoking, is necessarily the same or similar.¹⁹⁷

67. With respect to the less favourable treatment analysis under Article 2.1 of the *TBT Agreement*, the European Union stresses that the relationship between trade and regulation is complex.¹⁹⁸ In its view, the problem is to distinguish between the exercise of regulatory autonomy that is acceptable, and that which is not.¹⁹⁹ This necessarily entails looking at whether the design of the measure is, expressly or by proxy, related to the foreign origin of the regulated products. The European Union also considers that any "countervailing explanations" should be considered together with the inquiry into whether there is some relation with foreign origin, because such an approach provides for the most flexibility when considering a wide range of potential factual situations.²⁰⁰ In addition, the European Union raises concerns regarding the Panel's approach in allocating the burden of proof under Article 2.1 of the *TBT Agreement*.²⁰¹ In particular, according to the European Union, the Panel seems to reason that, because both menthol and clove cigarettes appeal to youth, the only plausible explanation for the failure to extend the ban to menthol cigarettes is *de facto* discrimination.²⁰² However, this reasoning overlooks the possibility advocated by the United States that the attractiveness of clove cigarettes to youth is more pronounced than in the case of menthol cigarettes.²⁰³ The European Union contends that the Panel did not explain how Indonesia had discharged its burden of proving that the situation with respect to menthol cigarettes and youth smoking was the same as or similar to the situation with respect to clove cigarettes.²⁰⁴ If Indonesia

¹⁹⁴European Union's third participant's submission, para. 19.

¹⁹⁵European Union's third participant's submission, para. 20.

¹⁹⁶European Union's third participant's submission, para. 21.

¹⁹⁷European Union's third participant's submission, para. 23.

¹⁹⁸European Union's third participant's submission, para. 32.

¹⁹⁹European Union's third participant's submission, para. 33.

²⁰⁰European Union's third participant's submission, para. 44.

²⁰¹European Union's third participant's submission, para. 51.

²⁰²European Union's third participant's submission, para. 54.

²⁰³European Union's third participant's submission, para. 54 (referring to United States' appellant's submission, paras. 32-36, 54, 55, and 61-63).

²⁰⁴European Union's third participant's submission, para. 56.

failed to provide evidence in that respect, the European Union wonders how Indonesia may be considered to have discharged its burden of proof with respect to an alleged "in fact" breach of Article 2.1 of the *TBT Agreement*.²⁰⁵

68. Lastly, with respect to Article 2.12 of the *TBT Agreement*, the European Union considers that paragraph 5.2 of the Doha Ministerial Decision is relevant either pursuant to Article 31(3)(a) of the *Vienna Convention*, or as a fact.²⁰⁶ It further contends that Indonesia had the burden of proving, under Article 2.12 of the *TBT Agreement*, that the time actually allowed by the measure was not reasonable.²⁰⁷ With respect to the question of whether or not six months would be ineffective in fulfilling the legitimate objective pursued, the European Union finds nothing in the Doha Ministerial Decision that expressly reverses the burden of proof.²⁰⁸ It recalls, in that regard, that the Appellate Body in *EC – Sardines* placed the burden of proof on the complainant under Article 2.4 of the *TBT Agreement*.²⁰⁹

4. Mexico

69. Mexico submits that it is difficult to incorporate the objective of a technical regulation into the like products analysis. In its view, when the purpose of a technical regulation is to protect the highest values, such as human life or health, the analysis of the four criteria will itself be sufficient to reach a correct interpretation of likeness because "the product differences themselves will have inspired the objective of the technical regulation, and not the opposite".²¹⁰ Mexico contends, in particular, that the consumer tastes and habits criterion needs to be approached very carefully because regulatory intervention by a Member can "shape consumer perceptions".²¹¹ Moreover, Mexico submits that the creation of sub-categories of like products on the basis of different end-uses, as suggested by the United States, could lead to circumvention of the disciplines in Article 2.1 of the *TBT Agreement*.²¹² Mexico further stresses that, if regulatory distinctions could be used to determine like products, this could "render the concept of *de facto* discrimination meaningless".²¹³

70. With respect to the Panel's less favourable treatment analysis, Mexico disagrees with the United States that the group of like imported products should include like imported products from all WTO Members and not just from the complaining Member. According to Mexico, the term "any

²⁰⁵European Union's third participant's submission, para. 57.

²⁰⁶European Union's third participant's submission, para. 62.

²⁰⁷European Union's third participant's submission, para. 63.

²⁰⁸European Union's third participant's submission, para. 66.

²⁰⁹European Union's third participant's submission, para. 67 (referring to Appellate Body Report, *EC – Sardines*, paras. 259-282).

²¹⁰Mexico's third participant's submission, para. 15.

²¹¹Mexico's third participant's submission, para. 16.

²¹²Mexico's third participant's submission, paras. 17-19.

²¹³Mexico's third participant's submission, para. 21.

[Member]" under Article 2.1 of the *TBT Agreement* provides "considerable flexibility" when assessing conformity with this provision, and hence the focus can be on like products from "one Member, some Members or all Members".²¹⁴ In Mexico's view, the Panel correctly focused on the treatment accorded to like products from Indonesia. In addition, contrary to the United States' argument that the Panel should have compared the treatment accorded to imported and like domestic products as a group, Mexico submits that the Panel's "efficient approach" to applying the "group" comparison when determining less favourable treatment was "not a legal error".²¹⁵ On the contrary, the Panel properly found that the "vast majority" of imports of Indonesian cigarettes with characterizing flavours were banned while "all or almost all" of the US cigarettes with characterizing flavours were excluded from the ban.²¹⁶

71. Mexico lastly addresses three additional issues concerning the less favourable treatment analysis. First, it agrees with the Panel's reasoning that a measure is discriminatory when it minimizes the costs for the domestic producers while triggering costs to the foreign producers. In Mexico's view, the Panel's approach is also applicable to any case where the technical regulation is designed in such a way that, either *de facto* or *de jure*, avoids or minimizes costs for the domestic producers and triggers costs to the foreign producers.²¹⁷ Second, with respect to the United States' argument that there is no temporal limitation on the analysis of *de facto* less favourable treatment²¹⁸, Mexico posits that the date of a panel's establishment is "the key date" when assessing whether *de facto* discrimination exists.²¹⁹ Mexico considers that, although past and possibly future events may inform an assessment of *de facto* discrimination at the time of the establishment of the panel, "great care must be taken when incorporating such facts into the assessment".²²⁰ Third, Mexico is concerned with the interpretation that the non-discrimination obligations in Article 2.1 of the *TBT Agreement* are not violated if the adverse impact is primarily the result of factors "unrelated to the foreign origin of the product".²²¹ According to Mexico, *de facto* discrimination precisely occurs, by its very nature, when the challenged measure does not, on its face, discriminate on the basis of origin.

²¹⁴Mexico's third participant's submission, para. 40. (original emphasis)

²¹⁵Mexico's third participant's submission, para. 43.

²¹⁶Mexico's third participant's submission, para. 48 (referring to Panel Report, paras. 7.276-7.279).

²¹⁷Mexico's third participant's submission, paras. 53 and 54.

²¹⁸Mexico's third participant's submission, para. 56 (referring to United States' appellant's submission, paras. 91-94).

²¹⁹Mexico's third participant's submission, para. 57.

²²⁰Mexico's third participant's submission, para. 59.

²²¹Mexico's third participant's submission, para. 65 (quoting United States' appellant's submission, para. 101; and referring to Panel Report, para. 7.259, in turn referring to Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 96).

5. Norway

72. Norway agrees with the United States that a panel's terms of reference are not limited by the products listed in a panel request.²²² In this regard, Norway is not convinced by the Panel's reasoning that "the identification of the specific products at issue in a panel request pertains to the claim at issue".²²³ In Norway's view, since the product scope of the likeness analysis may influence the outcome of a discrimination claim, a panel should be entitled to define "the product scope of its own analysis" to determine the existence of discrimination, "without being subject to limitations chosen by the complainant, for whatever reason, in its panel request".²²⁴

73. With respect to the analysis of less favourable treatment, Norway first notes that the Panel compared "one like product (i.e. clove cigarettes), from one source (i.e. Indonesia), to one like domestic product in the United States (i.e. menthol cigarettes)".²²⁵ In its view, however, the Panel should have compared the impact of the measure at issue on "all like imported products, from all WTO Members" vis-à-vis its impact "on all like domestic products".²²⁶ According to Norway, the correct starting point for the analysis should be "the entire group of products identified as like products".²²⁷ Second, Norway disagrees with the United States' assertion that, because its measure distinguishes between cigarettes "on the basis of an origin-neutral criterion *derived from a legitimate regulatory purpose*", it is WTO-consistent.²²⁸ In Norway's view, the United States appears to "stretch the Appellate Body's statement in *Dominican Republic – [Import and Sale of] Cigarettes too far*"²²⁹, to circumstances that differ from those prevailing in that dispute. A proper assessment of *de facto* discrimination turns on whether the like imported products are predominantly subject to less favourable treatment, while like domestic products are predominantly subject to more favourable treatment. If there is such *de facto* discrimination, whether a measure's policy objective justifies that discrimination belongs more properly to the analysis under an applicable exception.²³⁰

²²²Norway's third participant's submission, para. 5.

²²³Norway's third participant's submission, para. 6 (quoting Panel Report, para. 7.139).

²²⁴Norway's third participant's submission, para. 7.

²²⁵Norway's third participant's submission, para. 12 (referring to Panel Report, paras. 7.274 and 7.275). (original emphasis)

²²⁶Norway's third participant's submission, para. 12. (original emphasis)

²²⁷Norway's third participant's submission, para. 13 (referring to Panel Report, *US – Tuna (II) (Mexico)*, para. 7.295, in turn referring to Appellate Body Report, *EC – Asbestos*, para. 100). (original underlining)

²²⁸Norway's third participant's submission, para. 15. (original emphasis)

²²⁹Norway's third participant's submission, para. 20 (referring to Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 96).

²³⁰Norway's third participant's submission, para. 21.

6. Turkey

74. Turkey considers that the Panel did not commit a legal error in its general interpretation of the term "like products" in Article 2.1 of the *TBT Agreement*. In its view, the Panel properly considered the *TBT Agreement* as immediate context while also taking into account the jurisprudence on Article III:4 of the GATT 1994.²³¹ Turkey thus contends that the Panel correctly found that the declared legitimate public health objective of the measure, namely, reducing youth smoking, "must permeate and inform [its] likeness analysis".²³² Regarding the general assessment of the criteria for determining likeness, Turkey notes that the Appellate Body has rejected a "one-fits-all" approach and has advocated a case-by-case analysis.²³³ As for the end-use criterion, Turkey believes that a competition-based approach to determine likeness should not be as influential under the *TBT Agreement* as under Article III of the GATT 1994. Instead, the public health aspect of the measure "creates the immediate context".²³⁴ With respect to consumer tastes and habits, Turkey considers the Panel's focus on the relevant group of consumers—young smokers—not to be erroneous. In its view, it is not necessary to show that consumers are "actually substituting one product for the other"; rather, it is sufficient to show that consumers "can potentially substitute" them.²³⁵

75. Turkey further submits that the Panel did not commit legal error in limiting its analysis to a comparison between treatment of menthol cigarettes and clove cigarettes under Section 907(a)(1)(A) of the FFDCA. In its view, the Panel was under an obligation to make a comparison between the products specified in its terms of reference because, "at least in this case", the product specification was part of Indonesia's claim itself.²³⁶ In addition, Turkey notes that, in a less favourable treatment analysis, detrimental effects stemming from factors other than the origin of a product are "an essential issue".²³⁷ In assessing this key issue, Turkey contends, the critical benchmark is whether imported and domestic products are treated equally, taking account of all economic and social factors. Turkey therefore considers that the Panel was correct in concluding that the purpose of the *TBT Agreement* would be defeated if Members were "allowed to remove their domestic products" from the application of technical regulations "to avoid potential costs that it might otherwise incur".²³⁸

²³¹Turkey's third participant's submission, para. 4 (referring to Panel Report, para. 7.117).

²³²Turkey's third participant's submission, para. 5 (quoting Panel Report, para. 7.116).

²³³Turkey's third participant's submission, para. 7 (quoting Appellate Body Report, *EC – Asbestos*, para. 101).

²³⁴Turkey's third participant's submission, para. 11.

²³⁵Turkey's third participant's submission, para. 15.

²³⁶Turkey's third participant's submission, paras. 18 and 19.

²³⁷Turkey's third participant's submission, para. 21.

²³⁸Turkey's third participant's submission, para. 22 (quoting Panel Report, para. 7.291).

III. **Issues Raised in This Appeal**

76. The following issues are raised in this appeal:

- (a) Whether the Panel erred in finding that Section 907(a)(1)(A) of the FFDCA is inconsistent with Article 2.1 of the *TBT Agreement*, and in particular:
 - (i) Whether the Panel erred in finding that clove cigarettes and menthol cigarettes are like products within the meaning of Article 2.1 of the *TBT Agreement*, and in particular:
 - whether the Panel performed an incomplete analysis of the different end-uses of the products at issue;
 - whether the Panel erred in its analysis of consumer tastes and habits; and
 - whether the Panel acted inconsistently with Article 11 of the DSU in its assessment of consumer tastes and habits;
 - (ii) Whether the Panel erred in finding that Section 907(a)(1)(A) accords to imported clove cigarettes less favourable treatment than that accorded to domestic menthol cigarettes within the meaning of Article 2.1 of the *TBT Agreement*, and in particular:
 - whether the Panel improperly narrowed the product scope of its analysis by comparing treatment accorded to imported clove cigarettes and to domestic menthol cigarettes;
 - whether the Panel erred in assessing less favourable treatment at the time the ban on flavoured cigarettes came into effect;
 - whether the Panel erred in finding that the detrimental impact on competitive opportunities of imported clove cigarettes could not be explained by reasons unrelated to the foreign origin of those products; and
 - whether the Panel acted inconsistently with Article 11 of the DSU in finding that Section 907(a)(1)(A) accords to imported clove

cigarettes less favourable treatment than that accorded to domestic menthol cigarettes; and

(b) Whether the Panel erred in finding that, by failing to allow an interval of not less than six months between the publication and the entry into force of Section 907(a)(1)(A) of the FFDCA, the United States acted inconsistently with Article 2.12 of the *TBT Agreement*, and in particular:

- (i) whether the Panel attributed an incorrect "interpretative value" to paragraph 5.2 of the Doha Ministerial Decision in interpreting the term "reasonable interval" in Article 2.12 of the *TBT Agreement*; and
- (ii) whether the Panel incorrectly found that Indonesia had established a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement* that the United States failed to rebut.

IV. Background

77. Before commencing our analysis of the issues of law and legal interpretations raised in this appeal, we briefly outline certain pertinent facts and background information. This dispute concerns Section 907(a)(1)(A) of the United States Federal Food, Drug and Cosmetic Act²³⁹ (the "FFDCA"). Section 907(a)(1)(A) was added to the FFDCA by Section 101(b) of the Family Smoking Prevention and Tobacco Control Act²⁴⁰ (the "FSPTCA")²⁴¹, and became law on 22 June 2009.²⁴²

78. Under Section 907(a)(1)(A), beginning three months after the enactment of the FSPTCA—that is, as from 22 September 2009:

... a cigarette or any of its components (including the tobacco, filter, or paper) shall not contain, as a constituent ... or additive, an artificial or natural flavour (other than tobacco or menthol) or an herb or spice, including strawberry, grape, orange, clove, cinnamon, pineapple, vanilla, coconut, liquorice, cocoa, chocolate, cherry, or coffee, that is a characterizing flavour of the tobacco product or tobacco smoke.

79. The specific objective of Section 907(a)(1)(A) is not set forth in the FSPTCA itself. However, a report prepared by the House Energy and Commerce Committee²⁴³ (the "House Report")

²³⁹ *Supra*, footnote 2.

²⁴⁰ *Supra*, footnote 3.

²⁴¹ Panel Report, para. 2.4.

²⁴² Panel Report, para. 2.5 (referring to Indonesia's first written submission to the Panel, footnote 1 to para. 1).

²⁴³ H.R. Rep. No. 111-58, Pt. 1 (2009) (Panel Exhibits IND-2 and US-67).

articulates both the objectives of the FSPTCA overall, and of Section 907(a)(1)(A) in particular. According to the House Report, "[t]he objectives of [the FSPTCA] are to provide the Secretary with the proper authority over tobacco products in order to protect the public health and to reduce the number of individuals under 18 years of age who use tobacco products."²⁴⁴ The House Report also explains the purpose of Section 907(a)(1)(A) as follows:

Consistent with the overall intent of the bill to protect the public health, including by reducing the number of children and adolescents who smoke cigarettes, Section 907(a)(1)(A) is intended to prohibit the manufacture and sale of cigarettes with certain 'characterizing flavors' that appeal to youth.²⁴⁵

80. According to the Guidance for Industry and FDA Staff²⁴⁶ ("FDA Guidance"), Section 907(a)(1)(A) applies to all flavoured tobacco products²⁴⁷ that meet the definition of a "cigarette" in Section 3(1) of the Federal Cigarette Labeling and Advertising Act²⁴⁸, that is: "(A) any roll of tobacco wrapped in paper or in any substance not containing tobacco"; or "(B) any roll of tobacco wrapped in any substance containing tobacco which, because of its appearance, the type of tobacco used in the filler, or its packaging and labeling, is likely to be offered to, or purchased by, consumers as a cigarette described [under] (A)."²⁴⁹ The ban contained in Section 907(a)(1)(A) also extends to flavoured loose tobacco and rolling papers, and filters intended to be used in "roll-your-own" cigarettes.²⁵⁰

81. The Panel identified the products at issue in this dispute as being clove cigarettes and menthol cigarettes.²⁵¹ Clove cigarettes are composed of tobacco combined with flavouring additives, which is presented to the consumer in a paper wrapped with a filter.²⁵² More specifically, clove cigarettes are generally manufactured with 60 to 80 per cent tobacco content, usually resulting from a blend of

²⁴⁴ House Report, p. 14.

²⁴⁵ House Report, p. 37.

²⁴⁶ General Questions and Answers on the Ban of Cigarettes that Contain Characterizing Flavours (Edition 2)", 23 December 2009 (Panel Exhibit IND-41).

²⁴⁷ The Panel noted that, in referring to cigarettes *not containing any characterizing flavours*, the parties often used the terms "regular" and "tobacco-flavoured" cigarettes interchangeably, and found this ambiguity to be "susceptible of causing confusion". The Panel observed that referring to tobacco-flavoured cigarettes may confuse the reader into believing that cigarettes such as clove-flavoured or menthol-flavoured cigarettes do not contain tobacco. In fact, *all* cigarettes contain tobacco, but "flavoured" cigarettes such as menthol, kreteks, bidis, and so on, contain, as well, an additive that imparts a characterizing flavour to cigarettes. Therefore, the Panel decided to use the term "regular" cigarettes, and not "tobacco-flavoured" cigarettes, as it better describes the fact that they do not include *additional* characterizing flavours. (Panel Report, para. 7.131)

²⁴⁸ *United States Code*, Title 15, Chapter 36.

²⁴⁹ FDA Guidance, answer to Question 2.

²⁵⁰ FDA Guidance, answers to Questions 3 and 4.

²⁵¹ Panel Report, para. 7.147.

²⁵² Panel Report, para. 7.157 (referring to Indonesia's first written submission to the Panel, para. 54; and Indonesia's second written submission to the Panel, para. 67).

different varieties of tobacco.²⁵³ As for the additives, clove cigarettes contain approximately 20 to 40 per cent cloves, either in the form of clove buds or ground/minced cloves.²⁵⁴ They also generally include a "sauce" as part of the flavouring ingredients chosen by each manufacturer²⁵⁵, as well as other components inherent to cloves, such as benzyl acetate, methyl salicylate, trans-anethole, and methyl eugenol.²⁵⁶ Before the Panel, the parties did not dispute that clove cigarettes contain eugenol²⁵⁷—a substance that the United States defined as "a common topical anesthetic used in dental procedures"²⁵⁸—and they also agreed that the Polzin paper, a study on certain ingredients of Indonesian clove cigarettes, shows that 19 of 33 clove cigarette brands analyzed contained coumarin, a flavouring additive.²⁵⁹

82. Menthol cigarettes, in contrast, have approximately 90 per cent tobacco content by weight and are composed of a blend of Virginia, Maryland burley, Oriental, and reconstituted tobacco.²⁶⁰ The Panel noted that the March 2011 report by the Tobacco Products Scientific Advisory Committee to the FDA²⁶¹ (the "March 2011 TPSAC Report") specifies that "[m]enthol cigarettes are typically blended using more flue-cured and less burley tobacco ... because some of the chemicals in burley tobaccos create an incompatible taste character with menthol."²⁶² The main additive in menthol cigarettes is menthol oil, a chemical compound extracted from the peppermint plant (*Mentha piperita*), the corn mint plant (*Mentha arvensis*), or produced by synthetic or semi-synthetic means. Menthol is added to cigarettes in several different ways²⁶³ and diffuses throughout the cigarette, irrespective of the means of application.²⁶⁴ According to the March 2011 TPSAC Report, menthol is added to cigarettes both as a characterizing flavour and for other taste reasons, which include brightening the flavour of tobacco blends and/or smoothing the taste of the blend. Menthol amounts

²⁵³Panel Report, para. 7.158 (referring to S. Farrer, "Alternative Cigarettes May Deliver More Nicotine Than Conventional Cigarettes" (August 2003) 18(2) *National Institute on Drug Abuse (NIDA) Notes* (Panel Exhibit IND-29)); United States' first written submission to the Panel, para. 163; and Indonesia's and United States' responses to Panel Question 33).

²⁵⁴Panel Report, para. 7.159.

²⁵⁵Panel Report, para. 7.160 (referring to United States' first written submission to the Panel, para. 165).

²⁵⁶Panel Report, para. 7.164 (referring to Indonesia's response to Panel Question 30).

²⁵⁷Panel Report, para. 7.162.

²⁵⁸Panel Report, para. 7.161 (quoting United States' first written submission to the Panel, para. 38).

²⁵⁹Panel Report, para. 7.163 (referring to Polzin et al., "Determination of eugenol, anethole, and coumarin in the mainstream cigarette smoke of Indonesian clove cigarettes" (October 2007) 45(10) *Food & Chemical Toxicology* (Panel Exhibit US-45)); and Indonesia's and United States' responses to Panel Question 34).

²⁶⁰Panel Report, para. 7.166 (referring to United States' response to Panel Question 31). The Panel noted that Indonesia did not provide any specific information in that respect. (*Ibid.*, footnote 357 to para. 7.166)

²⁶¹Available at <http://www.fda.gov/downloads/AdvisoryCommittees/CommitteesMeetingMaterials/TobaccoProductsScientificAdvisoryCommittee/UCM247689.pdf>.

²⁶²Panel Report, para. 7.166.

²⁶³The different ways in which menthol is added to cigarettes are the following: (a) by spraying the cut tobacco during blending; (b) by applying it to the pack foil; (c) by injecting it into the tobacco stream; (d) by injecting it into the filter; (e) by inserting a crushable capsule in the filter; (f) by placing a menthol thread in the filter; or (g) any combination of the above. (Panel Report, para. 7.167)

²⁶⁴Panel Report, para. 7.167.

to roughly 1 per cent of the content of the cigarette, although the specific amount varies from brand to brand.²⁶⁵ Moreover, menthol may have cooling, analgesic, or irritating properties, and is reported to reduce sensitivity to noxious chemicals, including nicotine.²⁶⁶

83. In this Report, we first consider the United States' claim that the Panel erred in finding that clove and menthol cigarettes are like products within the meaning of Article 2.1 of the *TBT Agreement*. We then address the United States' claim that the Panel erred in finding that the United States acted inconsistently with Article 2.1 of the *TBT Agreement* by according to imported clove cigarettes less favourable treatment than that accorded to domestic menthol cigarettes. Lastly, we consider the United States' claim that the Panel erred in finding that, by not allowing a period of not less than six months between the publication and the entry into force of Section 907(a)(1)(A), the United States acted inconsistently with Article 2.12 of the *TBT Agreement*.

V. Article 2.1 of the *TBT Agreement*

A. Introduction

84. The Panel found that Section 907(a)(1)(A) of the FFDCA is a "technical regulation" within the meaning of Annex 1.1 of the *TBT Agreement*, and that it is inconsistent with Article 2.1 of the *TBT Agreement* because it accords to imported clove cigarettes less favourable treatment than that accorded to like menthol cigarettes of national origin.²⁶⁷ In particular, the Panel found that "clove cigarettes and menthol cigarettes are 'like products' for the purpose of Article 2.1 of the *TBT Agreement*"²⁶⁸, and that, "by banning clove cigarettes while exempting menthol cigarettes from the ban, Section 907(a)(1)(A) does accord imported clove cigarettes less favourable treatment than that accorded to domestic menthol cigarettes, for the purpose of Article 2.1 of the *TBT Agreement*".²⁶⁹

85. The United States appeals the Panel's finding that Section 907(a)(1)(A) is inconsistent with Article 2.1 of the *TBT Agreement*, and argues that the Panel erred in finding that clove and menthol cigarettes are like products and that Section 907(a)(1)(A) accords to imported clove cigarettes less favourable treatment than that accorded to like products of national origin within the meaning of Article 2.1 of the *TBT Agreement*. We address separately in this Report the United States' claims in respect of the Panel's findings on like products and on less favourable treatment under Article 2.1 of

²⁶⁵According to Indonesia, the menthol content can range up to 3 per cent. (Panel Report, para. 7.169 (referring to Indonesia's response to Panel Question 32))

²⁶⁶Panel Report, para. 7.168 (referring to March 2011 TPSAC Report, pp. 18-20 and 22).

²⁶⁷Panel Report, paras. 7.293, 8.1(a), and 8.1(b).

²⁶⁸Panel Report, para. 7.248.

²⁶⁹Panel Report, para. 7.292.

the *TBT Agreement*. Before doing so, however, we consider Article 2.1 as a whole in its context and in the light of the object and purpose of the *TBT Agreement*.

86. Article 2.1 of the *TBT Agreement* provides that, with respect to their central government bodies:

Members shall ensure that in respect of technical regulations, products imported from the territory of any Member shall be accorded treatment no less favourable than that accorded to like products of national origin and to like products originating in any other country.

87. Article 2.1 of the *TBT Agreement* contains a national treatment and a most-favoured nation treatment obligation. In this dispute, we are called upon to clarify the meaning of the national treatment obligation. For a violation of the national treatment obligation in Article 2.1 to be established, three elements must be satisfied: (i) the measure at issue must be a technical regulation; (ii) the imported and domestic products at issue must be like products; and (iii) the treatment accorded to imported products must be less favourable than that accorded to like domestic products. The United States' appeal concerns only the second and the third elements of this test of inconsistency, namely, whether the products at issue are like and whether the treatment accorded to clove cigarettes imported from Indonesia is less favourable than that accorded to like domestic products in the United States.²⁷⁰

88. In sections V.B and V.C of this Report, we interpret Article 2.1 of *TBT Agreement* and, in particular, the terms "like products" and "treatment no less favourable". However, before engaging in this interpretative effort, we wish to make some observations of general import on: the preamble of the *TBT Agreement*; the definition of "technical regulation"; the relevance of Article III:4 of the GATT 1994 in interpreting Article 2.1 of the *TBT Agreement*; and the absence among the provisions of the *TBT Agreement* of a general exception provision similar to Article XX of the GATT 1994.

89. The preamble of the *TBT Agreement* is part of the context of Article 2.1 and also sheds light on the object and purpose of the Agreement. We find guidance for the interpretation of Article 2.1, in particular, in the second, fifth, and sixth recitals of the preamble of the *TBT Agreement*.

90. The second recital links the *TBT Agreement* to the GATT 1994. It states:

Desiring to further the objectives of GATT 1994;

²⁷⁰We recall that it was not disputed before the Panel that Section 907(a)(1)(A) is a technical regulation and that the United States has not appealed the Panel's finding that Section 907(a)(1)(A) is a technical regulation within the meaning of Annex 1.1 to the *TBT Agreement* (Panel Report, paras. 7.21 and 7.41).

91. While this recital may be read as suggesting that the *TBT Agreement* is a "development" or a "step forward" from the disciplines of the GATT 1994²⁷¹, in our view, it also suggests that the two agreements overlap in scope and have similar objectives. If this were not true, the *TBT Agreement* could not serve to "further the objectives" of the GATT 1994. The second recital indicates that the *TBT Agreement* expands on pre-existing GATT disciplines and emphasizes that the two Agreements should be interpreted in a coherent and consistent manner.

92. The fifth recital reflects the trade-liberalization objective of the *TBT Agreement* by expressing the "desire" that technical regulations, technical standards, and conformity assessment procedures do not create unnecessary obstacles to international trade. It states:

Desiring however to ensure that technical regulations and standards, including packaging, marking and labelling requirements, and procedures for assessment of conformity with technical regulations and standards do not create unnecessary obstacles to international trade;

93. We see the fifth recital reflected in those TBT provisions that aim at reducing obstacles to international trade and that limit Members' right to regulate, for instance, by prohibiting discrimination against imported products (Article 2.1) or requiring that technical regulations be no more trade restrictive than necessary to fulfil a legitimate objective (Article 2.2).

94. The objective of avoiding the creation of unnecessary obstacles to international trade through technical regulations, standards, and conformity assessment procedures is, however, qualified in the sixth recital by the explicit recognition of Members' right to regulate in order to pursue certain legitimate objectives. The sixth recital states:

Recognizing that no country should be prevented from taking measures necessary to ensure the quality of its exports, or for the protection of human, animal or plant life or health, of the environment, or for the prevention of deceptive practices, at the levels it considers appropriate, subject to the requirement that they are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail or a disguised restriction on international trade, and are otherwise in accordance with the provisions of this Agreement;

95. We read the sixth recital as counterbalancing the trade-liberalization objective expressed in the fifth recital. The sixth recital "recognizes" Members' right to regulate versus the "desire" to avoid creating unnecessary obstacles to international trade, expressed in the fifth recital. While the fifth recital clearly suggests that Members' right to regulate is not unbounded, the sixth recital affirms

²⁷¹Panel Report, para. 7.112.

that such a right exists while ensuring that trade-distortive effects of regulation are minimized. The sixth recital suggests that Members' right to regulate should not be constrained if the measures taken are necessary to fulfil certain legitimate policy objectives, and provided that they are not applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade, and are otherwise in accordance with the provisions of the Agreement. We thus understand the sixth recital to suggest that Members have a right to use technical regulations in pursuit of their legitimate objectives, provided that they do so in an even-handed manner and in a manner that is otherwise in accordance with the provisions of the *TBT Agreement*.

96. The balance set out in the preamble of the *TBT Agreement* between, on the one hand, the desire to avoid creating unnecessary obstacles to international trade and, on the other hand, the recognition of Members' right to regulate, is not, in principle, different from the balance set out in the GATT 1994, where obligations such as national treatment in Article III are qualified by the general exceptions provision of Article XX.

97. We observe that Article 2.1 of the *TBT Agreement* applies only in respect of technical regulations, which are defined in Annex I.1 as "[d]ocument[s] which lay[] down product characteristics or their related processes and production methods, including the applicable administrative provisions, with which compliance is mandatory".²⁷² Product characteristics laid down in a technical regulation may themselves be relevant to the determination of whether products are like within the meaning of Article 2.1. Thus, we consider that, in the case of technical regulations, the measure itself *may* provide elements that are relevant to the determination of whether products are like and whether less favourable treatment has been accorded to imported products.

98. The definition of technical regulations as documents laying down product characteristics gives an indication that, under the *TBT Agreement*, measures making distinctions based on product characteristics are in principle permitted. However, the fact that a technical regulation defines a product's characteristics with a view to fulfilling a legitimate policy objective does not mean that it may do so by treating imported products less favourably than like domestic products.

99. We note that the language of the national treatment obligation of Article 2.1 of the *TBT Agreement* closely resembles the language of Article III:4 of the GATT 1994. Article III:4 of the GATT 1994 reads, in relevant part:

²⁷²The second sentence of Annex I.1 reads as follows: "It may also include or deal exclusively with terminology, symbols, packaging, marking or labelling requirements as they apply to a product, process or production method".

The products of the territory of any Member imported into the territory of any other Member shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use.

100. The national treatment obligations of Article 2.1 and Article III:4 are built around the same core terms, namely, "like products" and "treatment no less favourable". We further note that technical regulations are in principle subject not only to Article 2.1 of the *TBT Agreement*, but also to the national treatment obligation of Article III:4 of the GATT 1994, as "laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use" of products. The very similar formulation of the provisions, and the overlap in their scope of application in respect of technical regulations, confirm that Article III:4 of the GATT 1994 is relevant context for the interpretation of the national treatment obligation of Article 2.1 of the *TBT Agreement*.²⁷³ We consider that, in interpreting Article 2.1 of the *TBT Agreement*, a panel should focus on the text of Article 2.1, read in the context of the *TBT Agreement*, including its preamble, and also consider other contextual elements, such as Article III:4 of the GATT 1994.²⁷⁴

101. Finally, we observe that the *TBT Agreement* does not contain among its provisions a general exceptions clause. This may be contrasted with the GATT 1994, which contains a general exceptions clause in Article XX.

102. With these observations of general import in mind, we turn to the United States' appeal of the Panel's findings that clove and menthol cigarettes are like products, and that Section 907(a)(1)(A) accords imported clove cigarettes from Indonesia less favourable treatment than that accorded to like domestic menthol cigarettes, within the meaning of Article 2.1 of the *TBT Agreement*.

B. *The Panel's Finding that Clove Cigarettes and Menthol Cigarettes are "Like Products" within the Meaning of Article 2.1 of the TBT Agreement*

103. We begin our analysis by addressing the Panel's interpretation of the concept of "like products" under Article 2.1 of the *TBT Agreement*. We then turn to the United States' claims that the

²⁷³We recall that, in *EC – Asbestos*, the Appellate Body found that the terms used in one provision "must be interpreted in light of the context, and of the object and purpose, of the provision at issue, and of the object and purpose of the covered agreement in which the provision appears" and that the meaning attributed to the same terms in other provisions of the same agreement or in other covered agreements, may also be relevant context. (Appellate Body Report, *EC – Asbestos*, paras. 88-89)

²⁷⁴In setting out its interpretative approach to Article 2.1 of the *TBT Agreement*, the Panel considered that, "[e]ven if the GATT 1994 were considered to serve as context for Article 2.1 of the *TBT Agreement*, it would not be the immediate context of that provision" and that "an interpreter should first assess the immediate context of the provision subject to interpretation before reaching for an interpretative aid that is further removed." (Panel Report, para. 7.103)

Panel erred in its interpretation and application of the "likeness" criteria of end-use and consumer tastes and habits, as well as to its claim that the Panel acted inconsistently with Article 11 of the DSU in its assessment of consumer tastes and habits. The United States does not appeal the Panel's findings concerning the products' physical characteristics and tariff classification.

1. "Like Products" under Article 2.1 of the TBT Agreement

104. The Panel found that clove cigarettes and menthol cigarettes are like products within the meaning of Article 2.1 of the *TBT Agreement*.²⁷⁵ The Panel reached this conclusion after having evaluated the traditional "likeness" criteria (physical characteristics, end-uses, consumer tastes and habits, and tariff classification), "bearing in mind that the measure at issue is a technical regulation, with the immediate purpose of regulating cigarettes having a characterizing flavour, with a view to attaining the legitimate objective of reducing youth smoking".²⁷⁶ Before addressing the United States' appeal of the Panel's specific findings in respect of the "likeness" criteria of end-uses and consumer tastes and habits, we first consider the Panel's approach to interpreting "like products" in the context of Article 2.1 of the *TBT Agreement*.

105. The Panel considered that "it is far from clear that it is always appropriate to transpose automatically the competition-oriented approach to likeness under Article III:4 of the GATT 1994 to Article 2.1 of the *TBT Agreement*" in the absence of a general principle such as that expressed in Article III:1 of the GATT 1994.²⁷⁷ The Panel also noted that, despite the similarity in wording, Article 2.1 of the *TBT Agreement* and Article III:4 of the GATT 1994 differ in that the former only applies to technical regulations whereas the latter applies to a much broader range of measures.²⁷⁸ The Panel stated that Article III:4 of the GATT 1994 could not be regarded as immediate context to Article 2.1 of the *TBT Agreement* and noted that the Appellate Body's reference to an "accordion" of "likeness" allows, and potentially mandates, different interpretations of the term "like products" under Article III:4 of the GATT 1994 and Article 2.1 of the *TBT Agreement*.²⁷⁹

106. The Panel turned to what it considered the immediate context of the term "like products" in Article 2.1 of the *TBT Agreement*, namely, Article 2.1 itself and the *TBT Agreement* as a whole, and to that Agreement's object and purpose as set out in its preamble. The Panel considered that the fact that Section 907(a)(1)(A) of the FFDCA is a technical regulation within the meaning of Annex 1.1 of the *TBT Agreement*, which has the immediate purpose of regulating cigarettes with characterizing flavours with the view to attaining the legitimate objective of reducing youth smoking, should have

²⁷⁵Panel Report, para. 7.248.

²⁷⁶Panel Report, para. 7.244.

²⁷⁷Panel Report, para. 7.99.

²⁷⁸Panel Report, para. 7.106.

²⁷⁹Panel Report, para. 7.105.

"some weight and potentially considerable weight" in the determination of whether the products at issue are like.²⁸⁰ The Panel also noted that the sixth recital of the preamble of the *TBT Agreement*, which recognizes Members' right to take measures for legitimate objectives, and Article 2.2 could justify a different interpretation of "likeness" under Article 2.1 of the *TBT Agreement* from that developed under Article III:4 of the GATT 1994.²⁸¹

107. The Panel thus found that, in the circumstances of this case, the interpretation of Article 2.1 of the *TBT Agreement* should not be approached primarily from a competition-oriented perspective, but that the weighing of the evidence relating to the "likeness" criteria should be influenced by the fact that Section 907(a)(1)(A) is a technical regulation having the immediate purpose of regulating cigarettes with a characterizing flavour for public health reasons.²⁸² Having developed this interpretative approach, the Panel turned to the analysis of the traditional "likeness" criteria, namely, the physical characteristics of the products, end-uses, consumer tastes and habits, and tariff classification. The Panel gave particular weight to the health objective of Section 907(a)(1)(A) in its assessment of the products' physical characteristics and of consumer tastes and habits.²⁸³

108. We agree with the Panel that the interpretation of the term "like products" in Article 2.1 of the *TBT Agreement* should start with the text of that provision in the light of the context provided by Article 2.1 itself, by other provisions of the *TBT Agreement*, and by the *TBT Agreement* as a whole. We also agree that the relevant context includes the fact that Article 2.1 applies to technical regulations, which are documents laying down the characteristics of products. We further note that the preamble of the *TBT Agreement* recognizes Members' right to regulate through technical regulations. As explained below, however, we are not persuaded that these contextual elements and the object and purpose of the *TBT Agreement* suggest that the interpretation of the concept of "like products" in Article 2.1 of the *TBT Agreement* cannot be approached from a competition-oriented perspective.

109. As we have observed above, the balance that the preamble of the *TBT Agreement* strikes between, on the one hand, the pursuit of trade liberalization and, on the other hand, Members' right to regulate, is not, in principle, different from the balance that exists between the national treatment obligation of Article III and the general exceptions provided under Article XX of the GATT 1994. The second recital of the preamble links the two Agreements by expressing the "desire" "to further the objectives of the GATT 1994", while the "recognition" of a Member's right to regulate in the sixth recital is balanced by the "desire" expressed in the fifth recital to ensure that technical

²⁸⁰Panel Report, para. 7.109.

²⁸¹Panel Report, para. 7.114.

²⁸²Panel Report, para. 7.119.

²⁸³Panel Report, para. 7.119.

regulations, standards, and conformity assessment procedures do not create unnecessary obstacles to international trade. We note, however, that in the GATT 1994 this balance is expressed by the national treatment rule in Article III:4 as qualified by the exceptions in Article XX, while, in the *TBT Agreement*, this balance is to be found in Article 2.1 itself, read in the light of its context and of its object and purpose.

110. The Panel was also of the view that the absence of a provision like Article III:1 of the GATT 1994 in the *TBT Agreement* would prevent the transposition of the GATT competition-oriented approach to likeness to Article 2.1 of the *TBT Agreement*.²⁸⁴ Article III:1 provides that internal fiscal and regulatory measures "should not be applied to imported or domestic products so as to afford protection to domestic production". We observe, in this respect, that, in *EC – Asbestos*, the Appellate Body considered that the "general principle" articulated in Article III:1 of the GATT 1994 "seeks to prevent Members from applying internal taxes and regulations in a manner which affects the competitive relationship, in the marketplace, between the domestic and imported products involved, 'so as to afford protection to domestic production'".²⁸⁵ However, the Appellate Body did not base its conclusion that "likeness" in Article III:4 is about the "nature and extent of a competitive relationship between and among products"²⁸⁶ exclusively on the "general principle" expressed in Article III:1. Rather, the Appellate Body further clarified that "the word 'like' in Article III:4 is to be interpreted to apply to products that are in ... a competitive relationship", because it is "products that are in a competitive relationship in the marketplace [that] could be affected through treatment of imports' less favourable' than the treatment accorded to domestic products".²⁸⁷

111. We agree that the very concept of "treatment no less favourable", which is expressed in the same words in Article III:4 of the GATT 1994 and in Article 2.1 of the *TBT Agreement*, informs the determination of likeness, suggesting that likeness is about the "nature and extent of a competitive relationship between and among products". Indeed, the concept of "treatment no less favourable" links the products to the marketplace, because it is only in the marketplace that it can be determined how the measure treats like imported and domestic products. We note, however, that, in determining likeness based on the competitive relationship between and among the products, a panel should discount any distortive effects that the measure at issue may itself have on the competitive relationship, and reserve the consideration of such effects for the analysis of less favourable treatment. In such cases, a panel should determine the nature and the extent of the competitive relationship for

²⁸⁴Panel Report, para. 7.99.

²⁸⁵Appellate Body Report, *EC – Asbestos*, para. 98. (original emphasis)

²⁸⁶Appellate Body Report, *EC – Asbestos*, para. 99.

²⁸⁷Appellate Body Report, *EC – Asbestos*, para. 99. (original emphasis)

the purpose of determining likeness in isolation from the measure at issue, to the extent that the latter informs the physical characteristics of the products and/or consumers' preferences.

112. In the light of the above, we disagree with the Panel that the text and context of the *TBT Agreement* support an interpretation of the concept of "likeness" in Article 2.1 of the *TBT Agreement* that focuses on the legitimate objectives and purposes of the technical regulation, rather than on the competitive relationship between and among the products.

113. We further observe that measures often pursue a multiplicity of objectives, which are not always easily discernible from the text or even from the design, architecture, and structure of the measure. Determining likeness on the basis of the regulatory objectives of the measure, rather than on the products' competitive relationship, would require the identification of all the relevant objectives of a measure, as well as an assessment of which objectives among others are relevant or should prevail in determining whether the products are like. It seems to us that it would not always be possible for a complainant or a panel to identify all the objectives of a measure and/or be in a position to determine which among multiple objectives are relevant to the determination of whether two products are like, or not.²⁸⁸

114. The appeal by the United States of the Panel's determination of consumer tastes and habits, which we address further below, highlights the difficulties that arise when attempting to determine likeness based on the regulatory purposes of the measure rather than on the competitive relationship between and among products. The Panel relied on the objective of the measure at issue, which it identified as reducing youth smoking, to determine the likeness of the products.²⁸⁹ The United States questions the basis for the Panel's narrow focus on the immediate objective of the measure²⁹⁰ and cites to other regulatory objectives related to health considerations associated with heavily used cigarettes to draw further distinctions between menthol and clove cigarettes.²⁹¹

115. Measures, such as technical regulations, may have more than one objective. However, a panel that is tasked with determining whether two products are like may not be able to reach a coherent result if, in determining likeness, it has to rely on various possible regulatory objectives of the measure. If a panel were to focus on one of the objectives of a measure to the exclusion of all others that are equally important, it may reach a somewhat arbitrary result in the determination of what are the like products at issue which, in turn, has implications for the determination of whether

²⁸⁸See Panel Report, *Japan – Alcoholic Beverages II*, para. 6.16.

²⁸⁹Panel Report, para. 7.119.

²⁹⁰United States' appellant's submission, para. 60.

²⁹¹The United States cites to "possible countervailing public health factors" associated with banning heavily used cigarettes, such as "possible increases in unregulated black market cigarettes or strain to the healthcare system". (United States' appellant's submission, para. 61)

less favourable treatment has been accorded. Moreover, we note that a purpose-based approach to the determination of likeness does not, necessarily, leave more regulatory autonomy for Members, because it almost invariably puts panels into the position of having to determine which of the various objectives purportedly pursued by Members are more important, or which of these objectives should prevail in determining likeness or less favourable treatment in the event of conflicting objectives.

116. More importantly, however, we do not consider that the concept of "like products" in Article 2.1 of the *TBT Agreement* lends itself to distinctions between products that are based on the regulatory objectives of a measure. As we see it, the concept of "like products" serves to define the scope of products that should be compared to establish whether less favourable treatment is being accorded to imported products. If products that are in a sufficiently strong competitive relationship to be considered like are excluded from the group of like products on the basis of a measure's regulatory purposes, such products would not be compared in order to ascertain whether less favourable treatment has been accorded to imported products. This would inevitably distort the less favourable treatment comparison, as it would refer to a "marketplace" that would include some like products, but not others. As we consider further below in respect of the United States' appeal of the Panel's less favourable treatment finding, distinctions among products that have been found to be like are better drawn when considering, subsequently, whether less favourable treatment has been accorded, rather than in determining likeness, because the latter approach would alter the scope and result of the less favourable treatment comparison.

117. Nevertheless, in concluding that the determination of likeness should not be based on the regulatory purposes of technical regulations, we are not suggesting that the regulatory concerns underlying technical regulations may not play a role in the determination of whether or not products are like. In this respect, we recall that, in *EC – Asbestos*, the Appellate Body found that regulatory concerns and considerations may play a role in applying certain of the "likeness" criteria (that is, physical characteristics and consumer preferences) and, thus, in the determination of likeness under Article III:4 of the GATT 1994.

118. In *EC – Asbestos*, the Appellate Body found that, in examining whether products are like, panels must evaluate all relevant evidence, including evidence relating to the health risks associated with a product, which was the underlying concern of the challenged measure in that dispute. The Appellate Body found that such evidence would not be examined as a separate criterion but, rather, under the traditional "likeness" criteria. In particular, the Appellate Body stated that a product's health risks are relevant to the determination of the competitive relationship between products, and addressed health risks as part of the products' physical characteristics and of the tastes and habits of

consumers.²⁹² In respect of physical characteristics, the Appellate Body considered that a panel should examine fully the physical properties of products, in particular, those physical properties that are likely to influence the competitive relationship between products in the marketplace. These include those physical properties that make a product toxic or otherwise dangerous to health.²⁹³ In respect of consumer tastes and habits, the Appellate Body found that the health risks associated with a product could influence the preference of consumers.²⁹⁴

119. Similarly, we consider that the regulatory concerns underlying a measure, such as the health risks associated with a given product, may be relevant to an analysis of the "likeness" criteria under Article III:4 of the GATT 1994, as well as under Article 2.1 of the *TBT Agreement*, to the extent they have an impact on the competitive relationship between and among the products concerned.

120. The interpretation of the concept of "likeness" in Article 2.1 has to be based on the text of that provision as read in the context of the *TBT Agreement* and of Article III:4 of the GATT 1994, which also contains a similarly worded national treatment obligation that applies to laws, regulations, and requirements including technical regulations. In the light of this context and of the object and purpose of the *TBT Agreement*, as expressed in its preamble, we consider that the determination of likeness under Article 2.1 of the *TBT Agreement*, as well as under Article III:4 of the GATT 1994, is a determination about the nature and extent of a competitive relationship between and among the products at issue. To the extent that they are relevant to the examination of certain "likeness" criteria and are reflected in the products' competitive relationship, regulatory concerns underlying technical regulations may play a role in the determination of likeness.

121. With this interpretative approach in mind, we now turn to the claims by the United States that the Panel committed errors in its assessments of the end-uses of clove and menthol cigarettes and of the tastes and habits of consumers of clove and menthol cigarettes, as well as to the United States' claim that the Panel acted inconsistently with Article 11 of the DSU in its assessment of consumer tastes and habits. We begin by examining the Panel's finding that clove and menthol cigarettes have the same end-use.

²⁹²Appellate Body Report, *EC – Asbestos*, para. 113.

²⁹³The Appellate Body noted that a characteristic of chrysotile asbestos fibres was that the microscopic particles and filaments of these fibres were carcinogenic for humans when inhaled. Thus, the Appellate Body concluded that the carcinogenicity, or toxicity, constituted a defining aspect of the physical properties of chrysotile asbestos fibres as opposed to polyvinyl alcohol, cellulose, and glass (PCG) fibres, which did not present the same health risk. (Appellate Body Report, *EC – Asbestos*, para. 114)

²⁹⁴The Appellate Body found that the health risks associated with chrysotile asbestos fibres influenced the behaviour of both manufacturers (who incorporate fibres into another product) and ultimate consumers. The Appellate Body noted that a manufacturer cannot ignore the preferences of the ultimate consumers of a product and, if the risks posed by a particular product are sufficiently great, the ultimate consumers may simply cease to buy that product. (Appellate Body Report, *EC – Asbestos*, para. 122)

2. End-Uses

122. In examining the end-uses of clove and menthol cigarettes, the Panel found that both clove and menthol cigarettes have the same end-use, that is, "to be smoked"²⁹⁵, and disagreed with the United States that the end-uses of a cigarette include "satisfying an addiction to nicotine" and "creating a pleasurable experience associated with the taste of the cigarette and the aroma of the smoke". The Panel considered that the end-uses presented by the United States relate to the reasons why people smoke, but that does not mean that cigarettes have several end-uses.²⁹⁶ In particular, the Panel considered that the United States' comments on the appeal of flavours to certain smokers relate more properly to consumer tastes and habits than to end-use.²⁹⁷

123. The United States claims that a panel, when conducting an end-use analysis, must consider the different uses of the products and not just the use that is a "common denominator" of the products in question.²⁹⁸ According to the United States, it is undisputed that both clove and menthol cigarettes are used for smoking, but the Panel improperly limited its analysis to considering only this common use between the products while ignoring other relevant end-uses. Menthol cigarettes, the United States posits, are used to "satisfy the nicotine addictions of millions of smokers in the United States", whereas clove cigarettes are primarily used "for experimentation and special social settings" and generally are not smoked to satisfy nicotine addiction in the US market.²⁹⁹

124. Indonesia responds that the Panel did not err in finding that the end-use of clove and menthol cigarettes is "to be smoked". In Indonesia's view, moreover, even assuming *arguendo* that the end-uses put forward by the United States were pertinent ones, the United States presented no evidence showing that clove and menthol cigarettes were not both *capable* of performing the end-uses of satisfying a nicotine addiction and creating a pleasurable experience.³⁰⁰

125. We observe that end-uses describe the possible functions of a product, while consumer tastes and habits reflect the consumers' appreciation of these functions. In *EC – Asbestos*, the Appellate Body described end-uses as "the extent to which products are *capable* of performing the same, or similar, functions" and consumer tastes and habits as "the extent to which consumers are willing to

use the products to perform these functions".³⁰¹ That a product is not principally used to perform a certain function does not exclude that it may nevertheless be *capable* of performing that function.

126. The Appellate Body has also considered that, while each criterion addresses, in principle, a different aspect of the products involved, which should be examined separately, the different criteria are "interrelated"³⁰² and "not mutually exclusive", so that certain evidence may well fall under more than one criterion.³⁰³ Thus, in our view, that consumers smoke to satisfy an addiction or that they smoke for pleasure are relevant to the examination of both end-uses and consumer tastes and habits, although different aspects are addressed in the analysis of these two separate "likeness" criteria.

127. We do not consider that it is correct to characterize "satisfying an addiction to nicotine" and "creating a pleasurable experience associated with the taste of the cigarette and the aroma of the smoke" as consumer tastes and habits and not end-uses. To the extent that they describe possible functions of the products, rather than the consumers' appreciation of these functions, they represent, in fact, different end-uses of the products at issue, rather than consumer tastes and habits. Consumer tastes and habits should indicate to what extent consumers are willing to substitute clove cigarettes and menthol cigarettes to "satisfy an addiction to nicotine" and/or to "create a pleasurable experience associated with the taste of the cigarette and the aroma of the smoke".

128. We also recall that, in *EC – Asbestos*, the Appellate Body found that the panel had not provided a complete picture of the various end-uses of the different fibres at issue, because its analysis was based on a "small number of applications" for which the products were substitutable, and because it had failed to examine other, different end-uses for the products. The Appellate Body noted that it is only by forming a complete picture of the various end-uses of a product that a panel can assess the significance of the fact that products share a limited number of end-uses.³⁰⁴

129. An analysis of end-use should be comprehensive and specific enough to provide meaningful guidance as to whether the products in question are like products. It is not disputed that both clove and menthol cigarettes are "to be smoked". Nevertheless, "to be smoked" does not exhaustively describe the functions of cigarettes. As a consequence, to find, as the Panel did, that the end-use of both clove and menthol cigarettes is "to be smoked" does not, in our view, provide sufficient guidance as to whether such products are like products within the meaning of Article 2.1 of the *TBT Agreement*.

³⁰¹ Appellate Body Report, *EC – Asbestos*, para. 117. (emphasis added)

³⁰² Appellate Body Report, *EC – Asbestos*, para. 102.

³⁰³ Appellate Body Reports, *Philippines – Distilled Spirits*, para. 131. In that dispute, the Appellate Body considered that factors such as the perceptibility of differences among the products and the products' presentation and labelling concern both physical characteristics and consumer tastes and habits. (*Ibid.*, paras. 128 and 132)

³⁰⁴ Appellate Body Report, *EC – Asbestos*, para. 119.

²⁹⁵ Panel Report, para. 7.199.

²⁹⁶ Panel Report, para. 7.198.

²⁹⁷ Panel Report, para. 7.197.

²⁹⁸ United States' appellant's submission, para. 45.

²⁹⁹ United States' appellant's submission, para. 46.

³⁰⁰ Indonesia's appellee's submission, para. 73.

Also cigars, loose tobacco, and herbs share the same end-use of being "smoked", although this does not say much as to whether all these products are like.³⁰⁵

130. In our view, the Panel did not perform an analysis of the end-uses of clove and menthol cigarettes that was sufficiently comprehensive and specific to provide significant indications as to the likeness of these products. We agree with the United States that there are more specific permutations and functions of "smoking", which are relevant to the end-uses of cigarettes, such as "satisfying an addiction to nicotine" and "creating a pleasurable experience associated with the taste of the cigarette and the aroma of the smoke". The Panel should have considered these permutations and functions in its evaluation of whether the products at issue are like. We also note, however, the argument by Indonesia that, even assuming that the end-uses put forward by the United States were "legitimate end-uses", the United States did not show that clove and menthol cigarettes were not both *capable* of performing the functions of "satisfying an addiction to nicotine" and "creating a pleasurable experience associated with the taste of the cigarette and the aroma of the smoke".³⁰⁶

131. The United States argues on appeal that menthol cigarettes are used to satisfy the nicotine addictions of millions of smokers in the United States, while clove cigarettes are primarily used for experimentation and special social settings and generally are not used to satisfy addiction. The Panel, however, found that "both menthol and clove cigarettes appeal to youth because of the presence of an additive that gives them a characterizing flavour having the effect of masking the harshness of tobacco".³⁰⁷ Both types of cigarettes are capable of performing a social/experimentation function and, thus, share the end-use of "creating a pleasurable experience associated with the taste of the cigarette and the aroma of the smoke". At the same time, both clove and menthol cigarettes are capable of performing the function of "satisfying an addiction to nicotine", considering that both types of cigarettes contain nicotine, whose addictiveness is scientifically proven.³⁰⁸ The fact that more "addicts" smoke menthol than clove cigarettes does not mean that clove cigarettes cannot be smoked to "satisfy an addiction to nicotine". As we have observed above, what matters in determining a product's end-use is that a product is *capable* of performing it, not that such end-use represents the principal or the most common end-use of that product.

³⁰⁵ Similarly, to state that the end-use of alcoholic beverages is "to be drunk" would not distinguish alcoholic beverages from water, milk, or orange juice that are also consumed by drinking. In contrast, in *Philippines – Distilled Spirits*, the specific end-use of alcoholic beverages was described as "thirst quenching, socialization, relaxation, pleasant intoxication". (Appellate Body Reports, *Philippines – Distilled Spirits*, para. 171 (quoting Panel Reports, *Philippines – Distilled Spirits*, para. 7.81))

³⁰⁶ Indonesia's appellee's submission, para. 73.

³⁰⁷ Panel Report, para. 7.231.

³⁰⁸ In its response to Panel Question 37, the United States notes that, "[w]ith respect to the addictive effects of regular, menthol and clove cigarettes, all of these products contain nicotine and are thus addictive." (United States' response to Panel Question 37, para. 85)

132. In the light of the above, we disagree with the Panel that the end-use of cigarettes is simply "to be smoked" and agree with the United States that there are more specific end-uses of cigarettes such as "satisfying an addiction to nicotine" and "creating a pleasurable experience associated with the taste of the cigarette and the aroma of the smoke". We consider, however, that, based on the Panel's findings referred to above, it can be concluded that both clove and menthol cigarettes share the end-uses of "satisfying an addiction to nicotine" and "creating a pleasurable experience associated with the taste of the cigarette and the aroma of the smoke". Accordingly, we consider that the more specific products' end-uses put forward by the United States also support the Panel's overall finding that clove and menthol cigarettes are like products.

3. Consumer Tastes and Habits

133. In addressing consumer tastes and habits in respect of clove and menthol cigarettes, the Panel stated that the legitimate objective of Section 907(a)(1)(A) of the FFDCA, namely, reducing youth smoking, delimited the scope of the consumers whose tastes and habits should be examined under this criterion.³⁰⁹ Accordingly, the Panel considered it appropriate to examine the substitutability of clove and menthol cigarettes from the perspective of the relevant group of consumers, which included young smokers and those ready to become smokers (potential consumers).³¹⁰ The Panel found that the evidence submitted by the parties showed that both clove and menthol cigarettes, because of their characterizing flavours, which help to mask the harshness of tobacco, appeal to youth and are better vehicles for youth to start smoking than regular cigarettes.³¹¹ Therefore, the Panel concluded that, from the point of view of the consumers at issue in this case, menthol-flavoured and clove-flavoured cigarettes are "similar for the purpose of starting to smoke".³¹²

134. The United States claims that the Panel erred in considering the tastes and habits of only young smokers and potential young smokers, and not of current adult smokers. The United States notes that Section 907(a)(1)(A) makes regulatory distinctions among cigarettes based not only on their appeal to young and potential smokers, but also on their use by current adult smokers.³¹³ The United States argues that nothing in the text of Article 2.1 of the *TBT Agreement* provides a basis for the Panel to have limited its consideration of the public health distinctions drawn under the measure according to what the Panel construed to be the immediate objective of the measure.³¹⁴

³⁰⁹ Panel Report, para. 7.206.

³¹⁰ Panel Report, para. 7.214.

³¹¹ Panel Report, para. 7.217.

³¹² Panel Report, para. 7.232.

³¹³ United States' appellant's submission, para. 54.

³¹⁴ United States' appellant's submission, para. 60.

135. The United States contends that a like product analysis under Article 2.1 must take account of the regulatory distinctions drawn under the measure at issue, which are not limited to the immediate or primary objective of a measure, but that often reflect a balancing of other considerations relevant to the public welfare. In particular, the United States argues that, even though the primary or immediate purpose of Section 907(a)(1)(A) is to reduce youth smoking, the measure was developed based on a consideration of the health benefits, risks, and consequences to the population as a whole, including the possible negative consequences of banning a type of cigarette, such as menthol cigarettes, to which millions of adults are chemically and psychologically addicted.³¹⁵

136. We have disagreed with the Panel's approach to interpreting the concept of "likeness" in Article 2.1 of the *TBT Agreement* in the light of the regulatory objectives of the measure, rather than based on the competitive relationship between and among the products.³¹⁶ In particular, we have observed that the context of the *TBT Agreement* and its object and purpose do not suggest that the regulatory objectives of a technical regulation should play a role that is separate from the determination of a competitive relationship between and among products. We have also noted that determining likeness primarily in the light of the regulatory objectives of the measure is further complicated by the fact that measures, including technical regulations, often have multiple objectives. In contrast, we have considered that the determination of likeness under Article 2.1 of the *TBT Agreement* is a determination about the nature and the extent of a competitive relationship between and among products, and that the regulatory concerns that underlie a measure may be considered to the extent that they have an impact on the competitive relationship.³¹⁷

137. In the light of the above, we also consider that the Panel was wrong in confining its analysis of consumer tastes and habits to those consumers (young and potential young smokers) that are the concern of the objective of the regulation (to reduce youth smoking). In an analysis of likeness based on products' competitive relationship, it is the market that defines the scope of consumers whose preferences are relevant. The proportion of youth and adults smoking different types of cigarettes may vary, but clove, menthol, and regular cigarettes are smoked by both young and adult smokers. To evaluate the degree of substitutability among these products, the Panel should have assessed the tastes and habits of all relevant consumers of the products at issue, not only of the main consumers of clove and menthol cigarettes, particularly where it is clear that an important proportion of menthol cigarette smokers are adult consumers.

³¹⁵United States' appellant's submission, para. 62. The United States cites in particular to "possible increases in unregulated black market cigarettes or strain to the healthcare system". (United States' appellant's submission, para. 61)

³¹⁶Section V.B.1 of this Report.

³¹⁷See *supra*, para. 119.

138. Moreover, without at this stage entering into the merits of the other objectives of the regulation advocated by the United States, the Panel's approach discounts the fact that the technical regulation at issue may also have other objectives that concern other actual and potential consumers of the products at issue. Therefore, we disagree with the Panel that the legitimate objective of Section 907(a)(1)(A), that is, reducing youth smoking, delimits the scope of the consumers whose tastes and habits should be examined to young smokers and potential young smokers.³¹⁸

139. Having determined that the Panel was wrong in confining its analysis of consumer tastes and habits to young and potential young smokers, we now consider whether the Panel's failure to evaluate the tastes and habits of current adult consumers of menthol cigarettes undermines the proposition that there is a sufficient degree of substitutability between clove and menthol cigarettes to support an overall finding of likeness under Article 2.1 of the *TBT Agreement*.

140. The United States claims that "[e]vidence comparing the tastes and habits of younger, potential smokers and the tastes and habits of older, established smokers is directly relevant to the issue of consumer tastes and habits", because clove cigarettes are smoked disproportionately by youth, while menthol cigarettes are smoked more evenly among young and adult smokers. Accordingly, the United States argues, clove cigarettes present a unique risk to young, uninitiated smokers and have little to no impact on adults, while menthol cigarettes are a risk to young, uninitiated smokers, but also have a significant impact on adults.³¹⁹

141. Indonesia submits that the United States failed to present evidence showing that consumers, whether adult or youth, would be unwilling to substitute clove and menthol cigarettes for the end-use of smoking. Indonesia argues that the United States is wrong in presuming that consumer tastes and habits must be identical to be like, considering that the Appellate Body found that products that are close to being perfectly substitutable can be like products. Indonesia contends that there is sufficient evidence on record supporting the fact that young smokers and pre-smoking youth view clove and menthol cigarettes "as at least close to substitutable".³²⁰

142. We consider that, in order to determine whether products are like under Article 2.1 of the *TBT Agreement*, it is not necessary to demonstrate that the products are substitutable for all consumers or that they actually compete in the entire market. Rather, if the products are highly substitutable for some consumers but not for others, this may also support a finding that the products are like. In *Philippines – Distilled Spirits*, the Appellate Body considered that the standard of "directly

³¹⁸Panel Report, paras. 7.206.

³¹⁹United States' appellant's submission, para. 55.

³²⁰Indonesia's appellee's submission, para. 82 (referring to Appellate Body Reports, *Philippines – Distilled Spirits*, para. 149).

competitive or substitutable" relating to Article III:2, second sentence, of the GATT 1994 is satisfied even if competition does not take place in the whole market but is limited to a segment of the market. The Appellate Body found that "it was reasonable for the [panel] to draw, from the Philippines' argument that imported distilled spirits are only available to a 'narrow segment' of its population, the inference that there is actual competition between imported and domestic distilled spirits at least in the segment of the market that the Philippines admitted has access to both imported and domestic distilled spirits".³²¹ In that same dispute, the Appellate Body found that Article III:2, second sentence, does not require that competition be assessed in relation to the market segment that is most representative of the "market as a whole", and that Article III of the GATT 1994 "does not protect just *some* instances or *most* instances, but rather, it protects *all* instances of direct competition".³²²

143. Although the Appellate Body's finding in *Philippines – Distilled Spirits* concerned the second sentence of Article III:2 of the GATT 1994, we consider this interpretation of "directly competitive or substitutable products" to be relevant to the concept of "likeness" in Article III:4 of the GATT 1994 and 2.1 of the *TBT Agreement*, since likeness under these provisions is determined on the basis of the competitive relationship between and among the products.³²³ In our view, the notion that actual competition does not need to take place in the whole market, but may be limited to a segment of the market, is separate from the question of the degree of competition that is required to satisfy the standards of "directly competitive or substitutable products" and "like products".

144. The Panel's consideration of consumer tastes and habits was too limited. At the same time, the mere fact that clove cigarettes are smoked disproportionately by youth, while menthol cigarettes are smoked more evenly by young and adult smokers does not necessarily affect the degree of substitutability between clove and menthol cigarettes. The Panel found that, from the perspective of young and potential young smokers, clove-flavoured cigarettes and menthol-flavoured cigarettes are similar for purposes of starting to smoke.³²⁴ We understand this as a finding that young and potential young smokers perceive clove and menthol cigarettes as sufficiently substitutable. This, in turn, is sufficient to support the Panel's finding that those products are like within the meaning of Article 2.1 of the *TBT Agreement*, even if the degree of substitutability is not the same for all adult smokers.

³²¹ Appellate Body Reports, *Philippines – Distilled Spirits*, para. 220.

³²² Appellate Body Reports, *Philippines – Distilled Spirits*, para. 221 (referring to Panel Report, *Chile – Alcoholic Beverages*, para. 7.43). (original emphasis)

³²³ In *EC – Asbestos*, the Appellate Body, while not defining the precise scope of the concept of "like products" in Article III:4, found that Article III:4 applies to products that are in a competitive relationship and that "the scope of 'like' in Article III:4 is broader than the scope of 'like' in Article III:2, first sentence". (Appellate Body Report, *EC – Asbestos*, para. 99)

³²⁴ Panel Report, para. 7.232.

145. In the light of the above, we are of the view that, while the Panel should not have limited its analysis of consumer tastes and habits to young and potential young smokers to the exclusion of current adult smokers, this does not undermine the Panel's finding regarding consumer tastes and habits and its ultimate finding of likeness. This is so because the degree of competition and substitutability that the Panel found for young and potential young smokers is sufficiently high to support a finding of likeness under Article 2.1 of the *TBT Agreement*.

146. Finally, we turn to the claim by the United States that the Panel acted inconsistently with Article 11 of the DSU when it reached the conclusion that clove cigarettes and menthol cigarettes are perceived similarly by the consumers at issue in this case, and that it disregarded critical evidence on how consumers actually use and perceive the products at issue in the relevant market.³²⁵

147. The United States emphasizes that clove cigarettes are smoked disproportionately by young, novice smokers while menthol cigarettes are smoked more evenly by young people and adults. It recalls that both parties presented evidence—in particular a set of surveys—aimed at shedding light on the tastes and habits of consumers in the United States in respect of clove and menthol cigarettes. However, the United States argues, the Panel disregarded this evidence after having erroneously concluded that it could not "rely on the information provide[d]" in the surveys on the basis that this information was "not directly comparable".³²⁶ The United States submits that the survey data before the Panel were "directly relevant to the question" before it because the data provided evidence on how consumers and potential consumers "used and perceived different cigarettes in the United States"³²⁷, that is, the relevant market. The United States further argues that, after disregarding this evidence, the Panel proceeded to base its conclusions "entirely on speculation and conjecture", without any evidentiary support as to how consumers in the relevant market actually use the cigarettes at issue.³²⁸

148. Indonesia responds that, given that the research parameters varied from survey to survey, the Panel properly concluded that the survey data did not provide clear guidance on "consumer tastes and habits". In its view, the Panel's approach to that evidence "hardly amounts to excluding it *a priori*".³²⁹ Instead, the Panel "clearly articulated the difficulties it encountered in comparing the survey data"³³⁰ and simply did not place the same weight on the evidence as did the United States. Indonesia further argues that the Panel identified and relied on evidence showing that both clove and menthol cigarettes

³²⁵ United States' appellant's submission, para. 64.

³²⁶ United States' appellant's submission, para. 66 (quoting Panel Report, para. 7.210).

³²⁷ United States' appellant's submission, para. 67. (original emphasis)

³²⁸ United States' appellant's submission, para. 68.

³²⁹ Indonesia's appellee's submission, para. 106.

³³⁰ Indonesia's appellee's submission, para. 115.

are "trainer" or "starter" cigarettes that appeal to youth.³³¹ Based on this evidence on record, the Panel properly found that "all these flavoured cigarettes are perceived as vehicles to start smoking."³³²

149. We observe that Article 11 of the DSU requires a panel to make an objective assessment of the matter before it, including an objective assessment of the facts of the case. Thus, Article 11 requires a panel to "consider all the evidence presented to it, assess its credibility, determine its weight, and ensure that its factual findings have a proper basis in that evidence."³³³ In addition, panels "are not required to accord to factual evidence of the parties the same meaning and weight as do the parties."³³⁴ In this respect, the Appellate Body will not "interfere lightly" with a panel's fact-finding authority, and will not "base a finding of inconsistency under Article 11 simply on the conclusion that [it] might have reached a different factual finding."³³⁵ Instead, for a claim under Article 11 to succeed, the Appellate Body must be satisfied that the panel has exceeded its authority as the initial trier of facts. As the initial trier of facts, a panel must provide "reasoned and adequate explanations and coherent reasoning"³³⁶, must base its finding on a sufficient evidentiary basis³³⁷, and must treat evidence with "even-handedness."³³⁸ Moreover, a participant claiming that a panel disregarded certain evidence must explain why the evidence is so material to its case that the panel's failure to address such evidence has a bearing on the objectivity of the panel's factual assessment.³³⁹

150. Both the United States and Indonesia relied on a series of surveys addressing smoking patterns in the United States in order to support their respective arguments.³⁴⁰ The Panel observed,

³³¹Indonesia's appellee's submission, para. 111.

³³²Indonesia's appellee's submission, para. 113 (quoting Panel Report, para. 7.231).

³³³Appellate Body Reports, *Philippines – Distilled Spirits*, para. 135 (quoting Appellate Body Report, *Brazil – Retreaded Tyres*, para. 185, in turn referring to Appellate Body Report, *EC – Hormones*, paras. 132 and 133).

³³⁴Appellate Body Report, *Australia – Salmon*, para. 267.

³³⁵Appellate Body Reports, *Philippines – Distilled Spirits*, para. 136 (quoting Appellate Body Report, *US – Wheat Gluten*, para. 151).

³³⁶Appellate Body Report, *US – Upland Cotton (Article 21.5 – Brazil)*, footnote 618 to para. 293.

³³⁷See Appellate Body Report, *US – Carbon Steel*, para. 148.

³³⁸Appellate Body Report, *US – Upland Cotton (Article 21.5 – Brazil)*, para. 292.

³³⁹See Appellate Body Report, *EC – Fasteners (China)*, para. 442.

³⁴⁰Indonesia relied on the following four surveys: (i) the 2006-2008 National Survey on Drug Use and Health; (ii) the 2009 Western Watts Survey; (iii) the 2009 Monitoring the Future Survey; and (iv) a 2010 telephone survey conducted by Opinion Research Corporation. (Panel Report, footnote 426 to para. 7.210) (referring to National Survey on Drug Use and Health 2006-2008, "Essential Facts About Clove Cigarettes" (Panel Exhibit IND-3); Western Watts Data Collection, "Clove Cigarettes Attitude, Awareness and Usage Survey", 16-19 February 2009 (Panel Exhibit IND-26); L.D. Johnston et al., "Smoking continues gradual decline among U.S. teens, smokeless tobacco threatens a comeback," *University of Michigan News Service*, 14 December 2009 (Panel Exhibit IND-33); and Opinion Research Corporation, Teen CARAVAN Study No. 719381, 23-26 September 2010 (Panel Exhibit IND-34)) The United States based its arguments on two surveys: (i) the 2002-2003 National Survey on Drug Use and Health; and (ii) the National Youth Tobacco Survey. (Panel Report, footnote 426 to para. 7.210 (referring to FDA Survey Assessment, "Patterns of Use Among Menthol, Clove, and Other Flavored Cigarettes (Panel Exhibit US-53)))

however, that these surveys "do not share the same research parameters"³⁴¹; instead, they "examine[d] different age groups", "pose[d] different questions", and were "based on different methodological approaches".³⁴² Consequently, in the Panel's view, the information contained in the different surveys was "not directly comparable". On this basis, the Panel reached the conclusion that it could not "rely on the information [that the surveys] provide on market shares for the purposes of analyzing the consumers' tastes and habits criterion"³⁴³, and that "the evidence on consumer preferences submitted by the parties may not provide clear guidance" as to whether clove and menthol cigarettes are substitutable from the perspective of young smokers and potential young smokers.³⁴⁴

151. We acknowledge that extracting meaningful information from surveys that differ considerably in terms of research parameters might not be an easy task. Likewise, we do not suggest that panels must always be capable of engaging in sophisticated statistical exercises to solve data discrepancies that ultimately cannot be resolved. However, the fact that evidence relied on by the parties may be difficult to compare cannot excuse the panel from examining it. A panel has the obligation to "consider *all* the evidence presented to it"³⁴⁵, and it should at least attempt to extract potentially relevant information contained therein. It is only after such an examination that a panel might be able to provide "reasoned and adequate explanations"³⁴⁶ as to why it cannot or chooses not to rely on specific evidence submitted by the parties. In our view, a panel cannot determine *a priori* that some pieces of evidence are not reliable for the purposes of its analysis solely on the basis of a difference in the parameters and methodology used.

152. We recall, however, that not every error allegedly committed by a panel amounts to a violation of Article 11 of the DSU. A participant claiming that a panel ignored certain evidence must explain why that evidence is so material to its case that the panel's failure to address such evidence has a bearing on the objectivity of the panel's factual assessment.³⁴⁷ In that respect, the United States submits that, because the Panel did not examine the evidence related to consumers' tastes and habits, the Panel's finding with respect to this criterion "was fatally flawed"³⁴⁸. In the United States' view, the survey data presented by the parties "show that consumers and potential consumers use and

³⁴¹Panel Report, para. 7.210.

³⁴²Panel Report, para. 7.210.

³⁴³Panel Report, para. 7.210.

³⁴⁴Panel Report, para. 7.209.

³⁴⁵Appellate Body Reports, *Philippines – Distilled Spirits*, para. 135 (quoting Appellate Body Report, *Brazil – Retreaded Tyres*, para. 185, in turn referring to Appellate Body Report, *EC – Hormones*, paras. 132 and 133).

³⁴⁶Appellate Body Report, *US – Upland Cotton (Article 21.5 – Brazil)*, footnote 618 to para. 293.

³⁴⁷Appellate Body Report, *EC – Fasteners (China)*, para. 442.

³⁴⁸United States' appellant's submission, para. 68.

perceive clove and menthol cigarettes differently—even though they are both cigarettes with characterizing flavors that appeal to youth".³⁴⁹

153. We have considered above, in respect of the claim by the United States that the Panel erred in the application of the consumer tastes and habits criterion, that, although the Panel should not have limited its analysis to young and potential young consumers, to the exclusion of current adult consumers, this did not affect its finding that there is sufficient substitutability between clove and menthol cigarettes to support its overall finding that the products are like. The Panel's findings show that, while clove and menthol cigarettes do not compete in the whole market, these products are substitutable for young and potential young consumers.

154. Therefore, in our view, the fact that the Panel did not rely on evidence demonstrating that clove cigarettes are disproportionately smoked by youth while menthol cigarettes are smoked by both youth and adults, does not have material consequences for the Panel's finding on consumer tastes and habits. This is so because the Panel found that there is a sufficient degree of substitutability, at least in some segments of the market, between clove and menthol cigarettes, to support a finding of likeness under Article 2.1 of the *TBT Agreement*.

155. In sum, we are not persuaded that the reasons advanced by the Panel for not relying on the surveys submitted by the parties justify the cursory treatment given by the Panel to these surveys. Even if this evidence was not directly comparable or based on different methodological approaches, the Panel was required to consider this evidence and extract relevant information that it contained. The Panel did not provide an adequate explanation as to why this was not possible. Nevertheless, in our view, the Panel's error does not amount to a violation of Article 11 of the DSU, considering that the evidence that the Panel did not engage with does not have material consequences for the Panel's finding that consumer tastes and habits indicate that clove and menthol cigarettes are sufficiently substitutable in certain segments of the market, and does not, therefore, undermine the Panel's finding that clove and menthol cigarettes are like products under Article 2.1 of the *TBT Agreement*.

4. Conclusion on "Like Products"

156. We have disagreed with the Panel's interpretation of the concept of "like products" in Article 2.1 of the *TBT Agreement*, which focuses on the purposes of the technical regulation at issue, as separate from the competitive relationship between and among the products. In contrast, we have concluded that the context provided by Article 2.1 itself, by other provisions of the *TBT Agreement*, by the *TBT Agreement* as a whole, and by Article III:4 of the GATT 1994, as well as the object and

purpose of the *TBT Agreement*, support an interpretation of the concept of "likeness" in Article 2.1 that is based on the competitive relationship between and among the products and that takes into account the regulatory concerns underlying a technical regulation, to the extent that they are relevant to the examination of certain likeness criteria and are reflected in the products' competitive relationship.

157. As a consequence of our interpretative approach to the concept of "like products" in Article 2.1 of the *TBT Agreement*, we have also disagreed with the Panel's decision to examine the extent of substitutability of clove and menthol cigarettes from the perspective of a limited group of consumers, that is, young smokers and potential young smokers. We have, nevertheless, considered that the Panel's error does not vitiate the conclusion that there is a sufficient degree of substitutability between clove and menthol cigarettes to support an overall finding of likeness under Article 2.1 of the *TBT Agreement*. We have also determined that the Panel's decision that it could not rely on certain evidence submitted by the parties did not amount to an error under Article 11 of the DSU.

158. In respect of end-use, we have disagreed with the Panel's conclusion that the end-use of clove and menthol cigarettes is simply "to be smoked". Nevertheless, we have considered, based on the Panel's findings, that both clove and menthol cigarettes are *capable* of performing the more specific end-uses put forward by the United States, that is, "satisfying an addiction to nicotine" and "creating a pleasurable experience associated with the taste of the cigarette and the aroma of the smoke".³⁵⁰ We have thus concluded that the different end-uses of clove and menthol cigarettes support the Panel's overall finding of likeness.

159. Finally, we observe that the United States has not appealed the Panel's findings regarding the physical characteristics and the tariff classification of clove and menthol cigarettes. The Panel found that clove and menthol cigarettes are physically similar as "they share their main traits as cigarettes, that is, having tobacco as a main ingredient, and an additive which imparts a characterizing flavour, taste and aroma, and reduces the harshness of tobacco"³⁵¹; and that they are both classified under subheading 2402.20 of the Harmonized Commodity Description and Coding System.³⁵²

160. In the light of all of the above, while we disagree with certain aspects of the Panel's analysis, we agree with the Panel that the "likeness" criteria it examined support its overall conclusion that clove and menthol cigarettes are like products within the meaning of Article 2.1 of the *TBT Agreement*. Therefore, we *uphold*, albeit for different reasons, the Panel's finding, in

³⁵⁰Panel Report, para. 7.231; United States' response to Panel Question 37, para. 85.

³⁵¹Panel Report, para. 7.187.

³⁵²Panel Report, para. 7.239.

paragraph 7.248 of the Panel Report, that clove cigarettes and menthol cigarettes are like products within the meaning of Article 2.1 of the *TBT Agreement*.

C. *The Panel's Finding that Section 907(a)(1)(A) of the FFDCCA Accords Imported Clove Cigarettes Less Favourable Treatment than That Accorded to Domestic Menthol Cigarettes, within the Meaning of Article 2.1 of the TBT Agreement*

1. Introduction

161. In this section, we address the United States' appeal of the Panel's finding that the United States acted inconsistently with Article 2.1 of the *TBT Agreement* by according to clove cigarettes imported from Indonesia less favourable treatment than that accorded to domestic like products.

162. Having concluded that clove and menthol cigarettes are like products within the meaning of Article 2.1 of the *TBT Agreement*, the Panel undertook a four-step analysis to determine whether Section 907(a)(1)(A) of the FFDCCA accords to clove cigarettes imported from Indonesia less favourable treatment than that accorded to like domestic products. First, the Panel sought to determine the products to be compared in its analysis.³⁵³ The Panel found that Article 2.1 called for a comparison between treatment accorded to, on the one hand, clove cigarettes imported from Indonesia, and, on the other hand, domestic menthol cigarettes.³⁵⁴ Second, the Panel determined that under Section 907(a)(1)(A) clove and menthol cigarettes are treated differently, in that clove cigarettes are banned while menthol cigarettes are excluded from the ban.³⁵⁵ Third, the Panel found that such difference in treatment modifies the conditions of competition to the detriment of the imported products, insofar as imported clove cigarettes are banned while domestic menthol cigarettes are allowed to remain in the market.³⁵⁶ Fourth and finally, the Panel rejected the United States' argument that such detrimental impact could be "explained by factors or circumstances unrelated to the foreign origin of the products"³⁵⁷, because Section 907(a)(1)(A) imposes costs on foreign producers, notably producers in Indonesia, while at the same time imposing no costs on any US entity.³⁵⁸

163. On appeal, the United States claims that the Panel improperly narrowed the *product scope* of its analysis by focusing exclusively on treatment accorded to imported clove cigarettes and to

³⁵³Panel Report, para. 7.270.

³⁵⁴Panel Report, paras. 7.275-7.277.

³⁵⁵Panel Report, paras. 7.279 and 7.280.

³⁵⁶Panel Report, para. 7.281.

³⁵⁷Panel Report, para. 7.283 (referring to United States' second written submission to the Panel, para. 127, in turn referring to Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 96).

³⁵⁸Panel Report, para. 7.289.

domestic menthol cigarettes. The United States posits that the Panel should have compared the treatment accorded to the group of imported and to the group of domestic like products. The United States also claims that the Panel improperly narrowed the *temporal scope* of its analysis by focusing exclusively on the effects of Section 907(a)(1)(A) on domestic like products at the time the ban on flavoured cigarettes came into effect. The United States claims further that the Panel erred in finding that the less favourable treatment accorded to imported clove cigarettes was related to the origin of the products, because Section 907(a)(1)(A) imposes costs on foreign producers while at the same time imposing no costs on any US entity. Finally, the United States claims that the Panel acted inconsistently with Article 11 of the DSU in reaching these findings.

164. Indonesia responds that the Panel properly identified the products to be compared in its less favourable treatment analysis, and did not err in establishing the appropriate timeframe for its comparison. Indonesia also asserts that the Panel correctly found that the less favourable treatment accorded to clove cigarettes could not be explained by factors unrelated to the foreign origin of the imported products. Finally, Indonesia claims that the Panel acted in accordance with Article 11 of the DSU in performing its analysis.

165. Before turning to the specific issues raised by the United States on appeal, we find it useful to interpret the "treatment no less favourable" requirement of Article 2.1 of the *TBT Agreement* in the light of the conflicting interpretations of this phrase offered by the participants on appeal.

2. "Treatment No Less Favourable" under Article 2.1 of the TBT Agreement

166. Referring to the Appellate Body's interpretation of Article III:4 of the GATT 1994³⁵⁹, the United States and Indonesia agree that the "treatment no less favourable" standard of Article 2.1 of the *TBT Agreement* requires a panel to determine whether the technical regulation at issue modifies the conditions of competition in the relevant market to the detriment of the imported products. However, Indonesia considers that the existence of any detrimental effect on competitive opportunities for imported products is sufficient to establish less favourable treatment under Article 2.1.³⁶⁰ In contrast, the United States argues that the existence of a detrimental effect on competitive opportunities for imports is necessary, but not sufficient, to establish a violation of Article 2.1. Referring to the Appellate Body report in *Dominican Republic – Import and Sale of Cigarettes*, the United States

³⁵⁹See Appellate Body Report, *Korea – Various Measures on Beef*, para. 137.

³⁶⁰Indonesia's appellee's submission, para. 172.

argues that Article 2.1 requires further inquiry into whether "the detrimental effect is explained by factors or circumstances unrelated to the foreign origin of the product".³⁶¹

167. Article 2.1 of the *TBT Agreement* provides that, with respect to their central government bodies:

Members shall ensure that in respect of technical regulations, products imported from the territory of any Member shall be accorded treatment no less favourable than that accorded to like products of national origin and to like products originating in any other country.

168. As already set out above, for a violation of the national treatment obligation in Article 2.1 to be established, three elements must be satisfied: (i) the measure at issue must be a "technical regulation"; (ii) the imported and domestic products at issue must be like products; and (iii) the treatment accorded to imported products must be less favourable than that accorded to like domestic products. In this part of its appeal, the United States challenges only the Panel's finding that Section 907(a)(1)(A) of the FFDCA violates the national treatment obligation provided in Article 2.1 of the *TBT Agreement*, insofar as it accords to imported clove cigarettes less favourable treatment than that accorded to like domestic products.

169. The "treatment no less favourable" requirement of Article 2.1 of the *TBT Agreement* applies "in respect of technical regulations". A technical regulation is defined in Annex 1.1 thereto as a "[d]ocument which lays down product characteristics or their related processes and production methods ... with which compliance is mandatory". As such, technical regulations are measures that, by their very nature, establish distinctions between products according to their characteristics or their related processes and production methods. This suggests, in our view, that Article 2.1 should not be read to mean that *any* distinction, in particular those that are based *exclusively* on particular product characteristics or their related processes and production methods, would *per se* accord less favourable treatment within the meaning of Article 2.1.

170. We next observe that Article 2.2 of the *TBT Agreement* provides, in relevant part, that:

Members shall ensure that technical regulations are not prepared, adopted or applied with a view to or with the effect of creating unnecessary obstacles to international trade. For this purpose, technical regulations shall not be more trade-restrictive than necessary to fulfil a legitimate objective, taking account of the risks non-fulfilment would create.

³⁶¹United States' appellant's submission, para. 101 (referring to Panel Report, para. 7.269; and Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 96).

171. The context provided by Article 2.2 suggests that "obstacles to international trade" may be permitted insofar as they are not found to be "unnecessary", that is, "more trade-restrictive than necessary to fulfil a legitimate objective". To us, this supports a reading that Article 2.1 does not operate to prohibit *a priori* any obstacle to international trade. Indeed, if *any* obstacle to international trade would be sufficient to establish a violation of Article 2.1, Article 2.2 would be deprived of its *effet utile*.

172. This interpretation of Article 2.1 is buttressed by the sixth recital of the preamble of the *TBT Agreement*, in which WTO Members recognize that:

... no country should be prevented from taking measures necessary to ensure the quality of its exports, or for the protection of human, animal, or plant life or health, of the environment, or for the prevention of deceptive practices, at the levels it considers appropriate, subject to the requirement that they are not applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail or a disguised restriction on international trade, and are otherwise in accordance with the provisions of this Agreement.

173. The language of the sixth recital expressly acknowledges that Members may take measures necessary for, *inter alia*, the protection of human life or health, provided that such measures "are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination" or a "disguised restriction on international trade" and are "otherwise in accordance with the provisions of this Agreement". We consider that the sixth recital of the preamble of the *TBT Agreement* provides relevant context regarding the ambit of the "treatment no less favourable" requirement in Article 2.1, by making clear that technical regulations may pursue the objectives listed therein, provided that they are not applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, and are otherwise in accordance with the provisions of the *TBT Agreement*.

174. Finally, as noted earlier³⁶², the object and purpose of the *TBT Agreement* is to strike a balance between, on the one hand, the objective of trade liberalization and, on the other hand, Members' right to regulate. This object and purpose therefore suggests that Article 2.1 should not be interpreted as prohibiting any detrimental impact on competitive opportunities for imports in cases where such detrimental impact on imports stems exclusively from legitimate regulatory distinctions.

175. Accordingly, the context and object and purpose of the *TBT Agreement* weigh in favour of reading the "treatment no less favourable" requirement of Article 2.1 as prohibiting both *de jure* and

³⁶²*Supra*, paras. 94 and 95.

de facto discrimination against imported products, while at the same time permitting detrimental impact on competitive opportunities for imports that stems exclusively from legitimate regulatory distinctions.

176. Like the participants, we also find it useful to consider the context provided by the other covered agreements. In particular, we note that the non-discrimination obligation of Article 2.1 of the *TBT Agreement* is expressed in the same terms as that of Article III:4 of the GATT 1994.³⁶³ In the context of Article III:4, the "treatment no less favourable" requirement has been widely interpreted by previous GATT and WTO panels and by the Appellate Body. Beginning with the GATT panel in *US – Section 337 Tariff Act*, the term "treatment no less favourable" in Article III:4 was interpreted as requiring "effective equality of opportunities for imported products".³⁶⁴ Subsequent GATT and WTO panels followed a similar approach, and found violations of Article III:4 in cases where regulatory distinctions in enforcement procedures³⁶⁵, distribution channels³⁶⁶, statutory content requirements³⁶⁷, and allocation of import licenses³⁶⁸ resulted in alteration of the competitive opportunities in the market of the regulating Member to the detriment of imported products vis-à-vis domestic like products.

177. In *Korea – Various Measures on Beef*, the Appellate Body agreed that the analysis of less favourable treatment under Article III:4 focuses on the "conditions of competition" between imported and domestic like products.³⁶⁹ The Appellate Body further clarified that a formal difference in treatment between imported and like domestic products is:

... neither necessary, nor sufficient, to show a violation of Article III:4. Whether or not imported products are treated "less favourably" than like domestic products should be assessed instead by examining whether a measure modifies the *conditions of competition* in the relevant market to the detriment of imported products.³⁷⁰ (original emphasis)

178. Subsequently, in *EC – Asbestos*, the Appellate Body explained that imports will be treated less favourably than domestic like products when regulatory distinctions disadvantage the group of

³⁶³ Article III:4 of the GATT 1994 reads:

The products of the territory of any Member imported into the territory of any other Member shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use.

³⁶⁴ GATT Panel Report, *US – Section 337 Tariff Act*, para. 5.10.

³⁶⁵ GATT Panel Report, *US – Section 337 Tariff Act*, para. 5.20.

³⁶⁶ GATT Panel Report, *Canada – Provincial Liquor Boards (US)*, paras. 5.12-5.16.

³⁶⁷ Panel Report, *US – Gasoline*, para. 6.10.

³⁶⁸ Panel Reports, *EC – Bananas III*, paras. 7.179-7.180.

³⁶⁹ Appellate Body Report, *Korea – Various Measures on Beef*, para. 136.

³⁷⁰ Appellate Body Report, *Korea – Various Measures on Beef*, para. 137.

imported products vis-à-vis the group of domestic like products. The Appellate Body reasoned that the "treatment no less favourable" clause of Article III:4:

... expresses the general principle, in Article III:1, that internal regulations "should not be applied ... so as to afford protection to domestic production." If there is "less favourable treatment" of the group of "like" imported products, there is, conversely, "protection" of the group of "like" domestic products. However, a Member may draw distinctions between products which have been found to be "like", without, for this reason alone, according to the group of "like" imported products "less favourable treatment" than that accorded to the group of "like" domestic products.³⁷¹ (original emphasis)

179. Thus, the "treatment no less favourable" standard of Article III:4 of the GATT 1994 prohibits WTO Members from modifying the conditions of competition in the marketplace to the detriment of the group of imported products vis-à-vis the group of domestic like products.³⁷²

180. Although we are mindful that the meaning of the term "treatment no less favourable" in Article 2.1 of the *TBT Agreement* is to be interpreted in the light of the specific context provided by the *TBT Agreement*, we nonetheless consider these previous findings by the Appellate Body in the context of Article III:4 of the GATT 1994 to be instructive in assessing the meaning of "treatment no less favourable", provided that the specific context in which the term appears in Article 2.1 of the *TBT Agreement* is taken into account. Similarly to Article III:4 of the GATT 1994, Article 2.1 of the *TBT Agreement* requires WTO Members to accord to the group of imported products treatment no less favourable than that accorded to the group of like domestic products. Article 2.1 prescribes such

³⁷¹ Appellate Body Report, *EC – Asbestos*, para. 100.

³⁷² We disagree with the United States to the extent that it suggests that *Dominican Republic – Import and Sale of Cigarettes* stands for the proposition that, under Article III:4, panels should inquire further whether "the detrimental effect is unrelated to the foreign origin of the product". (United States' appellant's submission, para. 101 (referring to Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 96)) Although the statement referred to by the United States, when read in isolation, could be viewed as suggesting that further inquiry into the rationale for the detrimental impact is necessary, in that dispute the Appellate Body rejected Honduras' claim under Article III:4 because:

... the difference between the per-unit costs of the bond requirement alleged by Honduras is explained by the fact that the importer of Honduran cigarettes has a smaller market share than two domestic producers (the per-unit cost of the bond requirement being the result of dividing the cost of the bond by the number of cigarettes sold on the Dominican Republic market).

(Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 96)

Thus, in that dispute, the Appellate Body merely held that the higher *per unit* costs of the bond requirement for imported cigarettes did not conclusively demonstrate less favourable treatment, because it was not attributable to the specific measure at issue but, rather, was a function of sales volumes. In *Thailand – Cigarettes (Philippines)*, the Appellate Body further clarified that for a finding of less favourable treatment under Article III:4 "there must be in every case a genuine relationship between the measure at issue and its adverse impact on competitive opportunities for imported versus like domestic products to support a finding that imported products are treated less favourably". (Appellate Body Report, *Thailand – Cigarettes (Philippines)*, para. 134) The Appellate Body eschewed an additional inquiry as to whether such detrimental impact was related to the foreign origin of the products or explained by other factors or circumstances.

treatment specifically in respect of technical regulations. For this reason, a panel examining a claim of violation under Article 2.1 should seek to ascertain whether the technical regulation at issue modifies the conditions of competition in the market of the regulating Member to the detriment of the group of imported products vis-à-vis the group of like domestic products.

181. However, as noted earlier, the context and object and purpose of the *TBT Agreement* weigh in favour of interpreting the "treatment no less favourable" requirement of Article 2.1 as not prohibiting detrimental impact on imports that stems exclusively from a legitimate regulatory distinction. Rather, for the aforementioned reasons³⁷³, the "treatment no less favourable" requirement of Article 2.1 only prohibits *de jure* and *de facto* discrimination against the group of imported products.

182. Accordingly, where the technical regulation at issue does not *de jure* discriminate against imports, the existence of a detrimental impact on competitive opportunities for the group of imported vis-à-vis the group of domestic like products is not dispositive of less favourable treatment under Article 2.1. Instead, a panel must further analyze whether the detrimental impact on imports stems exclusively from a legitimate regulatory distinction rather than reflecting discrimination against the group of imported products. In making this determination, a panel must carefully scrutinize the particular circumstances of the case, that is, the design, architecture, revealing structure, operation, and application of the technical regulation at issue, and, in particular, whether that technical regulation is even-handed, in order to determine whether it discriminates against the group of imported products.

3. Product Scope of the "Treatment No Less Favourable" Comparison

183. We now turn to the specific issues raised by the United States on appeal. We begin with the United States' appeal of the scope of products considered by the Panel to determine whether imported clove cigarettes are treated less favourably than US domestic like products within the meaning of Article 2.1 of the *TBT Agreement*.

184. Before the Panel, Indonesia argued that the "treatment no less favourable" requirement of Article 2.1 calls for a comparison between, on the one hand, treatment accorded to imported clove cigarettes and, on the other hand, treatment accorded to any like domestic cigarettes that are not banned by Section 907(a)(1)(A) of the FFDCA (that is, menthol or regular cigarettes, but not other flavoured cigarettes, which are prohibited under Section 907(a)(1)(A)).³⁷⁴ The United States responded that the Panel should compare treatment accorded under Section 907(a)(1)(A) to all

imported cigarettes (to the extent they are like) and not just clove cigarettes, with the treatment accorded to all domestically produced like cigarettes.³⁷⁵

185. The Panel determined that the comparison should be between the treatment accorded to imported clove cigarettes and that accorded to the domestically produced cigarettes that it had earlier found to be like products, that is, menthol cigarettes. It reasoned that:

Article 2.1 of the *TBT Agreement* calls for a comparison of "products imported from the territory of any Member" with "like products of national origin". These provisions refer to the products imported from the territory of "any other Member", and not "Members" or "other Members" more generally. The imported products in this case are the products imported from the territory of *Indonesia*. And it appears to be common ground between the parties that the vast majority of cigarettes that were imported from Indonesia into the United States were *clove* cigarettes.³⁷⁶ (original emphasis; footnote omitted)

On the domestic side, we recall that we have found that menthol cigarettes are "like" clove cigarettes for the purpose of Article 2.1 of the *TBT Agreement* because, *inter alia*, they both contain an additive that provides them with a characterizing flavour which makes them appealing to youth. We have not entered into an analysis of whether domestic regular cigarettes are "like" imported clove cigarettes as we consider that we would be exceeding our terms of reference.³⁷⁷

186. On appeal, the United States claims that the Panel erred in *a priori* limiting its less favourable treatment comparison to one imported product (Indonesian clove cigarettes) and one domestic like product (menthol cigarettes). Referring to the Appellate Body report in *EC – Asbestos* and the panel report in *US – Tuna II (Mexico)*, the United States argues that Article 2.1 required the Panel to compare the treatment accorded to all imported and domestic like products as a group.³⁷⁸ For the United States, a proper comparison would have demonstrated that Section 907(a)(1)(A) does not alter the conditions of competition between imported and domestic like products as a group.³⁷⁹

187. With respect to the imported products, the United States argues that the Panel erred in failing to consider the treatment accorded to menthol cigarettes imported from other countries.³⁸⁰ According to the United States, the reference to imported products of "any other Member" in Article 2.1 does not justify the Panel's focus on Indonesian clove cigarettes, because Article 2.1 aims at discerning

³⁷⁵Panel Report, para. 7.272.

³⁷⁶Panel Report, para. 7.275.

³⁷⁷Panel Report, para. 7.277.

³⁷⁸United States' appellant's submission, paras. 75-77 (referring to Appellate Body Report, *EC – Asbestos*, para. 100; and quoting Panel Report, *US – Tuna II (Mexico)*, para. 7.295).

³⁷⁹United States' appellant's submission, para. 81.

³⁸⁰United States' appellant's submission, para. 79.

legitimate regulatory distinctions from those that serve as a proxy for singling out the like products of the complaining Member³⁸¹ for less favourable treatment.

188. With respect to like domestic products, the United States argues that the Panel erred in failing to consider the treatment accorded to domestic flavoured cigarettes.³⁸² To the extent that the Panel limited its analysis to domestic menthol cigarettes by virtue of the product scope of Indonesia's panel request, the United States maintains that a panel's terms of reference do not limit the scope of the products to be considered in a discrimination claim.³⁸³

189. For its part, Indonesia responds that the Panel did not err in comparing the treatment accorded to imported clove cigarettes with the treatment accorded to domestic menthol cigarettes. Indonesia argues that the Panel correctly limited its less favourable treatment comparison to those imported and domestic products that it reviewed in its likeness analysis.³⁸⁴ Whereas the Appellate Body in *EC – Asbestos* and the panel in *US – Tuna II (Mexico)* engaged in a likeness analysis on the basis of groups of products, the Panel in this case correctly limited its analysis to the specific products at issue, namely, imported clove cigarettes and domestic menthol cigarettes.³⁸⁵ Indonesia further maintains that the Panel did not rely on its terms of reference to limit the product scope of its less favourable treatment comparison, but rather on its determination of the scope of its likeness analysis.³⁸⁶

190. Article 2.1 provides that "products imported from the territory of any Member"³⁸⁷ shall be accorded treatment no less favourable than that accorded to "like products of national origin and like products originating in any other country". The text of Article 2.1 thus calls for a comparison of treatment accorded to, on the one hand, products imported from any Member alleging a violation of Article 2.1, and treatment accorded to, on the other hand, like products of domestic and any other origin. Therefore, for the purposes of the less favourable treatment analysis, treatment accorded to products imported from the complaining Member is to be compared with that accorded to like domestic products and like products of any other origin.

191. In determining what are the "like products of national origin and like products originating in any other country", a panel must seek to establish, based on the nature and extent of the competitive relationship between the products in the market of the regulating Member, the products of domestic (and other) origin(s) that are like the products imported from the complaining Member. In

³⁸¹United States' appellant's submission, para. 84.

³⁸²United States' appellant's submission, para. 79.

³⁸³United States' appellant's submission, para. 87.

³⁸⁴Indonesia's appellee's submission, paras. 138 and 139.

³⁸⁵Indonesia's appellee's submission, paras. 123-130.

³⁸⁶Indonesia's appellee's submission, paras. 147 and 148.

³⁸⁷Emphasis added.

determining what the like products at issue are, a panel is not bound by its terms of reference to limit its analysis to those products identified by the complaining Member in its panel request. Rather, Article 2.1 requires the panel to identify the domestic products that stand in a sufficiently close competitive relationship with the products imported from the complaining Member to be considered like products within the meaning of that provision.

192. To be clear, a panel's duty under Article 2.1 to identify the products of domestic and other origins that are like the products imported from the complaining Member does not absolve the complainant from making a *prima facie* case of violation of Article 2.1. Ordinarily, in discharging that burden, the complaining Member will identify the imported and domestic products that are allegedly like and whose treatment needs to be compared for purposes of establishing a violation of Article 2.1. The products identified by the complaining Member are the starting point in a panel's likeness analysis. However, Article 2.1 requires panels to assess objectively, on the basis of the nature and extent of the competitive relationship between the products in the market of the regulating Member, the universe of domestic products that are like the products imported from the complaining Member.³⁸⁸

193. Once the imported and domestic like products have been properly identified, Article 2.1 requires a panel dealing with a national treatment claim to compare, on the one hand, the treatment accorded under the technical regulation at issue to all like products imported from the complaining Member with, on the other hand, that accorded to all like domestic products. However, the national treatment obligation of Article 2.1 does not require Members to accord no less favourable treatment to each and every imported product as compared to each and every domestic like product. Article 2.1 does not preclude any regulatory distinctions between products that are found to be like, as long as treatment accorded to the *group* of imported products is no less favourable than that accorded to the *group* of like domestic products. As noted by the Appellate Body in the context of Article III:4 of the GATT 1994:

[A] Member may draw distinctions between products which have been found to be "like", without, for this reason alone, according to the group of "like" imported products "less favourable treatment" than that accorded to the group of "like" domestic products.³⁸⁹
(original emphasis)

194. In sum, the national treatment obligation of Article 2.1 calls for a comparison of treatment accorded to, on the one hand, the group of products imported from the complaining Member and, on the other hand, the treatment accorded to the group of like domestic products. In determining what

³⁸⁸See Appellate Body Report, *EC and certain member States – Large Civil Aircraft*, para. 1131.

³⁸⁹Appellate Body Report, *EC – Asbestos*, para. 100.

the scope of like imported and domestic products is, a panel is not limited to those products specifically identified by the complaining Member. Rather, a panel must objectively assess, based on the nature and extent of their competitive relationship, what are the domestic products that are like the products imported from the complaining Member. Once the universe of imported and domestic like products has been identified, the treatment accorded to all like products imported from the complaining Member must be compared to that accorded to all like domestic products. The "treatment no less favourable" standard of Article 2.1 does not prohibit regulatory distinctions between products found to be like, provided that the group of like products imported from the complaining Member is treated no less favourably than the group of domestic like products.

195. Against this analytical framework, we turn to the United States' specific allegations of error. The United States essentially claims that the Panel impermissibly narrowed the scope of products to be compared for the purpose of assessing Indonesia's claim that Section 907(a)(1)(A) violates the national treatment obligation of Article 2.1.

196. With respect to the group of imported products, the United States claims that the Panel erred in failing to include in its analysis treatment accorded to menthol cigarettes imported into the United States from all Members. We cannot agree. As noted earlier, the national treatment obligation of Article 2.1 calls for a comparison of treatment accorded to the group of like products imported from the Member alleging a violation of Article 2.1, and treatment accorded to the group of like domestic products. It follows that the Panel did not err in finding that a determination of Indonesia's claims under Article 2.1 required an examination of whether Section 907(a)(1)(A) accords to the group of products imported *from Indonesia* less favourable treatment than that accorded to the group of like products of US origin.³⁹⁰

197. In determining the group of products imported from Indonesia whose treatment needed to be compared with the treatment accorded to like domestic products, the Panel found that it was uncontested that the "vast majority" of cigarettes that were imported from Indonesia into the United States were clove cigarettes.³⁹¹ The Panel also observed that only "a small percentage of non-clove cigarettes" was imported from Indonesia into the United States.³⁹² Accordingly, the Panel did not err in finding that the group of products imported from Indonesia essentially consisted of clove cigarettes.

198. With respect to the group of like domestic products, the United States' challenge focuses on the Panel's exclusion of domestically produced flavoured cigarettes from its less favourable treatment

³⁹⁰Panel Report, paras. 7.275-7.276.

³⁹¹Panel Report, para. 7.275.

³⁹²Panel Report, footnote 503 to para. 7.275 (referring to United States' response to Panel Question 81, in turn referring to World Trade Atlas, Indonesia Cigarette Exports to the United States, 1998-2009 (Panel Exhibit US-134)).

analysis. The Panel felt bound by its terms of reference to limit its likeness analysis to two categories of products regulated under Section 907(a)(1)(A)—imported clove cigarettes and domestic menthol cigarettes³⁹³—and accordingly limited its less favourable treatment analysis to a comparison of the treatment accorded to those two product groups.³⁹⁴ The Panel did not address domestic flavoured cigarettes at either the likeness or the less favourable treatment stage of its analysis.

199. We note, however, that the United States does not challenge on appeal the Panel's exclusion of domestically produced flavoured cigarettes from the likeness stage of its analysis. Rather, the United States' challenge focuses exclusively on the Panel's exclusion of domestically produced flavoured cigarettes from the less favourable treatment stage of the Panel's analysis. Because Article 2.1 expressly limits the scope of the less favourable treatment comparison to imported and domestic like products, in the absence of specific findings by the Panel that domestically produced flavoured cigarettes other than menthol are like clove cigarettes, we cannot determine whether the Panel erred in failing to include domestically produced flavoured cigarettes in its less favourable treatment comparison.

200. Even assuming, for the sake of argument, that the Panel had found that domestic flavoured cigarettes are like clove cigarettes imported from Indonesia, we are not persuaded that this would have changed the Panel's ultimate conclusion that Section 907(a)(1)(A) modifies the conditions of competition to the detriment of the group of imported products *vis-à-vis* like domestic products. Aside from the Panel's finding that, "at the time of the ban, there were no domestic cigarettes with characterizing flavours other than menthol cigarettes"³⁹⁵ in the US market—which is challenged by the United States and addressed below—the Panel did not have evidence on the record that flavoured cigarettes other than menthol cigarettes had "any sizeable market share in the United States prior to the implementation of the ban in 2009".³⁹⁶ To the contrary, in response to a Panel question, the United States confirmed that the non-clove-flavoured cigarettes banned under Section 907(a)(1)(A) "were on the market for a relatively short period of time and represented a relatively small market share".³⁹⁷ Therefore, we consider it safe to assume that, given their relatively low share in the US market, the inclusion of domestically produced flavoured cigarettes in the comparison would not have altered the Panel's ultimate conclusion that the group of like domestic products essentially consisted of domestic menthol cigarettes.

³⁹³Panel Report, para. 7.147.

³⁹⁴Panel Report, para. 7.277.

³⁹⁵Panel Report, para. 7.289.

³⁹⁶Panel Report, para. 2.28.

³⁹⁷United States' response to Panel Question 17, para. 43.

4. Temporal Scope of the "Treatment No Less Favourable" Comparison

201. To the extent that the Panel's exclusion of domestic flavoured cigarettes other than menthol cigarettes from its analysis stemmed from its finding that those products were not on the market at the time when the ban came into effect, the United States submits that this constitutes legal error. In particular, the United States claims that the Panel erred in *a priori* excluding from its analysis evidence concerning the effects of Section 907(a)(1)(A) of the FFDCA on domestic like products prior to the entry into force of the ban on flavoured cigarettes. Moreover, the United States claims that the Panel acted inconsistently with Article 11 of the DSU in ignoring evidence demonstrating that there were domestic flavoured cigarettes other than menthol cigarettes on the US market at the time of the ban.³⁹⁸

(a) Application of Article 2.1 of the TBT Agreement

202. The United States argues that Article 2.1 of the *TBT Agreement* does not establish a rigid temporal limitation in relation to the evidence that a panel may consider in performing a less favourable treatment analysis. For this reason, the United States argues that the Panel should have taken into account evidence demonstrating that there were domestically produced flavoured cigarettes on the market "in the years closely preceding the effective date of the ban".³⁹⁹ Section 907(a)(1)(A) was enacted specifically to respond to an "emerging trend of products", and closed off a "potential market" that US producers were actively exploring as recently as 2008.⁴⁰⁰ Therefore, the fact that the ban on flavoured cigarettes went into effect before US producers were able to "saturate" the market with those products should not be construed as evidence that US producers were not affected by the ban.⁴⁰¹

203. Indonesia responds that the United States' appeal of the relevant timeframe for the Panel's analysis is irrelevant, because the Panel properly compared only the treatment accorded to the products found to be like in this dispute—imported clove and domestic menthol cigarettes—both of which were on the market before the ban went into effect.⁴⁰² Indonesia agrees with the United States that Article 2.1 establishes "no rigid temporal limitation" on the timeframe of the analysis, and affords panels discretion in selecting the appropriate period.⁴⁰³

³⁹⁸United States' appellant's submission, paras. 97 and 98.

³⁹⁹United States' appellant's submission, para. 92.

⁴⁰⁰United States' appellant's submission, para. 93.

⁴⁰¹United States' appellant's submission, para. 94.

⁴⁰²Indonesia's appellee's submission, para. 151.

⁴⁰³Indonesia's appellee's submission, para. 152 (quoting United States's appellant's submission, para. 92).

204. The United States' challenge is directed at the Panel's statement that:

... at the time of the ban, there were no domestic cigarettes with characterizing flavours other than menthol cigarettes which accounted for approximately 25 per cent of the market and for a very significant proportion of the cigarettes smoked by youth in the United States. (emphasis added; footnote omitted)

205. In the present dispute, the Panel's mandate was established by its terms of reference, as defined in Indonesia's panel request. These terms of reference required the Panel to determine whether Section 907(a)(1)(A) was consistent with various provisions of the *TBT Agreement* and of the GATT 1994 at the date of the Panel's establishment. Accordingly, the Panel was required to assess whether there existed a violation of those Agreements at that time and, if so, to make a recommendation that the United States bring its measure into compliance. It follows that, in relation to Indonesia's claim under Article 2.1 of the *TBT Agreement*, the Panel was required to assess, as of the date of its establishment, whether Section 907(a)(1)(A) is a technical regulation that accords to products imported from Indonesia less favourable treatment than that accorded to like domestic products.

206. We agree with the participants that Article 2.1 does not establish a rigid temporal limitation on the evidence that the Panel could review in assessing Indonesia's claim under Article 2.1. Nothing in Article 2.1 enjoins panels from taking into account evidence pre-dating the establishment of a panel to the extent that such evidence informs the panel's assessment of the consistency of the measure at that point in time. This is particularly so in the case of a *de facto* discrimination claim, where a panel must base its determination on the totality of facts and circumstances before it, including the design, architecture, revealing structure, operation, and application of the technical regulation at issue. Therefore, evidence that Section 907(a)(1)(A) had "chilling" regulatory effects on domestic producers of flavoured cigarettes prior to the entry into force of the ban on those cigarettes could be relevant in the Panel's assessment of Indonesia's claim under Article 2.1.

207. In the present dispute, it is not clear that the Panel considered Article 2.1 to prohibit review of evidence pre-dating the entry into force of Section 907(a)(1)(A). As noted earlier, the Panel did not explain why it did not include domestic flavoured cigarettes other than menthol cigarettes in the group of like domestic products. In any event, the Panel's statement that, "at the time of the ban, there were no domestic cigarettes with characterizing flavours other than menthol" on the US market, was not the basis for the Panel's exclusion of domestic flavoured cigarettes from the less favourable treatment analysis. Rather, it was the basis for its finding that Section 907(a)(1)(A) imposes "costs on producers in other Members, notably producers in Indonesia, while at the same time imposing no costs on any

US entity."⁴⁰⁴ This finding by the Panel is challenged by the United States on appeal, and addressed in subsection V.C.5 of this Report.

(b) Article 11 of the DSU

208. The United States claims that the Panel acted inconsistently with Article 11 of the DSU in disregarding evidence demonstrating that, *at the time of the ban*, domestic flavoured cigarettes other than menthol cigarettes were marketed in the United States.⁴⁰⁵

209. Indonesia responds that the Panel did consider the evidence submitted by the United States in this regard but was ultimately not persuaded by it.⁴⁰⁶ According to Indonesia, in weighing the evidence before it, the Panel did not act inconsistently with Article 11 of the DSU.

210. We recall that Article 11 of the DSU requires a panel to "consider all the evidence presented to it, assess its credibility, determine its weight, and ensure that its factual findings have a proper basis in that evidence".⁴⁰⁷ Within these parameters, "it is generally within the discretion of the [panel] to decide which evidence it chooses to utilize in making findings"⁴⁰⁸, and panels "are not required to accord to factual evidence of the parties the same meaning and weight as do the parties".⁴⁰⁹

211. We observe that, in finding that "at the time of the ban there were no domestic cigarettes with characterizing flavours other than menthol cigarettes which accounted for 25 per cent of the market"⁴¹⁰, the Panel noted:

The United States argues that there is evidence showing that U.S.-produced cigarettes with characterizing flavours were on the market in 2008 and 2009 (United States' second written submission, para. 132). In this regard, the United States points to exhibits US-52 and US-62. In our view, none of the exhibits submitted demonstrate that U.S.-produced flavour cigarettes were being sold on the market as of the entry into force of Section 907(a)(1)(A). Exhibit US-52 only contains the "known and possible 'flavored' cigarette brands sold in the United States" as of 2008. Thus, it does not shed light upon the brands of cigarettes present in the U.S. market at the time Section 907(a)(1)(A) entered into force. Exhibit US-62 lists the flavoured cigarette brands that were certified as "fire-safe" brands in the States of New York and Maine as of 2009. Although this exhibit

⁴⁰⁴Panel Report, para. 7.289.

⁴⁰⁵United States' appellant's submission, paras. 97 and 98.

⁴⁰⁶Indonesia's appellee's submission, paras. 158 and 162.

⁴⁰⁷Appellate Body Reports, *Philippines – Distilled Spirits*, para. 135 (quoting Appellate Body Report, *Brazil – Retreaded Tyres*, para. 185, in turn referring to Appellate Body Report, *EC – Hormones*, paras. 132 and 133).

⁴⁰⁸Appellate Body Report, *EC – Hormones*, para. 135.

⁴⁰⁹Appellate Body Report, *Australia – Salmon*, para. 267.

⁴¹⁰Panel Report, para. 7.289.

extends until the entry into force of Section 907(a)(1)(A), it does not demonstrate which brands and types of cigarettes were actually being sold on the U.S. market on that date. Rather, it merely lists the brands cigarettes certified as "fire-safe". We therefore stand by our conclusion.⁴¹¹

212. Thus, it appears that the Panel did not disregard the evidence that, according to the United States, demonstrated the presence of domestically produced flavoured cigarettes other than menthol cigarettes on the US market at the time of the ban. Rather, the Panel reviewed that evidence but was ultimately not persuaded by it. In determining the weight to be attributed to the evidence before it, the Panel did not act inconsistently with Article 11 of the DSU. In particular, the Panel did not exceed its authority under Article 11 of DSU merely by attributing to the evidence a weight and significance different from that attributed to it by the United States.

5. Detrimental Impact on Imported Products

213. Finally, the United States claims that, even if the Appellate Body were to agree with the comparison undertaken by the Panel in its less favourable treatment analysis, the Panel nonetheless erred in finding that the detrimental effect on competitive opportunities for imported clove cigarettes was not "explained by factors unrelated to the foreign origin of those products".⁴¹²

214. The United States does not challenge on appeal the Panel's findings that Section 907(a)(1)(A) of the FFDCA accords different treatment to imported clove cigarettes and to domestic menthol cigarettes, and that such differential treatment is to the detriment of the imported product, insofar as clove cigarettes are banned while menthol cigarettes are permitted.⁴¹³ Accordingly, the Panel's conclusion that Section 907(a)(1)(A) modifies the conditions of competition in the US market to the detriment of imported clove cigarettes stands.

215. However, as noted earlier⁴¹⁴, the existence of a detrimental impact on competitive opportunities in the relevant market for the group of imported products vis-à-vis the group of domestic like products is not sufficient to establish a violation of the national treatment obligation contained in Article 2.1 of the *TBT Agreement*. Where the technical regulation at issue does not *de jure* discriminate against imports, a panel must carefully scrutinize the particular circumstances of the case, that is, the design, architecture, revealing structure, operation, and application of the technical regulation at issue, and, in particular, whether that technical regulation is even-handed, in

⁴¹¹Panel Report, footnote 524 to para. 7.289.

⁴¹²United States' appellant's submission, para. 99 (referring to Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 96).

⁴¹³Panel Report, paras. 7.279-7.281.

⁴¹⁴See *supra*, paras. 174 and 175.

order to determine whether the detrimental impact on imports stems exclusively from a legitimate regulatory distinction rather than reflects discrimination against the group of imported products.

216. Before the Panel, the United States argued that the exemption of menthol cigarettes from the ban on flavoured cigarettes is unrelated to the origin of the products, because it addresses two distinct objectives: one relates to the potential impact on the US health care system associated with the need to treat "millions" of menthol cigarette addicts with withdrawal symptoms; and the other relates to the risk of development of a black market and smuggling to supply the needs of menthol cigarette smokers.⁴¹⁵

217. The Panel considered that "the potential impact on the health care system and the potential development of a black market and smuggling of menthol cigarettes"⁴¹⁶ did not constitute legitimate objectives, because:

These reasons which the United States has presented as constituting a legitimate objective by themselves, appear to us as relating in one way or another to the costs that might be incurred by the United States were it to ban menthol cigarettes. Indeed, the United States is not banning menthol cigarettes because it is not a type of cigarette with a characterizing flavour that appeals to youth, but rather because of the costs that might be incurred as a result of such a ban. We recall that at the time of the ban, there were no domestic cigarettes with characterizing flavours other than menthol cigarettes which accounted for approximately 25 per cent of the market and for a very significant proportion of the cigarettes smoked by youth in the United States. It seems to us that the effect of banning cigarettes with characterizing flavours other than menthol is to impose costs on producers in other Members, notably producers in Indonesia, while at the same time imposing no costs on any U.S. entity.⁴¹⁷ (footnotes omitted)

218. On appeal, the United States claims that the Panel erred in concluding that any detriment to the competitive opportunities for imported clove cigarettes could not be explained by factors unrelated to the foreign origin of the products.⁴¹⁸ In addition, the United States claims that the Panel failed to make an objective assessment of the matter under Article 11 of the DSU in finding that there were no costs imposed on any US entity.⁴¹⁹

⁴¹⁵Panel Report, para. 7.289 and footnote 522 thereto.

⁴¹⁶Panel Report, para. 7.289.

⁴¹⁷Panel Report, para. 7.289.

⁴¹⁸United States' appellant's submission, para. 99.

⁴¹⁹United States' appellant's submission, para. 109.

(a) Application of Article 2.1

219. We begin with the United States' claim that the Panel erred in concluding that any detriment to the competitive opportunities for imported clove cigarettes could not be explained by factors unrelated to the foreign origin of the products.⁴²⁰ The United States argues that, "even where a technical regulation adversely affects the competitive situation of imported products compared to like domestic products, this does not constitute less favourable treatment when the detrimental effect is unrelated to the foreign origin of the product."⁴²¹ According to the United States, many factors affect the costs associated with a technical regulation, such as transportation costs, production methods, the age of the producer's facility, size, efficiency, productivity, and marketing strategy. As a result, Article 2.1 does not prohibit the imposition of costs on imported products as compared to domestic products, where those costs are not related to the origin of the product.⁴²² The Panel did not examine the "architecture, structure and design" of Section 907(a)(1)(A), including the fact that it allows Indonesia to import and sell regular and menthol cigarettes in the United States.⁴²³ For the United States, reference to unspecified "costs" on foreign producers does not establish that the effects of Section 907(a)(1)(A) on competitive opportunities for imported products are related to their origin.⁴²⁴ The United States underscores that the costs that Section 907(a)(1)(A) allegedly avoids would be incurred by the US regulatory enforcement and health care systems (and not by domestic menthol cigarette producers), even if all menthol cigarettes were imported.⁴²⁵

220. For Indonesia, the Panel's finding that Section 907(a)(1)(A) modifies the conditions of competition in the United States to the detriment of imported clove cigarettes vis-à-vis domestic menthol cigarettes was sufficient to establish a violation of Article 2.1.⁴²⁶ Although Indonesia maintains that an additional "national origin" test was not required, Indonesia argues that, nevertheless, the Panel was correct in concluding that Section 907(a)(1)(A) had a "discriminatory intent", because menthol cigarettes accounted for 25 per cent of the market, and for a significant proportion of the cigarettes smoked by youth in the United States.⁴²⁷ The Panel correctly rejected the potential costs on the US health care and enforcement systems as "legitimate reasons" for exempting menthol cigarettes from the ban on flavoured cigarettes. The Panel also appropriately found that the

⁴²⁰United States' appellant's submission, para. 99.

⁴²¹United States' appellant's submission, para. 101.

⁴²²United States' appellant's submission, para. 101.

⁴²³United States' appellant's submission, para. 103.

⁴²⁴United States' appellant's submission, para. 106.

⁴²⁵United States' appellant's submission, para. 107.

⁴²⁶Indonesia's appellee's submission, para. 172.

⁴²⁷Indonesia's appellee's submission, para. 183.

disproportionate allocation of costs between Indonesian and US entities evidenced *de facto* discrimination against imports.⁴²⁸

221. At the outset, we agree with the United States that the Panel did not clearly articulate its reasons for concluding that "the effect of banning cigarettes with characterizing flavours other than menthol is to impose costs on producers in other Members, notably producers in Indonesia, while at the same time imposing no costs on any US entity."⁴²⁹ To the extent that actual or potential costs are relevant to the analysis of less favourable treatment under Article 2.1, the Panel did not elaborate on why, in its view, Section 907(a)(1)(A) does not impose costs "on any US entity" beyond observing that, "at the time of the ban, there were no domestic cigarettes with characterizing flavours other than menthol cigarettes"⁴³⁰ on the US market.⁴³¹

222. Nonetheless, we are not persuaded that the Panel erred in ultimately finding that Section 907(a)(1)(A) is inconsistent with Article 2.1. By design, Section 907(a)(1)(A) prohibits all cigarettes with characterizing flavours other than tobacco or menthol. In relation to the cigarettes that are banned under Section 907(a)(1)(A), the Panel made a factual finding that "virtually all clove cigarettes" that were imported into the United States in the three years prior to the ban came from Indonesia.⁴³² The Panel also noted that the "vast majority" of clove cigarettes consumed in the United States came from Indonesia.⁴³³ Although the United States stated that it was "unable to attain market share data for all non-clove products banned under Section 907(a)(1)(A)"⁴³⁴, the Panel did not find evidence that these products had "any sizeable market share in the United States prior to the implementation of the ban in 2009".⁴³⁵ In response to a Panel question, the United States confirmed that non-clove-flavoured cigarettes banned under Section 907(a)(1)(A) "were on the market for a relatively short period of time and represented a relatively small market share".⁴³⁶

⁴²⁸Indonesia's appellee's submission, paras. 184-185.

⁴²⁹Panel Report, para. 7.289.

⁴³⁰Panel Report, para. 7.289.

⁴³¹Moreover, to the extent that the Panel's finding could be read as suggesting that reducing potential costs of regulation *per se* constitutes an illegitimate regulatory objective, we disagree. Nothing in Article 2.1 prevents a Member from seeking to minimize the potential costs arising from technical regulations, provided that the technical regulation at issue does not overtly or covertly discriminate against imports.

⁴³²Panel Report, para. 2.26 (referring to Indonesia's first written submission to the Panel, para. 18; United States' first written submission to the Panel, para. 35; World Trade Atlas, United States – Imports, Clove Cigarette Market Share Data (Panel Exhibit US-100); and World Trade Atlas, Indonesia Cigarette Exports to the United States, 1998-2009 (Panel Exhibit US-134)).

⁴³³Panel Report, para. 2.27. The Panel nonetheless was able to identify at least one US company that manufactured clove cigarettes prior to the entry into force of the FSPTCA. (*Ibid.* (referring to United States' first written submission to the Panel, para. 35))

⁴³⁴Panel Report, footnote 58 to para. 2.28.

⁴³⁵Panel Report, para. 2.28.

⁴³⁶United States' response to Panel Question 17, para. 43.

223. With respect to the cigarettes that are *not* banned under Section 907(a)(1)(A), the record demonstrates that, in the years 2000 to 2009, between 94.3 and 97.4 per cent of all cigarettes sold in the United States were domestically produced⁴³⁷, and that menthol cigarettes accounted for about 26 per cent of the total US cigarette market.⁴³⁸ Information on the record also shows that three domestic brands dominate the US market for menthol cigarettes: Kool, Salem (Reynolds American), and Newport (Lorillard), with Marlboro having a smaller market share.⁴³⁹

224. Given the above, the design, architecture, revealing structure, operation, and application of Section 907(a)(1)(A) strongly suggest that the detrimental impact on competitive opportunities for clove cigarettes reflects discrimination against the group of like products imported from Indonesia. The products that are prohibited under Section 907(a)(1)(A) consist primarily of clove cigarettes imported from Indonesia, while the like products that are actually permitted under this measure consist primarily of domestically produced menthol cigarettes.

225. Moreover, we are not persuaded that the detrimental impact of Section 907(a)(1)(A) on competitive opportunities for imported clove cigarettes does stem from a legitimate regulatory distinction. We recall that the stated objective of Section 907(a)(1)(A) is to reduce youth smoking. One of the particular characteristics of flavoured cigarettes that makes them appealing to young people is the flavouring that masks the harshness of the tobacco, thus making them more pleasant to start smoking than regular cigarettes.⁴⁴⁰ To the extent that this particular characteristic is present in both clove and menthol cigarettes⁴⁴¹, menthol cigarettes have the same product characteristic that, from the perspective of the stated objective of Section 907(a)(1)(A), justified the prohibition of clove cigarettes. Furthermore, the reasons presented by the United States for the exemption of menthol cigarettes from the ban on flavoured cigarettes do not, in our view, demonstrate that the detrimental impact on competitive opportunities for imported clove cigarettes does stem from a legitimate regulatory distinction. The United States argues that the exemption of menthol cigarettes from the ban on flavoured cigarettes aims at minimizing: (i) the impact on the US health care system associated with treating "millions" of menthol cigarette smokers affected by withdrawal symptoms;

⁴³⁷Cigarettes: Domestic and Imported, 2000-2009 (Panel Exhibit US-31).

⁴³⁸United States' first written submission to the Panel, para. 27 (referring to US Federal Trade Commission, *Cigarette Report for 2006*, Table 1A (2009) (Panel Exhibit US-29); and P.S. Gardiner, "The African Americanization of menthol cigarette use in the United States" (February 2004) 6(1) *Nicotine & Tobacco Research* S55 (Panel Exhibit US-30)).

⁴³⁹See United States' first written submission to the Panel, para. 29 and P.S. Gardiner, "The African Americanization of menthol cigarette use in the United States" (February 2004) 6(1) *Nicotine & Tobacco Research* S55 (Panel Exhibit US-30), p. 58.

⁴⁴⁰Panel Report, paras. 7.216-7.221.

⁴⁴¹Panel Report, para. 7.221 (referring to "Use of Menthol Cigarettes", The National Survey on Drug Use and Health Report, 19 November 2009 (Panel Exhibit IND-66); and American Lung Association, Tobacco Policy Trend Alert, *From Joe Camel to Katani Kolada – the Marketing of Candy-Flavored Cigarettes* (2006) (Panel Exhibit US-35), p. 1, available at <<http://slati.lungusa.org/reports/CandyFlavoredUpdatedAlert.pdf>>).

and (ii) the risk of development of a black market and smuggling of menthol cigarettes to supply the needs of menthol cigarette smokers. Thus, according to the United States, the exemption of menthol cigarettes from the ban on flavoured cigarettes is justified in order to avoid risks arising from withdrawal symptoms that would afflict menthol cigarette smokers in case those cigarettes were banned. We note, however, that the additive ingredient in menthol cigarettes is nicotine, not peppermint or any other ingredient that is exclusively present in menthol cigarettes, and that this ingredient is also present in a group of products that is likewise permitted under Section 907(a)(1)(A), namely, regular cigarettes. Therefore, it is not clear that the risks that the United States claims to minimize by allowing menthol cigarettes to remain in the market would materialize if menthol cigarettes were to be banned, insofar as regular cigarettes would remain in the market.

226. Therefore, even though Section 907(a)(1)(A) does not expressly distinguish between treatment accorded to the imported and domestic like products, it operates in a manner that reflects discrimination against the group of like products imported from Indonesia. Accordingly, despite our reservations on the brevity of the Panel's analysis, we agree with the Panel that, by exempting menthol cigarettes from the ban on flavoured cigarettes, Section 907(a)(1)(A) accords to clove cigarettes imported from Indonesia less favourable treatment than that accorded to domestic like products, within the meaning of Article 2.1 of the *TBT Agreement*.

(b) Article 11 of the DSU

227. Finally, the United States argues that the Panel acted inconsistently with Article 11 of the DSU because it found that Section 907(a)(1)(A) avoids costs on any US entity, in the absence of any basis in the Panel record that would have allowed it to reach such conclusion.⁴⁴² The United States argues that the measure imposed enforcement costs on the United States Food and Drug Administration (the "FDA"), and on domestic producers of cigarettes with characterizing flavours whose potential market was closed off. By reducing youth smoking, Section 907(a)(1)(A) also reduces subsequent demand for cigarettes. Therefore, it also shrinks the "adult" cigarette market, which is comprised almost entirely of domestic producers.⁴⁴³

228. Indonesia responds that the Panel did not act inconsistently with Article 11 of the DSU in reaching its finding, which is supported by evidence showing that the exemption of menthol cigarettes from the ban was the result of a political compromise with the US tobacco industry.⁴⁴⁴

229. We recall that, in *EC – Fasteners (China)*, the Appellate Body considered that "[i]t is ... unacceptable for a participant effectively to recast its arguments before the panel under the guise of an Article 11 claim" and that "a claim that a panel failed to comply with its duties under Article 11 of the DSU must stand by itself and should not be made merely as a subsidiary argument or claim in support of a claim that the panel failed to apply correctly a provision of the covered agreements."⁴⁴⁵ With these considerations in mind, we turn to review the United States' appeal that the Panel acted inconsistently with Article 11 of the DSU in finding that Section 907(a)(1)(A) imposed no costs on any US entity.

230. As noted above, we believe that the Panel did not fully explain the basis for the statement that Section 907(a)(1)(A), while imposing "costs" on foreign producers, imposed "no costs on any US entity". However, the Panel's statement should be read in the light of the fact that, in paragraph 7.289 of its Report, the Panel considered the costs imposed on producers "at the time of the ban" and that it equated the concept of "entity" with that of "producer", thus comparing the costs imposed on producers in Indonesia with the costs imposed on US producers, to the exclusion of government entities such as the FDA.

231. It seems to us that the United States' claim is concerned with the Panel's less favourable treatment comparison, rather than with the alleged absence of evidence in the Panel record justifying the lack of costs on any US entity. We note that the United States argues that the Panel erred, under Article 2.1 of the *TBT Agreement*, in limiting the scope of its less favourable treatment analysis to the effects of Section 907(a)(1)(A) on all domestic cigarettes at the time the measure entered into force, to the exclusion of flavoured cigarettes that were produced in the United States before the ban came into force.⁴⁴⁶ In our view, the United States' argument that the Panel erred in not considering the impact of Section 907(a)(1)(A) on US producers before the entry into force of the ban also implies that the Panel was wrong in stating that the measure imposed no costs on any US producers. We thus consider that the claim by the United States that the Panel violated Article 11 of the DSU because it found that Section 907(a)(1)(A) imposed "no costs on any US entity" is subsidiary to its claim that the Panel erred in concluding that Section 907(a)(1)(A) accords less favourable treatment to imported clove cigarettes than to like menthol cigarettes of national origin within the meaning of Article 2.1 of the *TBT Agreement*.

232. In the light of the above, we do not consider that the Panel acted inconsistently with Article 11 of the DSU in finding that Section 907(a)(1)(A) accords imported clove cigarettes less

⁴⁴⁵ Appellate Body Report, *EC – Fasteners (China)*, para. 442. See also Appellate Body Report, *US – Steel Safeguards*, para. 498; and Appellate Body Report, *Chile – Price Band System (Article 2.1.5 – Argentina)*, para. 238.

⁴⁴⁶ United States' appellant's submission, para. 96.

favourable treatment than that accorded to domestic menthol cigarettes, within the meaning of Article 2.1 of the *TBT Agreement*.

6. Conclusion on "Treatment No Less Favourable"

233. Given the above, we *uphold*, albeit for different reasons, the Panel's finding, in paragraph 7.292 of the Panel Report, that, by banning clove cigarettes while exempting menthol cigarettes from the ban, Section 907(a)(1)(A) of the FFDCA accords imported clove cigarettes less favourable treatment than that accorded to domestic menthol cigarettes, within the meaning of Article 2.1 of the *TBT Agreement*.

D. *Conclusions under Article 2.1 of the TBT Agreement*

234. In the light of the foregoing considerations with regard to the Panel's findings on likeness and less favourable treatment, we therefore *uphold*, albeit for different reasons, the Panel's finding, in paragraphs 7.293 and 8.1(b) of the Panel Report, that Section 907(a)(1)(A) of the FFDCA is inconsistent with Article 2.1 of the *TBT Agreement* because it accords to imported clove cigarettes less favourable treatment than that accorded to like menthol cigarettes of national origin.

235. In reaching this conclusion, we wish to clarify the implications of our decision. We do not consider that the *TBT Agreement* or any of the covered agreements is to be interpreted as preventing Members from devising and implementing public health policies generally, and tobacco-control policies in particular, through the regulation of the content of tobacco products, including the prohibition or restriction on the use of ingredients that increase the attractiveness and palatability of cigarettes for young and potential smokers. Moreover, we recognize the importance of Members' efforts in the World Health Organization on tobacco control.

236. While we have upheld the Panel's finding that the specific measure at issue in this dispute is inconsistent with Article 2.1 of the *TBT Agreement*, we are not saying that a Member cannot adopt measures to pursue legitimate health objectives such as curbing and preventing youth smoking. In particular, we are not saying that the United States cannot ban clove cigarettes: however, if it chooses to do so, this has to be done consistently with the *TBT Agreement*. Although Section 907(a)(1)(A) pursues the legitimate objective of reducing youth smoking by banning cigarettes containing flavours and ingredients that increase the attractiveness of tobacco to youth, it does so in a manner that is inconsistent with the national treatment obligation in Article 2.1 of the *TBT Agreement* as a result of the exemption of menthol cigarettes, which similarly contain flavours and ingredients that increase the attractiveness of tobacco to youth, from the ban on flavoured cigarettes.

VI. **Article 2.12 of the *TBT Agreement***

A. *Introduction*

237. We turn now to the United States' appeal of the Panel's finding that, by failing to allow a period of not less than six months between the publication and the entry into force of Section 907(a)(1)(A) of the FFDCA, the United States acted inconsistently with Article 2.12 of the *TBT Agreement*.

238. The FSPTCA was enacted on 22 June 2009. The measure at issue, Section 907(a)(1)(A), entered into force three months thereafter. Before the Panel, Indonesia argued that paragraph 5.2 of the Doha Ministerial Decision on Implementation-Related Issues and Concerns⁴⁴⁷ ("the Doha Ministerial Decision")—which defined the term "reasonable interval" in Article 2.12 of the *TBT Agreement* as at least six months—constitutes a legally binding interpretation pursuant to Article IX:2 of the *WTO Agreement*. Thus, according to Indonesia, by not allowing a reasonable interval of at least six months between the publication and the entry into force of Section 907(a)(1)(A), the United States acted inconsistently with its obligations under Article 2.12 of the *TBT Agreement*.⁴⁴⁸ The Panel framed the question before it as whether the United States acted inconsistently with its obligations under Article 2.12 by allowing an interval of three months between the enactment of the FSPTCA and the entry into force of Section 907(a)(1)(A). In particular, the Panel considered whether, as Indonesia claimed, Article 2.12 "obliged the United States to allow *as a minimum* a period of *six months* between the publication and the entry into force of Section 907(a)(1)(A)".⁴⁴⁹

239. In its analysis of Indonesia's claim under Article 2.12 of the *TBT Agreement*, the Panel considered the interpretative value of paragraph 5.2 of the Doha Ministerial Decision. The Panel took the view that, although the United States and Indonesia disagreed on the categorization of paragraph 5.2 as an authoritative interpretation under Article IX:2 of the *WTO Agreement*, it would "be guided by [the Doha Ministerial Decision] in its interpretation of the phrase 'reasonable interval' as [the Doha Ministerial Decision] was agreed by all WTO Members meeting in the form of Ministerial Conference, the highest ranking body of the WTO". Moreover, the Panel stated that, in its view, "paragraph 5.2 of the Doha Ministerial Decision could be considered as a subsequent agreement

⁴⁴⁷Decision of 14 November 2001, WT/MIN(01)/17, para. 5.2.

⁴⁴⁸Panel Report, para. 7.552.

⁴⁴⁹Panel Report, para. 7.561. (original emphasis)

of the parties", within the meaning of Article 31(3)(a) of the *Vienna Convention*, on the interpretation of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*.⁴⁵⁰

240. The United States claims on appeal that: (i) the Panel attributed an incorrect "interpretative value" to paragraph 5.2 of the Doha Ministerial Decision in its interpretation of Article 2.12 of the *TBT Agreement*; and (ii) the Panel erred in finding that Indonesia had established a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement*, that the United States failed to rebut.

B. *The Interpretative Value of Paragraph 5.2 of the Doha Ministerial Decision*

241. We recall that, with regard to the interpretative value of paragraph 5.2 of the Doha Ministerial Decision, the Panel stated that it "must be guided by [paragraph 5.2] in its interpretation of the phrase 'reasonable interval', as [paragraph 5.2] was agreed by all WTO Members meeting in the form of Ministerial Conference, the highest ranking body of the WTO".⁴⁵¹

242. According to the United States, the Panel "declined to formally determine" whether paragraph 5.2 constitutes an authoritative interpretation of Article 2.12, "only saying that it 'must be guided' by paragraph 5.2" because it was agreed by all WTO Members meeting in the form of Ministerial Conference, the highest ranking body of the WTO.⁴⁵² The United States submits that, despite not having found that paragraph 5.2 has the legal status of an authoritative interpretation adopted pursuant to Article IX:2 of the *WTO Agreement*, the Panel erred by applying paragraph 5.2 as a "rule" that amended the text of Article 2.12 of the *TBT Agreement*.⁴⁵³ The United States claims that the legal value of paragraph 5.2 is at most a supplementary means of interpretation within the meaning of Article 32 of the *Vienna Convention*.⁴⁵⁴

243. Indonesia responds that "the Panel *did* establish that paragraph 5.2 of the Doha Ministerial Decision is a binding interpretation as per Article IX:2 of the *WTO Agreement*", and that it may also be considered a subsequent agreement between the parties, within the meaning of Article 31(3)(a) of the *Vienna Convention*, on the interpretation of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*.⁴⁵⁵

244. In paragraph 7.575 of its Report, the Panel stated that the wording of paragraph 5.2 of the Doha Ministerial Decision "*appears to suggest* that the intention of the Ministerial Conference, and thus the highest level organ of the WTO where all Members meet, was that paragraph 5.2 is

⁴⁵⁰Panel Report, para. 7.576.

⁴⁵¹Panel Report, para. 7.576.

⁴⁵²United States' appellant's submission, para. 124 (referring to Panel Report, para. 7.576).

⁴⁵³United States' appellant's submission, para. 129.

⁴⁵⁴United States' appellant's submission, para. 126.

⁴⁵⁵Indonesia's appellee's submission, para. 222. (original emphasis)

binding".⁴⁵⁶ On appeal, Indonesia relies on this latter statement made by the Panel and argues that the Panel found that paragraph 5.2 of the Doha Ministerial Decision is a binding interpretation "as per" Article IX:2 of the *WTO Agreement*.⁴⁵⁷

245. In paragraph 7.576 of its Report, the Panel stated that, although the United States and Indonesia disagreed on the categorization of paragraph 5.2 of the Doha Ministerial Decision as an authoritative interpretation under Article IX:2 of the *WTO Agreement*, it would be "guided by [paragraph 5.2] in its interpretation of the phrase 'reasonable interval', as it was agreed by all WTO Members meeting in the form of Ministerial Conference, the highest ranking body of the WTO". On appeal, the United States relies on this statement of the Panel and argues that the Panel did not find that paragraph 5.2 constitutes an authoritative interpretation adopted by the Ministerial Conference pursuant to Article IX:2 of the *WTO Agreement*.⁴⁵⁸

246. As we see it, in paragraph 7.575 of its Report, the Panel identified certain features of the Doha Ministerial Decision that *suggest* that Members intended to adopt a "binding" interpretation of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*. The Panel's statement in paragraph 7.575 was, by its own terms, tentative. Moreover, the Panel's statement was not followed by any "finding" that paragraph 5.2 constitutes an interpretation adopted pursuant to Article IX:2 of the *WTO Agreement*. Thus, we do not agree with Indonesia that the Panel *found* that paragraph 5.2 of the Doha Ministerial Decision "is a binding interpretation as per Article IX:2 of the *WTO Agreement*".⁴⁵⁹

247. Despite our conclusion that the Panel did not formally determine whether paragraph 5.2 of the Doha Ministerial Decision constitutes a multilateral interpretation under Article IX:2 of the *WTO Agreement*, we will consider, nevertheless, whether paragraph 5.2, in fact, has that legal status. Before doing so, we set forth some general considerations on the role and function of multilateral interpretations adopted pursuant to Article IX:2 of the *WTO Agreement*.

⁴⁵⁶Emphasis added.

⁴⁵⁷Indonesia's appellee's submission, para. 222.

⁴⁵⁸United States' appellant's submission, para. 124.

⁴⁵⁹Indonesia's appellee's submission, para. 222.

248. Article IX:2 of the *WTO Agreement* provides:

The Ministerial Conference and the General Council shall have the exclusive authority to adopt interpretations of this Agreement and of the Multilateral Trade Agreements. In the case of an interpretation of a Multilateral Trade Agreement in Annex 1, they shall exercise their authority on the basis of a recommendation by the Council overseeing the functioning of that Agreement. The decision to adopt an interpretation shall be taken by a three-fourths majority of the Members. This paragraph shall not be used in a manner that would undermine the amendment provisions in Article X.

249. In *EC – Bananas III (Article 21.5 – Ecuador II) / EC – Bananas III (Article 21.5 – US)*, the Appellate Body opined that multilateral interpretations adopted pursuant to Article IX:2 of the *WTO Agreement* are "meant to clarify the meaning of existing obligations, not to modify their content".⁴⁶⁰ Article IX:2 establishes that a decision to adopt a multilateral interpretation can only be taken by Members sitting in the form of the Ministerial Conference or the General Council, and that such decisions must be taken by a three-fourths majority of Members. With regard to decisions adopting multilateral interpretations of a Multilateral Trade Agreement contained in Annex 1 to the *WTO Agreement*, Article IX:2 requires the Ministerial Conference or the General Council to exercise its authority on the basis of a recommendation by the Council overseeing the functioning of that Agreement. Thus, while Article IX:2 confers upon the Ministerial Conference and the General Council the exclusive authority to adopt multilateral interpretations of the *WTO Agreement*, the exercise of this authority is situated within defined parameters established by Article IX:2.

250. Multilateral interpretations adopted pursuant to Article IX:2 of the *WTO Agreement* have a pervasive legal effect. Such interpretations are binding on all Members. As we see it, the broad legal effect of these interpretations is precisely the reason why Article IX:2 subjects the adoption of such interpretations to clearly articulated and strict decision-making procedures.

251. Turning to the question of whether paragraph 5.2 of the Doha Ministerial Decision can be characterized as a multilateral interpretation of Article 2.12 of the *TBT Agreement*, we recall that Article IX:2 of the *WTO Agreement* establishes two specific requirements that apply to the adoption of multilateral interpretations of the Multilateral Trade Agreements contained in Annex 1 to the *WTO Agreement*: (i) a decision by the Ministerial Conference or the General Council to adopt such interpretations shall be taken by a three-fourths majority of Members; and (ii) such interpretations shall be taken on the basis of a recommendation by the Council overseeing the functioning of the

relevant Agreement. Thus, we will consider whether the decision to adopt paragraph 5.2 conforms with these specific decision-making procedures.

252. With regard to the first requirement, the Panel observed that the Ministerial Conference decided on the matters addressed in the Doha Ministerial Decision *by consensus*. The issue of whether the first requirement was met has not been raised in this appeal. With regard to the second requirement, the Panel noted that, "it appears that when adopting the Doha Ministerial Decision, the Ministerial Conference did not comply with the preliminary requirement under Article IX:2 of the *WTO Agreement*" to exercise its authority on the basis of a recommendation from the Council for Trade in Goods.⁴⁶¹ The Panel stated, further, that "it could be argued" that the absence of this "formal requirement" is insufficient to conclude that paragraph 5.2 of the Doha Ministerial Decision is not an authoritative interpretation under Article IX:2 of the *WTO Agreement*.⁴⁶² On appeal, the United States argues that "[a] panel is not authorized to waive the requirements of Article IX:2 or to impose on Members an interpretation that is not adopted in the manner required."⁴⁶³

253. We do not agree with the Panel to the extent that it suggested that the absence of a recommendation from the Council for Trade in Goods "is insufficient to conclude that paragraph 5.2 of the Doha Ministerial Decision is not an authoritative interpretation under Article IX:2 of the *WTO Agreement*".⁴⁶⁴ While Article IX:2 of the *WTO Agreement* confers upon the Ministerial Conference and the General Council the exclusive authority to adopt multilateral interpretations of the *WTO Agreement*, this authority must be exercised within the defined parameters of Article IX:2. It seems to us that the view expressed by the Panel does not respect a specific decision-making procedure established by Article IX:2 of the *WTO Agreement*. In our view, to characterize the requirement to act on the basis of a recommendation by the Council overseeing the functioning of the relevant Agreement as a "formal requirement" neither permits a panel to read that requirement out of a treaty provision, nor to dilute its effectiveness.

254. Although the Panel's reasoning may be read as suggesting that the Ministerial Conference could dispense with a specific requirement established by Article IX:2 of the *WTO Agreement*, the terms of Article IX:2 do not suggest that compliance with this requirement is dispensable. In this connection, we recall that, pursuant to Article IX:2 of the *WTO Agreement*, the Ministerial Conference or the General Council "*shall*" exercise their authority to adopt an interpretation of a

⁴⁶¹Panel Report, para. 7.574 (referring to United States' response to Panel Question 6, para. 5). (emphasis added)

⁴⁶²Panel Report, para. 7.575.

⁴⁶³United States' appellant's submission, para. 125.

⁴⁶⁴Panel Report, para. 7.575.

Multilateral Trade Agreement contained in Annex 1 to the *WTO Agreement* "on the basis of a recommendation" by the Council overseeing the functioning of that Agreement. We consider that the recommendation from the relevant Council is an essential element of Article IX:2, which constitutes the legal basis upon which the Ministerial Conference or the General Council exercise their authority to adopt interpretations of the *WTO Agreement*. Thus, an interpretation of a Multilateral Trade Agreement contained in Annex 1 to the *WTO Agreement* must be adopted on the basis of a recommendation from the relevant Council overseeing the functioning of that Agreement.

255. We note that, before the Panel, Indonesia relied on paragraph 12 of the Doha Ministerial Declaration⁴⁶⁵ and on the preamble of the Doha Ministerial Decision, and argued that the interpretation of Article 2.12 of the *TBT Agreement* was reached on the basis of discussions carried out within the General Council and the WTO subsidiary bodies.⁴⁶⁶ Whereas the content of paragraph 5.2 of the Doha Ministerial Decision might very well have been based on discussions within the Committee on Technical Barriers to Trade, we are not persuaded that this is sufficient to establish that the Ministerial Conference exercised its authority to adopt an interpretation of the *TBT Agreement* on the basis of a *recommendation* from the Council for Trade in Goods. Accordingly, we find that, in the absence of evidence of the existence of a specific recommendation from the Council for Trade in Goods concerning the interpretation of Article 2.12 of the *TBT Agreement*, paragraph 5.2 of the Doha Ministerial Decision does not constitute a multilateral interpretation adopted pursuant to Article IX:2 of the *WTO Agreement*.⁴⁶⁷

256. In the light of our finding that paragraph 5.2 of the Doha Ministerial Decision does not qualify as a multilateral interpretation within the meaning of Article IX:2 of the *WTO Agreement*, we address whether, as the Panel found, paragraph 5.2 "could be considered as a subsequent agreement of the parties within the meaning of Article 31(3)(a) of the [*Vienna Convention*], on the interpretation of 'reasonable interval' [in] Article 2.12 of the *TBT Agreement*".⁴⁶⁸

257. We note that, in response to questioning at the oral hearing, the United States argued that a decision by the Ministerial Conference that does not conform with the specific decision-making procedures established by Article IX:2 of the *WTO Agreement* cannot constitute a "subsequent agreement between the parties" within the meaning of Article 31(3)(a) of the *Vienna Convention*. We

⁴⁶⁵ Adopted on 14 November 2001, WT/MIN(01)/DEC/1.

⁴⁶⁶ Panel Report, para. 7.574 (referring to Indonesia's response to Panel Question 6, para. 27).

⁴⁶⁷ In reaching this finding, we are not saying that the Ministerial Conference failed to comply with a specific decision-making procedure established by Article IX:2 of the *WTO Agreement*. Rather, we are saying that the absence of a recommendation from the Council for Trade in Goods concerning the interpretation of Article 2.12 of the *TBT Agreement* supports a conclusion that paragraph 5.2 of the Doha Ministerial Decision does not constitute a multilateral interpretation adopted pursuant to Article IX:2 of the *WTO Agreement*.

⁴⁶⁸ Panel Report, para. 7.576. (footnote omitted)

observe that multilateral interpretations adopted pursuant to Article IX:2 of the *WTO Agreement*, on the one hand, and subsequent agreements on interpretation within the meaning of Article 31(3)(a) of the *Vienna Convention*, on the other hand, serve different functions and have different legal effects under WTO law. Multilateral interpretations under Article IX:2 of the *WTO Agreement* provide a means by which Members—acting through the highest organs of the WTO—may adopt binding interpretations that clarify WTO law for all Members. Such interpretations are binding on all Members, including in respect of all disputes in which these interpretations are relevant.

258. On the other hand, Article 31(3)(a) of the *Vienna Convention* is a rule of treaty interpretation, pursuant to which a treaty interpreter uses a subsequent agreement between the parties on the interpretation of a treaty provision as an interpretative tool to determine the meaning of that treaty provision. Pursuant to Article 3.2 of the DSU, panels and the Appellate Body are required to apply the customary rules of interpretation of public international law—including the rule embodied in Article 31(3)(a) of the *Vienna Convention*—to clarify the existing provisions of the covered agreements. Interpretations developed by panels and the Appellate Body in the course of dispute settlement proceedings are binding only on the parties to a particular dispute.⁴⁶⁹ Article IX:2 of the *WTO Agreement* does not preclude panels and the Appellate Body from having recourse to a customary rule of interpretation of public international law that, pursuant to Article 3.2 of the DSU, they are required to apply.

259. We also recall that, in *EC – Bananas III (Article 21.5 – Ecuador II) / EC – Bananas III (Article 21.5 – US)*, the Appellate Body stated that "multilateral interpretations are meant to clarify the meaning of existing obligations"⁴⁷⁰ and that "multilateral interpretations adopted pursuant to Article IX:2 of the *WTO Agreement* are *most akin* to subsequent agreements within the meaning of Article 31(3)(a) of the *Vienna Convention*".⁴⁷¹ Thus, given the specific function of multilateral

⁴⁶⁹ In *US – Stainless Steel (Mexico)*, the Appellate Body stated:

It is well settled that Appellate Body reports are not binding, except with respect to resolving the particular dispute between the parties. This, however, does not mean that subsequent panels are free to disregard the legal interpretations and the *ratio decidendi* contained in previous Appellate Body reports that have been adopted by the DSB.

... Thus, the legal interpretation embodied in adopted panel and Appellate Body reports becomes part and parcel of the *acquis* of the WTO dispute settlement system. Ensuring "security and predictability" in the dispute settlement system, as contemplated in Article 3.2 of the DSU, implies that, absent cogent reasons, an adjudicatory body will resolve the same legal question in the same way in a subsequent case.

(Appellate Body Report, *US – Stainless Steel (Mexico)*, paras. 158 and 160 (footnotes omitted))
⁴⁷⁰ Appellate Body Reports, *EC – Bananas III (Article 21.5 – Ecuador II) / EC – Bananas III (Article 21.5 – US)*, para. 383.

⁴⁷¹ Appellate Body Reports, *EC – Bananas III (Article 21.5 – Ecuador II) / EC – Bananas III (Article 21.5 – US)*, para. 390. (emphasis added)

interpretations adopted pursuant to Article IX:2, and the fact that these interpretations are adopted by Members sitting in the form of the highest organs of the WTO, such interpretations are most akin to, but *not exhaustive of*, subsequent agreements on interpretation within the meaning of Article 31(3)(a) of the *Vienna Convention*.

260. We consider, therefore, that a decision adopted by Members, *other than* a decision adopted pursuant to Article IX:2 of the *WTO Agreement*, may constitute a "subsequent agreement" on the interpretation of a provision of a covered agreement under Article 31(3)(a) of the *Vienna Convention*. Accordingly, we turn to the issue of whether paragraph 5.2 of the Doha Ministerial Decision can be considered to be a subsequent agreement, within the meaning of Article 31(3)(a) of the *Vienna Convention*, on the interpretation of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*.

261. Article 31(3)(a) of the *Vienna Convention* provides:

There shall be taken into account, together with the context:

- (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions[.]

262. Based on the text of Article 31(3)(a) of the *Vienna Convention*, we consider that a decision adopted by Members may qualify as a "subsequent agreement between the parties" regarding the interpretation of a covered agreement or the application of its provisions if: (i) the decision is, in a temporal sense, adopted subsequent to the relevant covered agreement; and (ii) the terms and content of the decision express an *agreement* between Members on the *interpretation* or *application* of a provision of WTO law.

263. With regard to the first element, we note that the Doha Ministerial Decision was adopted by consensus on 14 November 2001 on the occasion of the Fourth Ministerial Conference of the WTO. Thus, it is beyond dispute that paragraph 5.2 of the Doha Ministerial Decision was adopted subsequent to the relevant WTO agreement at issue, the *TBT Agreement*. With regard to the second element, the key question to be answered is whether paragraph 5.2 of the Doha Ministerial Decision expresses an *agreement* between Members on the *interpretation* or *application* of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*.

264. We recall that paragraph 5.2 of the Doha Ministerial Decision provides:

Subject to the conditions specified in paragraph 12 of Article 2 of the Agreement on Technical Barriers to Trade, the phrase "reasonable interval" shall be understood to mean normally a period of not less

than 6 months, except when this would be ineffective in fulfilling the legitimate objectives pursued.

265. In addressing the question of whether paragraph 5.2 of the Doha Ministerial Decision expresses an agreement between Members on the interpretation or application of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*, we find useful guidance in the Appellate Body reports in *EC – Bananas III (Article 21.5 – Ecuador II) / EC – Bananas III (Article 21.5 – US)*. The Appellate Body observed that the International Law Commission (the "ILC") describes a subsequent agreement within the meaning of Article 31(3)(a) of the *Vienna Convention* as "a further *authentic element of interpretation* to be taken into account together with the context". According to the Appellate Body, "by referring to 'authentic interpretation', the ILC reads Article 31(3)(a) as referring to *agreements bearing specifically upon the interpretation of the treaty*."⁴⁷² Thus, we will consider whether paragraph 5.2 bears specifically upon the interpretation of Article 2.12 of the *TBT Agreement*.

266. Paragraph 5.2 of the Doha Ministerial Decision refers explicitly to the term "reasonable interval" in Article 2.12 of the *TBT Agreement* and defines this interval as "normally a period of not less than 6 months, except when this would be ineffective in fulfilling the legitimate objectives pursued" by a technical regulation. In the light of the terms and content of paragraph 5.2, we are unable to discern a function of paragraph 5.2 *other than* to interpret the term "reasonable interval" in Article 2.12 of the *TBT Agreement*. We consider, therefore, that paragraph 5.2 *bears specifically* upon the interpretation of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*. We turn now to consider whether paragraph 5.2 of the Doha Ministerial Decision reflects an "agreement" among Members—within the meaning of Article 31(3)(a) of the *Vienna Convention*—on the interpretation of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*.

267. We note that the text of Article 31(3)(a) of the *Vienna Convention* does not establish a requirement as to the form which a "subsequent agreement between the parties" should take. We consider, therefore, that the term "agreement" in Article 31(3)(a) of the *Vienna Convention* refers, fundamentally, to substance rather than to form. Thus, in our view, paragraph 5.2 of the Doha Ministerial Decision can be characterized as a "subsequent agreement" within the meaning of Article 31(3)(a) of the *Vienna Convention* provided that it clearly expresses a common understanding, and an acceptance of that understanding among Members with regard to the meaning of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*. In determining whether this is so, we find the terms and content of paragraph 5.2 to be dispositive. In this connection, we note that the understanding among Members with regard to the meaning of the term "reasonable interval" in

⁴⁷²Appellate Body Reports, *EC – Bananas III (Article 21.5 – Ecuador II) / EC – Bananas III (Article 21.5 – US)*, para. 390. (emphasis added)

Article 2.12 of the *TBT Agreement* is expressed by terms—"shall be understood to mean"—that cannot be considered as merely hortatory.

268. For the foregoing reasons, we uphold the Panel's finding, in paragraph 7.576 of the Panel Report, that paragraph 5.2 of the Doha Ministerial Decision constitutes a subsequent agreement between the parties, within the meaning of Article 31(3)(a) of the *Vienna Convention*, on the interpretation of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*.

269. In the light of our characterization of paragraph 5.2 of the Doha Ministerial Decision as a subsequent agreement between the parties within the meaning of Article 31(3)(a) of the *Vienna Convention*, we turn now to consider the meaning of Article 2.12 of the *TBT Agreement* in the light of the clarification of the term "reasonable interval" provided by paragraph 5.2. We observe that, in its commentaries on the *Draft articles on the Law of Treaties*, the ILC states that a subsequent agreement between the parties within the meaning of Article 31(3)(a) "must be read into the treaty for purposes of its interpretation".⁴⁷³ As we see it, while the terms of paragraph 5.2 must be "read into" Article 2.12 for the purpose of interpreting that provision, this does not mean that the terms of paragraph 5.2 replace or override the terms contained in Article 2.12. Rather, the terms of paragraph 5.2 of the Doha Ministerial Decision constitute an interpretative clarification to be taken into account in the interpretation of Article 2.12 of the *TBT Agreement*.

270. Article 2.12 of the *TBT Agreement* provides:

Except in those urgent circumstances referred to in paragraph 10, Members shall allow a reasonable interval between the publication of technical regulations and their entry into force in order to allow time for producers in exporting Members, and particularly in developing country Members, to adapt their products or methods of production to the requirements of the importing Member.

271. Paragraph 5.2 of the Doha Ministerial Decision provides:

Subject to the conditions specified in paragraph 12 of Article 2 of the Agreement on Technical Barriers to Trade, the phrase "reasonable interval" shall be understood to mean normally a period of not less than 6 months, except when this would be ineffective in fulfilling the legitimate objectives pursued.

⁴⁷³*Draft articles on the Law of Treaties with commentaries*. Text adopted by the ILC at its eighteenth session, in 1966, and submitted to the United Nations General Assembly as a part of the Commission's report covering the work of that session (at para. 38). The ILC report, which also contains commentaries on the draft articles, appears in the *Yearbook of the International Law Commission, 1966*, Vol. II, p. 221, para. 14.

272. We note, as did the Panel, that Article 2.12 of the *TBT Agreement* explains that "the reason for allowing an interval between the publication and the entry into force of a technical regulation is to allow time for producers in exporting Members, and particularly in developing country Members, to adapt their products or methods of production" to the requirements of the importing Member's technical regulation.⁴⁷⁴ In our view, the term "normally" in paragraph 5.2 relates to the rationale of the obligation articulated in Article 2.12 of the *TBT Agreement*. Seen in this light, the term "normally" provides the interpretative link between Article 2.12, on the one hand, and paragraph 5.2, on the other hand. Thus, we consider that, taking into account the interpretative clarification provided by paragraph 5.2 of the Doha Ministerial Decision, Article 2.12 of the *TBT Agreement* establishes a rule that "normally" producers in exporting Members require a period of "not less than 6 months" to adapt their products or production methods to the requirements of an importing Member's technical regulation.

273. On appeal, the United States argues that the use of the term "normally" in paragraph 5.2 of the Doha Ministerial Decision does not support the conclusion that paragraph 5.2 represents a rule.⁴⁷⁵ We observe that the ordinary meaning of the term "normally" is defined as "under normal or ordinary conditions: as a rule".⁴⁷⁶ In our view, the qualification of an obligation with the adverb "normally" does not, necessarily, alter the characterization of that obligation as constituting a "rule". Rather, we consider that the use of the term "normally" in paragraph 5.2 indicates that the rule establishing that foreign producers require a minimum of "not less than 6 months" to adapt to the requirements of a technical regulation admits of derogation under certain circumstances.

274. The obligation imposed on Members by Article 2.12 to provide a "reasonable interval" between the publication and the entry into force of their technical regulations carefully balances the interests of, on the one hand, the exporting Member whose producers might be affected by a technical regulation and, on the other hand, the importing Member that wishes to pursue a legitimate objective through a technical regulation. With regard to the former, Article 2.12 of the *TBT Agreement*, as clarified by paragraph 5.2 of the Doha Ministerial Decision, establishes a rule that, "normally", producers in exporting Members require a period of at least six months to adapt their products or production methods to the requirements of the importing Member's technical regulation. Thus, Article 2.12 presumes that foreign producers in exporting Members, and particularly in developing country Members, require a minimum of at least six months to adapt to the requirements of an importing Member's technical regulation.

⁴⁷⁴Panel Report, para. 7.582.

⁴⁷⁵United States' appellant's submission, para. 127.

⁴⁷⁶*Shorter Oxford English Dictionary*, 6th edn, A. Stevenson (ed.) (Oxford University Press, 2007), Vol. 2, p. 1945.

275. With regard to the interests of the importing Member, we recall that paragraph 5.2 of the Doha Ministerial Decision tempers the obligation to provide a "reasonable interval" of not less than six months between the publication and the entry into force of a technical regulation by stipulating that this obligation applies "except when this would be ineffective in fulfilling the legitimate objectives pursued" by the technical regulation. Thus, while Article 2.12 of the *TBT Agreement* imposes an obligation on importing Members to provide a "reasonable interval" of not less than six months between the publication and entry into force of a technical regulation, an importing Member may depart from this obligation if this interval "would be ineffective to fulfil the legitimate objectives pursued" by the technical regulation.

C. *The Panel's Finding that the United States Acted Inconsistently with Article 2.12 of the TBT Agreement*

276. We turn now to consider the United States' claim that the Panel erred in finding that Indonesia had established a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement* that the United States failed to rebut. The United States advances, essentially, two arguments in support of its claim that the Panel incorrectly found that Indonesia had established a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement*. First, the United States argues that the Panel erred in finding that Indonesia had established a *prima facie* case because Indonesia did not establish that the three-month interval between the publication and entry into force of Section 907(a)(1)(A) of the FFDCA was unreasonable in the light of its impact on the ability of Indonesian producers to adapt to the requirements of that measure.⁴⁷⁷ Second, the United States argues that, even assuming *arguendo* that the Panel was correct in deciding that the elements of a *prima facie* case may be drawn exclusively from paragraph 5.2 of the Doha Ministerial Decision, the Panel erred in finding that Indonesia had "succeeded in making such a case".⁴⁷⁸

277. According to the United States, in view of the elements contained in paragraph 5.2 of the Doha Ministerial Decision, Indonesia "would have to establish with evidence and argument" a *prima facie* case that: (i) "urgent circumstances" did not exist; (ii) the interval period was less than six months; (iii) "this is a 'normal' situation"; and (iv) allowing an interval of at least six months would not render the fulfilment of the objective pursued by Section 907(a)(1)(A) ineffective.⁴⁷⁹ Indonesia, in response, argues that it did establish "a *prima facie* case that the 90-day interval provided by the United States was significantly shorter than the 6 months" normally required.⁴⁸⁰

⁴⁷⁷United States' appellant's submission, paras. 132-134.

⁴⁷⁸United States' appellant's submission, para. 135.

⁴⁷⁹United States' appellant's submission, para. 136.

⁴⁸⁰Indonesia's appellee's submission, para. 237.

278. The United States and Indonesia do not agree on the elements of a *prima facie* case that a complaining Member is required to establish under Article 2.12 of the *TBT Agreement*. Moreover, it appears that the divergence stems from the fact that the United States and Indonesia attribute a different interpretative value to paragraph 5.2 of the Doha Ministerial Decision. In this connection, we note that the United States argues that the elements of a *prima facie* case of inconsistency with Article 2.12 are to be drawn from the text of Article 2.12, but that, "[e]ven assuming *arguendo* that the Panel" could draw the elements of a *prima facie* case from paragraph 5.2, the Panel erred in finding that Indonesia had made such a case.⁴⁸¹

279. We do not consider that the elements of a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement* are to be drawn exclusively from either the terms of Article 2.12, on the one hand, or of paragraph 5.2 of the Doha Ministerial Decision, on the other hand. Article 2.12 imposes an obligation on importing Members to allow a "reasonable interval" between the publication and the entry into force of their technical regulations. We recall our finding above that paragraph 5.2 of the Doha Ministerial Decision constitutes a subsequent agreement between the parties, within the meaning of Article 31(3)(a) of the *Vienna Convention*, on the interpretation of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*. Thus, it seems to us that the elements of a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement* are to be drawn from a proper interpretation of Article 2.12, taking into account—pursuant to Article 31(3)(a) of the *Vienna Convention*—the interpretative clarification provided by the terms of paragraph 5.2 of the Doha Ministerial Decision.

280. We further recall our finding above that Article 2.12 of the *TBT Agreement*, properly interpreted in the light of paragraph 5.2 of the Doha Ministerial Decision, establishes a rule that, "normally", producers in exporting Members require a period of at least six months to adapt their products or production methods to the requirements of the importing Member's technical regulation. Based on our interpretation of Article 2.12 of the *TBT Agreement*, we consider that a *prima facie* case of inconsistency with Article 2.12 is established where it is shown that an importing Member has failed to allow an interval of not less than six months between the publication and the entry into force of the technical regulation at issue.

281. In accordance with the general rules on burden of proof reflected in *US – Wool Shirts and Blouses*, we consider that, under Article 2.12 of the *TBT Agreement*, it is for the complaining Member to establish that the responding Member has not allowed an interval of not less than six months

⁴⁸¹United States' appellant's submission, para. 135.

between the publication and the entry into force of the technical regulation at issue.⁴⁸² If the complaining Member establishes this *prima facie* case of inconsistency, it is for the responding Member to rebut the *prima facie* case of inconsistency with Article 2.12. We recall that, in *US – Wool Shirts and Blouses*, the Appellate Body stated that "precisely how much and precisely what kind of evidence" will be required to establish a *prima facie* case "will necessarily vary from measure to measure, provision to provision, and case to case".⁴⁸³ We consider that, similarly, this reasoning applies with regard to the quantity and nature of evidence required to *rebut* a *prima facie* case of inconsistency.

282. The text of Article 2.12 of the *TBT Agreement* read in the light of paragraph 5.2 of the Doha Ministerial Decision provides an indication of the nature of evidence that is required to rebut a *prima facie* case of inconsistency with that provision. First, Article 2.12 of the *TBT Agreement* excludes from the obligation to provide a "reasonable interval" between the publication and the entry into force of technical regulations "those urgent circumstances" referred to in Article 2.10 of the *TBT Agreement*. Thus, where "urgent problems of safety, health, environmental protection or national security" arise for a Member that is implementing a technical regulation, a period of six months or more cannot be considered to be a "reasonable interval" within the meaning of Article 2.12. Second, Article 2.12 expressly states that the rationale for providing a "reasonable interval" between the publication and the entry into force of a technical regulation is "to allow time for producers in exporting Members, and particularly in developing country Members, to adapt their products or methods of production" to the requirements of the importing Member's technical regulation. If these producers can adapt their products or production methods to the requirements of an importing Member's technical regulation in less than six months, a period of six months or more cannot be considered to be a "reasonable interval" within the meaning of Article 2.12. Third, paragraph 5.2 allows an importing Member to depart from the obligation to provide a "reasonable interval" of, "normally", not less than six months between the publication and entry into force of their technical regulation, if this interval would be "ineffective to fulfil the legitimate objectives pursued" by its technical regulation. Therefore, a period of "not less than six months" cannot be considered to be a "reasonable interval", within the meaning of Article 2.12, if this period would be ineffective to fulfil the legitimate objectives pursued by the technical regulation at issue.

⁴⁸²In *US – Wool Shirts and Blouses*, the Appellate Body outlined the general rules on burden of proof by stating that:

... the burden of proof rests upon the party, whether complaining or defending, who asserts the affirmative of a particular claim or defence. If that party adduces evidence sufficient to raise a presumption that what is claimed is true, the burden then shifts to the other party, who will fail unless it adduces sufficient evidence to rebut the presumption.

(Appellate Body Report, *US – Wool Shirts and Blouses*, p. 14, DSR 1997:1, 323, at 335)

⁴⁸³Appellate Body Report, *US – Wool Shirts and Blouses*, p. 14, DSR 1997:1, 323, at 335.

283. Thus, in the light of the above, we consider that, in order to rebut a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement*, a responding Member that has allowed an interval of less than six months between the publication and entry into force of its technical regulation must submit evidence and argument sufficient to establish *either*: (i) that the "urgent circumstances" referred to in Article 2.10 of the *TBT Agreement* surrounded the adoption of the technical regulation at issue; (ii) that producers of the complaining Member could have adapted to the requirements of the technical regulation at issue within the shorter interval that it allowed; *or* (iii) that a period of "not less than" six months would be ineffective to fulfil the legitimate objectives of its technical regulation.

284. The Panel found that Indonesia had made a *prima facie* case that "allowing at least six months between the date of publication of Section 907(a)(1)(A) and its entry into force would not render the fulfilment of the objective pursued by Section 907(a)(1)(A) ineffective."⁴⁸⁴ Thus, in the Panel's view, the burden was on Indonesia to establish a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement* that included establishing that a period of at least six months between the publication of Section 907(a)(1)(A) and its entry into force would not render the fulfilment of the objective pursued by Section 907(a)(1)(A) ineffective. The United States argues that Indonesia failed to establish such a *prima facie* case. Relying on the Appellate Body's ruling on the burden of proof under Article 2.4 of the *TBT Agreement* in *EC – Sardines*, the United States argues on appeal that the burden rests with the complaining Member to adduce sufficient evidence and argument to establish that an interval of not less than six months would be effective in fulfilling the objectives of the technical regulation at issue.⁴⁸⁵

285. In *EC – Sardines*, the Appellate Body was considering the allocation of the burden of proof in the context of a claim of inconsistency with Article 2.4 of the *TBT Agreement*. As we see it, the fact that two provisions manifest a degree of structural similarity does not, *necessarily*, support a conclusion that the allocation of the burden of proof in respect of each provision must be identical.⁴⁸⁶

286. We recall our view expressed above that the elements of a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement* are to be drawn from a proper interpretation of Article 2.12, taking into account—pursuant to Article 31(3)(a) of the *Vienna Convention*—the interpretative clarification provided by the terms of paragraph 5.2 of the Doha Ministerial Decision. In much the

⁴⁸⁴Panel Report, para. 7.592.

⁴⁸⁵United States' appellant's submission, para. 143 (referring to Appellate Body Report, *EC – Sardines*, para. 288).

⁴⁸⁶We are not saying that the fact that the burden of proof is allocated in a particular manner with respect to a particular provision of the covered agreements is not a relevant consideration in discerning how the burden of proof is allocated under a similar provision of the covered agreements. Rather, we are saying that the conceptual or structural similarity between two provisions does not, by itself, necessitate a conclusion that the burden of proof in respect of both provisions must be allocated in an identical manner.

same way, the manner in which the burden of proof is allocated under Article 2.12 of the *TBT Agreement* must be informed by an interpretation that properly canvasses the text, context, and object and purpose of Article 2.12. In our view, the burden of proof in respect of a particular provision of the covered agreements *cannot* be understood in isolation from the overarching logic of that provision, and the function which it is designed to serve. On the contrary, it is by having regard for the function and rationale of a particular provision that an adjudicator can, adequately, assess the manner in which the burden of proof should be allocated under that provision.

287. We recall that Article 2.12 of the *TBT Agreement* explains that the reason for allowing an interval between the publication and the entry into force of a technical regulation is "to allow time for producers in exporting Members, and particularly in developing country Members, to adapt their products or methods of production" to the requirements of the importing Member's technical regulation. By its own terms, Article 2.12 singles out producers in exporting Members, and particularly in developing country Members, as the beneficiaries of a "reasonable interval" between the publication and the entry into force of an importing Member's technical regulation. Thus, the concept of a "reasonable interval" within the meaning of Article 2.12 is meant to provide a degree of certainty to producers in exporting Members, and particularly in developing country Members, with regard to the time within which an importing Member's technical regulation can reasonably be expected to enter into force.

288. Paragraph 5.2 of the Doha Ministerial Decision provides interpretative clarification of the concept of a "reasonable interval" within the meaning of Article 2.12 by establishing a rule that producers in exporting Members require a period of at least six months to adapt their products or production methods to the requirements of the importing Member's technical regulation. Thus, paragraph 5.2 enhances the degree of certainty that the concept of a "reasonable interval" is meant to provide to producers in exporting Members, and particularly in developing country Members, with regard to the time within which an importing Member's technical regulation can reasonably be expected to enter into force.

289. The rule in Article 2.12, as clarified by paragraph 5.2 of the Doha Ministerial Decision, is expressly designed to allow producers in the complaining Member, and in particular in a complaining developing country Member, sufficient time to adapt their products or production methods to the requirements of the responding Member's technical regulation. Thus, it seems to us that, where a responding Member seeks to deviate from this rule, which, by its own terms, singles out producers in the complaining Member as the beneficiaries of a "reasonable interval" between the publication and the entry into force of a technical regulation, the responding Member must shoulder the burden of establishing a *prima facie* case that the conditions under which derogations from the rule are

permitted are extant. Thus, we disagree with the Panel that it was for Indonesia to establish a *prima facie* case that a period of at least six months between the publication of Section 907(a)(1)(A) and its entry into force would not render the fulfilment of the objective pursued by Section 907(a)(1)(A) ineffective. Instead, we consider that, under Article 2.12 of the *TBT Agreement*, as clarified by paragraph 5.2 of the Doha Ministerial Decision, the burden rests upon the responding Member to make a *prima facie* case that an interval of not less than six months "would be ineffective to fulfil the legitimate objectives pursued" by its technical regulation.

290. In sum, under Article 2.12 of the *TBT Agreement*, as clarified by paragraph 5.2 of the Doha Ministerial Decision, a complaining Member is required to establish a *prima facie* case that the responding Member has failed to allow for a period of at least six months between the publication and the entry into force of the technical regulation at issue. If the complaining Member establishes such a *prima facie* case, the burden rests on the responding Member that has allowed for an interval of less than six months between the publication and the entry into force of its technical regulation to establish *either*: (i) that the "urgent circumstances" referred to in Article 2.10 of the *TBT Agreement* surrounded the adoption of the technical regulation at issue; (ii) that producers of the complaining Member could have adapted to the requirements of the technical regulation at issue within the shorter interval that it allowed; *or* (iii) that a period of "not less than" six months would be ineffective to fulfil the legitimate objectives of its technical regulation.

291. In order to establish a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement*, Indonesia was required to establish that the United States did not allow an interval of at least six months between the publication and the entry into force of the technical regulation at issue. In this connection, we note the Panel's finding that the actual interval allowed by the United States between the publication and the entry into force of Section 907(a)(1)(A) was a "90-day period or a three-month period".⁴⁸⁷ Thus, we agree with the Panel that Indonesia established a *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement*.

292. In order to rebut the *prima facie* case of inconsistency with Article 2.12 of the *TBT Agreement* made by Indonesia, the United States was required to submit evidence and argument sufficient to establish *either*: (i) that the "urgent circumstances" referred to in Article 2.10 of the *TBT Agreement* surrounded the adoption of Section 907(a)(1)(A); (ii) that producers in Indonesia could have adapted to the requirements of Section 907(a)(1)(A) within a three-month interval; *or* (iii) that a period of "not less than" six months would be ineffective to fulfil the legitimate objectives of Section 907(a)(1)(A).

⁴⁸⁷Panel Report, para. 7.567.

293. With regard to whether the "urgent circumstances" referred to in Article 2.10 of the *TBT Agreement* surrounded the adoption of Section 907(a)(1)(A), we note that the Panel found that "[i]n the absence of any evidence or argument that such urgent problems of safety, health, environmental protection or national security arose or threatened to arise upon adoption of Section 907(a)(1)(A)", it could "only conclude that these urgent circumstances were not present".⁴⁸⁸ Thus, the United States did not contend that the "urgent circumstances" referred to in Article 2.10 surrounded the adoption of Section 907(a)(1)(A).

294. With regard to the question of whether producers in Indonesia could have adapted to the requirements of Section 907(a)(1)(A) within a three-month period, the United States argued before the Panel that "Indonesian producers have been and are able to market tobacco-flavoured and menthol-flavoured cigarettes in the United States' market", and that "Indonesian producers, even 16 months after the enactment of [Section 907(a)(1)(A)] have not adjusted their product lines to produce tobacco or menthol-flavoured cigarettes."⁴⁸⁹ Thus, according to the United States, whether it waited "three months or six months after the measure's enactment to allow it to enter into force appears not to have affected Indonesia producers in any way".⁴⁹⁰ On appeal, the United States submits that "[t]his evidence and argument" was sufficient to rebut the *prima facie* case that the Panel found Indonesia to have established.⁴⁹¹ We are not persuaded that the evidence and argument submitted by the United States before the Panel was sufficient to establish that producers in Indonesia could have adapted to the requirements of Section 907(a)(1)(A) within a three-month period. Contrary to what the United States argues, the fact that Indonesian producers had not adjusted to the requirements of Section 907(a)(1)(A) sixteen months after its entry into force is evidence that points in the direction of Indonesian producers requiring a significantly longer period than the three months allowed by the United States. Thus, the United States failed to establish that producers in Indonesia could have adapted to the requirements of Section 907(a)(1)(A) within a three-month period.

295. We turn now to consider whether the United States established, with sufficient evidence and argument, that a period of at least six months between the publication and the entry into force of Section 907(a)(1)(A) would be ineffective in fulfilling the legitimate objective pursued by Section 907(a)(1)(A). We note that the Panel stated that the United States had not explained "why it deemed that allowing a 90 day/three month interval between the publication and entry into force of Section 907(a)(1)(A) was not ineffective in fulfilling the objective pursued by Section 907(a)(1)(A), while a six month interval would be".⁴⁹² Before the Panel, the United States argued that the

⁴⁸⁸Panel Report, para. 7.507.

⁴⁸⁹Panel Report, para. 7.583 (referring to United States' first written submission to the Panel, para. 303).

⁴⁹⁰Panel Report, para. 7.583.

⁴⁹¹United States' appellant's submission, para. 153.

⁴⁹²Panel Report, para. 7.593.

FSPTCA "directly addresses a serious problem—youth smoking" and that "Congress intended to limit this behaviour as much as practicable".⁴⁹³ While the arguments advanced by the United States before the Panel identify the legitimate objective of Section 907(a)(1)(A), these arguments are insufficient to establish that allowing a period of not less than six months between the publication and entry into force of Section 907(a)(1)(A) would have been ineffective to fulfil the legitimate objective of Section 907(a)(1)(A).

296. Thus, while we disagree with the Panel that it was for Indonesia to establish a *prima facie* case that an interval of at least six months between the publication of the FSPTCA and the entry into force of Section 907(a)(1)(A) would not render the fulfilment of the objective pursued by Section 907(a)(1)(A) ineffective, we nevertheless share the Panel's view that the United States failed to establish that an interval of at least six months between publication and entry into force would be ineffective in fulfilling the legitimate objective pursued by Section 907(a)(1)(A). Accordingly, we agree with the Panel that the United States failed to rebut the *prima facie* case of inconsistency that Indonesia established under Article 2.12 of the *TBT Agreement*.

297. In the light of the foregoing reasons, we *uphold*, albeit for different reasons, the Panel's finding, in paragraphs 7.595 and 8.1(h) of the Panel Report, that, by failing to allow an interval of not less than six months between the publication and the entry into force of Section 907(a)(1)(A) of the FFDCA, the United States acted inconsistently with Article 2.12 of the *TBT Agreement*.

VII. Findings and Conclusions

298. For the reasons set out in this Report, the Appellate Body:

- (a) With respect to Article 2.1 of the *TBT Agreement*:
 - (i) upholds, albeit for different reasons, the Panel's finding, in paragraph 7.248 of the Panel Report, that clove cigarettes and menthol cigarettes are "like products" within the meaning of Article 2.1 of the *TBT Agreement*;
 - (ii) finds that the Panel did not act inconsistently with Article 11 of the DSU in its analysis of consumer tastes and habits;
 - (iii) upholds, albeit for different reasons, the Panel's finding, in paragraph 7.292 of the Panel Report, that, by banning clove cigarettes while exempting menthol cigarettes from the ban, Section 907(a)(1)(A) of the FFDCA accords imported clove cigarettes less favourable treatment than that accorded to

⁴⁹³Panel Report, para. 7.588 (referring to United States' first written submission to the Panel, para. 302).

domestic menthol cigarettes, within the meaning of Article 2.1 of the *TBT Agreement*;

- (iv) finds that the Panel did not act inconsistently with Article 11 of the DSU in its less favourable treatment analysis; and, therefore,
- (v) upholds, albeit for different reasons, the Panel's finding, in paragraphs 7.293 and 8.1(b) of the Panel Report, that Section 907(a)(1)(A) of the FFDCA is inconsistent with Article 2.1 of the *TBT Agreement* because it accords to imported clove cigarettes less favourable treatment than that accorded to like menthol cigarettes of national origin; and
- (b) With respect to Article 2.12 of the *TBT Agreement*:
 - (i) upholds the Panel's finding, in paragraph 7.576 of the Panel Report, that paragraph 5.2 of the Doha Ministerial Decision constitutes a subsequent agreement between the parties, within the meaning of Article 31(3)(a) of the *Vienna Convention*, on the interpretation of the term "reasonable interval" in Article 2.12 of the *TBT Agreement*; and
 - (ii) upholds, albeit for different reasons, the Panel's finding, in paragraphs 7.595 and 8.1(h) of the Panel Report, that, by failing to allow an interval of not less than six months between the publication and the entry into force of Section 907(a)(1)(A) of the FFDCA, the United States acted inconsistently with Article 2.12 of the *TBT Agreement*.

299. The Appellate Body recommends that the DSB request the United States to bring its measure, found in this Report, and in the Panel Report as modified by this Report, to be inconsistent with the *TBT Agreement*, into conformity with its obligations under that Agreement.

Signed in the original in Geneva this 22nd day of March 2012 by:

Shotaro Oshima
Presiding Member

Ricardo Ramirez-Hernández
Member

Peter Van den Bossche
Member

ANNEX I

**WORLD TRADE
ORGANIZATION**

WT/DS406/6
10 January 2012

(12-0103)

Original: English

**UNITED STATES – MEASURES AFFECTING THE PRODUCTION
AND SALE OF CLOVE CIGARETTES**

Notification of an Appeal by the United States
under Article 16.4 and Article 17 of the Understanding on Rules
and Procedures Governing the Settlement of Disputes (DSU)
and under Rule 20(1) of the Working Procedures for Appellate Review

The following notification, dated 5 January 2012, from the Delegation of the United States, is
being circulated to Members.

Pursuant to Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 20 of the *Working Procedures for Appellate Review*, the United States hereby notifies its decision to appeal to the Appellate Body certain issues of law covered in the Report of the Panel in *United States – Measures Affecting the Production and Sale of Clove Cigarettes* (WT/DS406/R) ("Panel Report") and certain legal interpretations developed by the Panel.

1. The United States seeks review of the Panel's conclusion that Section 907(a)(1)(A) of the Family Smoking Prevention and Tobacco Control Act (the "Tobacco Control Act"),¹ is inconsistent with Article 2.1 of the *Agreement on Technical Barriers to Trade* (the "TBT Agreement").² The United States appeals this finding based on a series of erroneous legal interpretations developed by the Panel, and on failure by the Panel to make an objective assessment of the facts of the case as called for by Article 11 of the DSU.

2. The United States seeks review of the Panel's finding that clove cigarettes and menthol cigarettes are like products.³ In making this erroneous finding, the Panel erred in its legal interpretation of Article 2.1 by excluding, *a priori*, evidence related to particular criteria and failing to analyze each criteria completely.⁴ Specifically the Panel erred by failing to perform a complete analysis of the end-uses⁵ of clove cigarettes and menthol cigarettes and failing to perform a complete

¹The Tobacco Control Act was adopted June 2009 and it went into effect September 2009 as an amendment to the Federal Food, Drug and Cosmetic Act, 21 U.S.C. §387g(a)(1)(A).
²*See, e.g.*, Panel Report, paras. 7.293, 8.1(b).
³*See, e.g.*, Panel Report, para. 7.248.
⁴*See, e.g.*, Panel Report, paras. 7.116, 7.119, 7.197-199, 7.206, 7.209-210, 7.214, 7.230-231.
⁵*See, e.g.*, Panel Report, paras. 7.197-199.

analysis of consumer tastes and habits.⁶ In developing this faulty legal interpretation, the Panel also acted inconsistently with Article 11 of the DSU by failing to make an objective assessment of the facts in the case by refusing to consider certain evidence related consumer tastes and habits.⁷

3. The United States also seeks review of the Panel's finding that Section 907(a)(1)(A) accords less favorable treatment to imported clove cigarettes.⁸ In making this finding, the Panel erred in its legal interpretations that the only products to be compared are imported clove cigarettes and domestic menthol cigarettes,⁹ and that the effect of Section 907(a)(1)(A) on U.S. production can be assessed by looking only at what products were on the market at the time the measure went into effect.¹⁰ The Panel also erred by applying an incorrect legal framework to assess whether the alleged detriment to the competitive conditions for clove cigarettes could be explained by factors or circumstances unrelated to the foreign origin of the products.¹¹ In developing these faulty legal interpretations, the Panel also acted inconsistently with Article 11 of the DSU by failing to make an objective assessment of the facts of the case in finding that at the time of the ban, there were no domestic cigarettes with characterizing flavors other than menthol cigarettes,¹² and that Section 907(a)(1)(A) imposes no costs on any U.S. entity.¹³

4. The United States seeks review by the Appellate Body of the Panel's conclusion and related findings that by not allowing an interval of no less than six months between the publication and the entry into force of Section 907(a)(1)(A), the United States acted inconsistently with Article 2.12 of the TBT Agreement.¹⁴ This conclusion is in error and is based on erroneous findings on issues of law and legal interpretations with respect to Article 2.12 of the TBT Agreement.¹⁵

5. Finally, the United States also makes a conditional appeal regarding the Panel's legal analysis with respect to Indonesia's claims under Article 2.2 of the TBT Agreement. Should Indonesia seek review by the Appellate Body of the Panel's findings with respect to Indonesia's claims under Article 2.2, the United States seeks review by the Appellate Body of the Panel's finding that it could draw upon jurisprudence developed under Article XX(b) of the *General Agreement on Tariffs and Trade 1994* when assessing the consistency of Section 907(a)(1)(A) with the requirement that technical regulations "not be more trade-restrictive than necessary to fulfill a legitimate objective . . .".¹⁶ While the United States agrees with the ultimate conclusion in the Panel Report regarding Indonesia's claims under Article 2.2 of the TBT Agreement, the United States considers the Panel's analysis on this particular aspect to be based on erroneous findings on issues of law and related legal interpretations with respect to Article 2.2 of the TBT Agreement.

⁶*See, e.g.*, Panel Report, paras. 7.116, 7.119, 7.206-7.232.

⁷*See, e.g.*, Panel Report, para. 7.210.

⁸*See, e.g.*, Panel Report, para. 7.292.

⁹*See, e.g.*, Panel Report, paras. 7.274, 7.277.

¹⁰*See, e.g.*, Panel Report, para. 7.289.

¹¹*See, e.g.*, Panel Report, paras. 7.269, 7.286-7.291.

¹²*See, e.g.*, Panel Report, para. 7.289.

¹³*See, e.g.*, Panel Report, para. 7.289.

¹⁴*See, e.g.*, Panel Report, paras. 7.595, 8.1(h).

¹⁵*See, e.g.*, Panel Report, paras. 7.561-7.595.

¹⁶Panel Report, paras. 7.351-7.369.