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DISPUTE SETTLEMENT

WORLD TRADE ORGANIZATION

3.5 GATT 1994

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NOTE

The **Course on Dispute Settlement in International Trade, Investment and Intellectual Property** consists of forty modules.

This module has been prepared by Mrs. Stéphanie Cartier at the request of the United Nations Conference on Trade and Development (UNCTAD). The views and opinions expressed in this module are those of the author and not necessarily those of the United Nations, WTO, WIPO, ICSID, UNCITRAL or the Advisory Centre on WTO Law.

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TABLE OF CONTENTS

WHAT YOU WILL LEARN

The GATT 1947 is at the very source of the current WTO system. Its basic principles applicable to trade in goods have been incorporated into other WTO agreements dealing with other areas of trade, such as trade in services and trade in intellectual property products and, it also provided the very first dispute settlement provisions upon which the WTO dispute settlement system is built. Although the GATT 1994 is only one of the numerous WTO "goods" agreements, its importance in the history of the GATT/WTO is undisputable. This Module provides an overview of the obligations relating to trade in goods in the GATT 1994.

The first Section of this Module defines the GATT 1994 and its constituent elements. The first Section also circumscribes the scope of application of the GATT 1994, and examines its relationship with other WTO agreements.

The second Section discusses the cornerstone of the entire multilateral trading system, the principle of non-discrimination in the GATT 1994, and explores its two facets: the most-favoured-nation treatment obligation and the national treatment obligation.

The third Section addresses the market access barriers to trade in goods and presents the obligations relating to the publication and administration of trade regulations.

The fourth Section deals with the exceptions to the disciplines of the GATT 1994, namely, the general exceptions, the security exceptions, and the exceptions for the purposes of applying safeguard measures, balance-of-payments restrictions, and for the purpose of carrying out regional trade agreements.

Finally, the Fifth Section analyses the position of developing country Members under the GATT 1994.

1. GATT 1994: TRADE IN GOODS

After completing this Section, the reader will be able to:

- **define the GATT 1994 and its scope of application;**
- **list the constituent elements of the GATT 1994:**
- **explain the relationship between the GATT 1994 and other WTO agreements.**

1.1 What Does "GATT" Mean?

GATT

The acronym "GATT" stands for the "General Agreement on Tariffs and Trade". It is an agreement between States aiming at eliminating discrimination and reducing tariffs and other trade barriers with respect to trade in goods.

Trade in Goods

The GATT was originally, and is still today, only concerned with trade in goods, although its main principles now also apply to trade in services, and intellectual property rights as dealt with respectively by the *General Agreement on Trade in Services* and the *TRIPS Agreement.* The GATT is a WTO agreement that deals exclusively with trade in goods, but it is not the only one. All the agreements listed in Annex 1A to the *Marrakesh Agreement Establishing the World Trade Organization* (hereinafter the "*WTO Agreement*") concern particular aspects or sectors of trade in goods.

The WTO " Goods " Agreements

The so-called WTO "goods agreements" in Annex 1A to the *WTO Agreement* consist of [1]:

WTO Agreement

ANNEX 1

ANNEX 1A: Multilateral Agreements on Trade in Goods

GATT 1994

- *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 (also known as the* Anti-Dumping Agreement*)*
- *Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994 (also known as the* Agreement on Customs Valuation*)*

→

[1] *Please refer to Module 3.1, Section 1.1. Several of these agreements are dealt with in separate Modules of this course.*

Agreement on Preshipment Inspection
Agreement on Rules of Origin
Agreement on Import Licensing Procedures
Agreement on Subsidies and Countervailing Measures
Agreement on Safeguards

GATT 1947

The GATT was concluded in 1947 and is now referred to as the GATT 1947. The GATT 1947 was last amended, last in 1965. Later on, additional disciplines were agreed to in side agreements, such as the Tokyo Round agreements, which did not amend the GATT 1947 as such, but only bound the GATT Contracting Parties that became a party to these side agreements.[2] The GATT 1947 was terminated in 1996. However, the provisions of the GATT 1947 as well as all legal instruments concluded under the GATT 1947 are integrated into the GATT 1994, subject to clarifications brought about by Understandings which also form integral parts of the GATT 1994.

Terminology

The acronym "GATT" is sometimes confusingly used to describe a number of different things. It is sometimes referred to as the "GATT disciplines", or "GATT disputes", to mean the current WTO obligations or disputes relating to trade in goods. However, it may also be referred to as the "GATT" to mean the old multilateral trading system and/or Secretariat preceding the WTO. In this Module, "GATT" only means the current obligations under the GATT 1994.

1.2 Scope of Application of the GATT 1994

A WTO agreement

The GATT 1994 is one of the multilateral agreements annexed to the *WTO Agreement*. It is an international treaty binding upon all WTO Members.

Scope of Application

The GATT 1994 is only concerned with trade in goods. The GATT 1994 aims at further liberalizing trade in goods through the reduction of tariffs and other trade barriers and eliminating discrimination.

GATT 1994 vs. GATS

In *EC – Bananas III*, the question arose whether the *General Agreement on Trade in Services* (hereinafter the "GATS") and the GATT 1994 were mutually exclusive agreements. The Appellate Body said:

... The GATS was not intended to deal with the same subject matter as the GATT 1994. The GATS was intended to deal with a subject matter not covered by the GATT 1994, that is, with trade in services. Thus, the GATS applies to the supply of services. It provides, inter alia, for both MFN treatment and national treatment for services and service suppliers. Given the respective scope of application of the two agreements, they may or may not overlap, depending on the nature of the measures at issue. Certain measures could be →

[2] *For more information on the history of the GATT, please refer to Module 3.1, Section 1.1.*

found to fall exclusively within the scope of the GATT 1994, when they affect trade in goods as goods. Certain measures could be found to fall exclusively within the scope of the GATS, when they affect the supply of services as services. There is yet a third category of measures that could be found to fall within the scope of both the GATT 1994 and the GATS. These are measures that involve a service relating to a particular good or a service supplied in conjunction with a particular good. In all such cases in this third category, the measure in question could be scrutinized under both the GATT 1994 and the GATS. However, while the same measure could be scrutinized under both agreements, the specific aspects of that measure examined under each agreement could be different. Under the GATT 1994, the focus is on how the measure affects the goods involved. Under the GATS, the focus is on how the measure affects the supply of the service or the service suppliers involved. Whether a certain measure affecting the supply of a service related to a particular good is scrutinized under the GATT 1994 or the GATS, or both, is a matter that can only be determined on a case-by-case basis.[3]

1.3 Structure of the GATT 1994

Constituent Elements

The GATT 1994 is a bizarre agreement. It "assembles" legal provisions from different sources. It consists of the provisions of the GATT 1947, of legal instruments concluded under the GATT 1947, of Understandings concluded during the Uruguay Round on the interpretation of the provision of the GATT 1947, and of the Marrakesh Protocol of Tariff Concessions.

AGREEMENT ESTABLISHING THE WORLD TRADE ORGANIZATION

ANNEX 1

ANNEX 1A: Multilateral Agreements on Trade in Goods

GATT 1994:

- ***Provisions of the GATT 1947***
- ***Provisions of Legal Instruments*** *concluded under the GATT 1947:*
  - *protocols and certifications relating to tariff concessions;*
  - *protocols of accession;*
  - *waivers granted under Article XXV of the GATT 1947 and still in force on the date of entry into force;*
  - *other decisions of the CONTRACTING PARTIES to the GATT 1947.*
- ***Understandings*** *concluded during the Uruguay Round on the interpretation of certain provisions of the GATT 1947*
- ***Marrakesh Protocol to the GATT 1994***

[3] *Appellate Body Report,* European Communities – *Regime for the Importation, Sale and Distribution of Bananas ("EC – Bananas III"), WT/DS27/AB/R, adopted 25 September 1997, DSR 1997:II, 591, para. 221.*

The GATT 1994 incorporates *as is* the provisions of the GATT 1947, and yet, it clarifies the nature and extent of some obligations set out in the GATT 1947 through the so-called "Understandings" and other legal instruments, including "other decisions" of the Contracting Parties to the GATT, which also form part of the GATT 1994. Furthermore, it changes the wording to be used when referring to the provisions of the GATT 1947. For instance, the phrase "Contracting Parties" in the GATT 1947 is now deemed to read "Members". In particular, the "Explanatory Notes" of Paragraph 2 stipulate:

> 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".*

1.4 Provisions of the GATT 1994

Para. 1(a) GATT 1994

Paragraph 1(a) of the language incorporating the GATT 1994 into the *WTO Agreement* provides that:

> *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; ...*

The provisions of the GATT 1947, now the provisions of the GATT 1994, consist of 38 articles – numbered in roman digits – which are split up into four "parts".

Part I

Part I of the GATT 1994 contains Articles I, enshrining the most-favoured-nation treatment obligation, and Article II, setting out the obligations applicable to the Schedules of Concessions of each WTO Member.

Part II

Part II of the GATT 1994 comprises Articles III through XXIII. Article III establishes the national treatment obligation. Articles IV to Article XIX cover mainly non-tariff measures, such as unfair trade practices (dumping and export subsidies), quantitative restrictions, restrictions for balance-of-payments reasons, state-trading enterprises, government assistance to economic development, and emergency safeguards measures. In addition, this Part also

deals with numerous technical issues relating to the application of border measures. Articles XX and XXI deal with the possible exceptions to the GATT 1994, namely the general exceptions and those for security reasons. Articles XXII and XXIII provide for dispute settlement procedures, which are further elaborated in the *Understanding on the Principles Governing the Settlement of Disputes* (hereinafter the "DSU").

Part III

Part III of the GATT 1994 consists of Article XXIV through Article XXXV. Article XXIV concerns mainly customs unions and free trade areas and the responsibility of Members for the acts of their regional and local governments. Articles XXVIII and XXVIII(bis) deal with the negotiation and renegotiation of tariff concessions.

Part IV

Finally, Part IV of the GATT 1994 is entitled "*Trade and Development*" and aims to increase trade opportunities for developing country Members in various ways.

Other Provisions

The provisions that deal with the entry into force, accession, amendments, withdrawal, non-application and joint action are no longer valid because they have been superseded by the relevant provisions of the *WTO Agreement*.

1.5 Legal Instruments Adopted under the GATT 1947

Para. 1(b) GATT 1994

Paragraph 1(b) of the language incorporating the GATT 1994 into the *WTO Agreement* provides the following:

> *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:*
>
> *(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 Agreement;*
>
> *(iv) other decisions of the CONTRACTING PARTIES to GATT 1947; ...*

The effect of incorporating by reference the provisions of these legal instruments into the GATT 1994 is to maintain their prior status under the GATT 1947,

and to bind all WTO Members.

In *US – FSC*, the Appellate Body said: :

> *... The inclusion of these "legal instruments" in the GATT 1994 recognizes that the legal character of the rights and obligations of the contracting parties under the GATT 1994 is not fully reflected by the text of the GATT 1994 because those rights and obligations are conditioned by the "protocols", "decisions" and other "legal instruments" to which paragraph 1(b) refers.*[4]

In *Japan – Alcoholic Beverages II*, the Appellate Body stated that not every decision of the Contracting Parties to the GATT 1947 constituted an "other decision" within the meaning of paragraph 1(b)(iv) of the language incorporating the GATT 1994 into the WTO Agreement.[5] In that case, the Appellate Body concluded that adopted panel reports do not constitute such "other decisions".[6] In *US – FSC*, the Appellate Body confirmed the Panel's finding that "other decisions" did not include a Council action adopting a panel report as a result of the parties' agreement.[7]

1.6 Understandings and the Marrakesh Protocol

Paras. 1(c) and 1(d) GATT 1994

Paragraphs 1(c) and 1(d) of the language incorporating the GATT 1994 into the WTO Agreement provide:

> *1. The General Agreement on Tariffs and Trade 1994 ("GATT 1994") shall consist of:*
>
> *...*
>
> *(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;*
>
> →

[4] *Appellate Body Report,* United States – *Tax Treatment for "Foreign Sales Corporations" ("US – FSC"), WT/DS108/AB/R, adopted 20 March 2000, para. 107.*

[5] *Appellate Body Report,* Japan – *Taxes on Alcoholic Beverages ("Japan – Alcoholic Beverages II"), WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, pp. 12-15. See also Appellate Body Report,* US – *FSC, para. 108.*

[6] *Appellate Body Report,* Japan – *Alcoholic Beverages II, pp. 12-15. See also Appellate Body Report,* US – *FSC, para. 108. The Appellate Body reasoned that adopted panel reports "are not binding, except with respect to resolving the particular dispute between the parties to that dispute". The Appellate Body finally said that the decision to adopt a panel report was not intended by the GATT 1947 Contracting Parties to "constitute a definitive interpretation of the relevant provisions of GATT 1947."*

[7] *See also Appellate Body Report,* US – *FSC, paras. 22 and 114. The reasoning of the Appellate Body is set out in paragraphs 107 to 113.*

> *(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.*

Understandings

The six Understandings are legal documents which have been concluded during the Uruguay Round with a view to clarifying some obligations set out in the GATT 1947. They concern six particular GATT provisions, namely, the ones relating to the schedules of concessions, state-trading enterprises, balance-of-payments exceptions, regional trade agreements, waivers and the withdrawal of concessions.

Some of these Understandings aim to introduce further "transparency" obligations, while others seek to refine terms or paragraphs of the concerned GATT article. For instance, the *Understanding on Article II:1(b)* requires that the nature and level of any "other duties or charges" levied on bound tariff items, as referred to in that provision, be recorded in the Schedules of Concessions annexed to GATT 1994 against the tariff item to which they apply. The *Understanding on Article XVII* (on state trading enterprises) sets out notification procedures and provides for subsequent reviews. The *Understanding on Balance-of-Payments Provisions* essentially aims to clarify the existing obligations under the provisions of the GATT 1994, but it also provides for transparency measures and consultation requirements. The *Understanding on Article XXIV* regarding regional trade agreements clarifies some of the subparagraphs to Article XXIV. The *Understanding on Waivers* sets out the elements to include in the request for a waiver and explains when and how it is possible to challenge the application of a waiver by a Member. Finally, the *Understanding on Article XXVIII* (concession withdrawal) defines the phrase "principal supplying interest" of Article XXVIII of the GATT 1994.

Marrakesh Protocol

With respect to the Marrakesh Protocol to the GATT 1994, it is the legal instrument that incorporates the Schedules of Concessions and Commitments on Goods negotiated under the Uruguay Round into the GATT 1994. It confirms their authenticity and sets out their implementation modalities.

1.7 The Relationship Between the GATT 1994 and Other WTO Agreements

The provisions of the GATT 1994 apply to a disputed measure even where the provisions of other WTO agreements are applicable, to the extent that the provisions of the GATT 1994 do not conflict with any of the provisions of the other applicable WTO agreements. In other words, if there is no conflict, the measure at issue should be examined against all the relevant provisions of the

different WTO agreements, including the GATT 1994.

The Appellate Body defined the term "conflict" in *Guatemala – Cement I*.[8] There is a conflict when adherence to one provision will lead to a violation of another provision. Following the terms of the Appellate Body, an interpreter must identify an inconsistency or a difference between the provisions examined before determining which one of the provisions will prevail.[9]

In the event of a conflict, and to the extent of that conflict, the GATT 1994 never prevails. The other WTO agreements on trade in goods contained in Annex 1A to the *WTO Agreement* always prevail over the GATT 1994. Moreover, the *WTO Agreement* always prevails over any of the multilateral trade agreements, including the GATT 1994 and all the other agreements on trade in goods included in Annex 1A to the *WTO Agreement*.

1.7.1 The Relationship Between the GATT 1994 and the *WTO Agreement*

Article XVI:3 WTO

The relationship between the GATT 1994 and the *WTO Agreement* is regulated by Article XVI:3 of the *WTO Agreement*, which provides:

> *In the event of a conflict between a provision of th[e WTO] Agreement and a provision of any of the Multilateral Trade Agreements, the provision of th[e WTO] Agreement shall prevail to the extent of the conflict.*

1.7.2 The Relationship Between the GATT 1994 and Other Agreements in Annex 1A to the *WTO Agreement*

General Interpretative Note to Annex 1A

Annex 1A to the *WTO Agreement*, which includes all multilateral agreements on trade in goods, is introduced by a "General interpretative note" giving prevalence to the other agreements on trade in goods over the GATT 1994 in the event of a conflict, and to the extent of that conflict.

> ***General interpretative note to Annex 1A***
>
> *In the event of a conflict between a provision of the [GATT 1994] and a provision of another agreement in Annex 1A to the [WTO Agreement], the provision of the other agreement shall prevail to the extent of the conflict.*

A number of disputes have raised the issue of conflict between the GATT 1994 and other multilateral agreements on trade in goods in Annex 1A to the

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[8] *Appellate Body Report,* Guatemala – *Anti-Dumping Investigation Regarding Portland Cement from Mexico ("Guatemala – Cement I"), WT/DS60/AB/R, adopted 25 November 1998, para. 65. Although in that case, the alleged conflicting provisions came from the DSU and the* Anti-Dumping Agreement, *the Appellate Body's analysis is relevant to the determination of whether there is a "conflict" between GATT provisions and provisions from other WTO agreements.*

[9] *Appellate Body Report,* Guatemala – *Cement I, para. 65.*

WTO Agreement.[10] Provided that there is no conflict between the GATT 1994 and the other goods agreement, the measure at issue should be examined against both the provisions of the GATT 1994 and the provisions of the other goods agreement.

1.8 Test Your Understanding

1. **What is the difference between the GATT 1994 and the GATT 1947? Does the GATT 1994 apply to trade in services?**
2. **What are the constituent elements of the GATT 1994?**
3. **How does an interpreter determine whether there is a conflict between the provisions of the GATT 1994 and the provisions of other WTO Agreements? In the event of a conflict between provisions of the GATT 1994 and those of other *WTO Agreements*, which provisions prevail?**

[10] *See, for instance, Appellate Body Report,* EC *– Bananas III, para. 155; Appellate Body Report, Argentina – Safeguard Measures on Imports of Footwear ("Argentina – Footwear (EC)"), WT/DS121/AB/R, adopted 12 January 2000, paras. 81 et 83; and Appellate Body Report, Brazil – Measures Affecting Desiccated Coconut ("Brazil – Desiccated Coconut"), WT/DS22/AB/R, adopted 20 March 1997, p. 16.*

2. THE PRINCIPLE OF NON-DISCRIMINATION IN THE GATT 1994

After completing this Section, the reader will be able to:

- **explain the non-discrimination principle in international trade law;**
- **distinguish between the most-favoured-nation treatment obligation and the national treatment obligation;**
- **identify and compare the elements of the most-favoured-nation treatment obligation and of those national treatment obligations.**

2.1 Non-Discrimination: Definition

Non-Discrimination

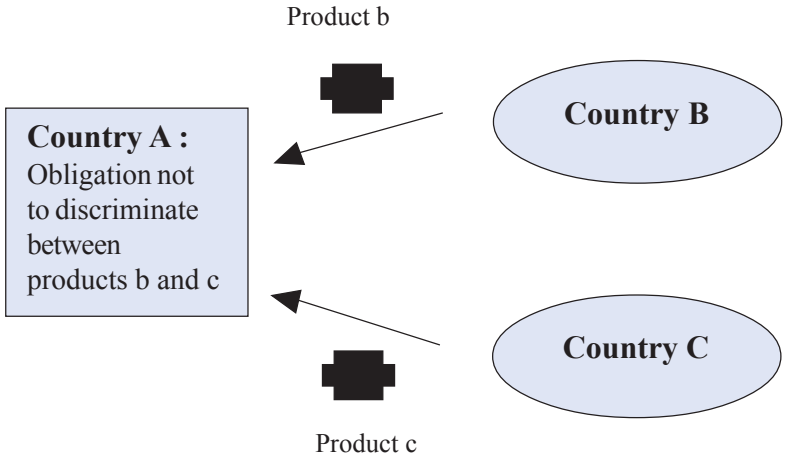
The principle of non-discrimination, or, in other words, the requirement not to treat less favourably all "like" products, irrespective of their origin or whether they are imported or domestic, is the cornerstone of the WTO multilateral trading system. The non-discrimination obligation contributes to ensuring fair and predictable international trade relations.

The principle of non-discrimination in international trade is two-faceted: it consists of the most-favoured-nation treatment obligation and the national treatment obligation.

2.2 Most-Favoured-Nation Treatment Obligation: Article I:1

MFN Treatment Obligation

The most-favoured-nation treatment obligation, widely known as the MFN treatment obligation, requires WTO Members not to discriminate *between* products originating in or destined for different countries. In simple terms, Country A should, for example, treat equally, or not discriminate *between* a product originating in Country B and a "like" product originating in Country C.



Article I:1 GATT 1994

More particularly, Article I:1 of the GATT 1994 provides:

> ***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 [Member] 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 [Members].***

Objective

The objective of the MFN treatment obligation is to ensure equality of opportunity to import from or to export to all WTO Members.

2.3 When is There a Violation of the Most-Favoured-Nation Treatment Obligation?

Three-Tier Test

Article I:1 of the GATT 1994 sets out a three-tier test. In order to determine whether or not there is a violation of the MFN treatment obligation of Article I:1, three questions need to be answered. First, does the measure at issue confer an "advantage" upon the products originating in or destined for the territories of all other Members? Second, are the products concerned "like"? Third, was the advantage at issue granted "immediately and unconditionally" to all like products concerned?

2.3.1 Has an "advantage" been conferred upon imported or exported products?

The MFN treatment obligation concerns any advantage granted by any Member to any product originating in or destined for any other country through a variety of measures. The obligation to provide MFN treatment is not confined to tariffs. Article I:1 of the GATT 1994 enumerates measures by which an "advantage" can be conferred upon the products of a country. They include:

- tariffs and charges of any kind imposed in connection with importation and exportation;
- the method of levying tariffs and such charges;
- rules and formalities in connection with importation and exportation;
- internal taxes and charges on imported goods;
- internal laws, regulations and requirements affecting sales.

"any other country"

It is important to emphasize that the MFN treatment obligation not only takes into consideration advantages conferred upon products originating in or destined for WTO Members, but also advantages granted to "any other country". Therefore, if a WTO Member grants an advantage to products originating in or destined for a non-Member, the Member is compelled to grant the same advantage to all other WTO Members.

"advantage"

A broad definition is usually given to the term "advantage", and Article I:1 of the GATT 1994 covers a wide variety of measures.[11] In particular, it includes the rules and formalities applicable to countervailing duties, and those applicable to the revocation of countervailing duty orders as they constitute "rules and formalities imposed in connection with importation", within the meaning of Article I:1.[12] Merchandise processing fees are considered to be "charges imposed on or in connection with importation", within the meaning of Article I:1.[13] Regulations making the suspension of an import levy conditional on the production of a certificate of authenticity also fall under Article I:1.[14]

EC – Bananas III

In *EC – Bananas III* , the European Communities maintained the so-called "activity function rules" which imposed requirements on importers of bananas from certain countries to qualify for tariff quotas that differed from those imposed on importers of bananas from other countries. The Panel found that the procedural and administrative requirements of the "activity function rules" for importing third-country and non-traditional ACP bananas differed from and went significantly beyond those required for importing traditional ACP bananas.[15] The Appellate Body, relying on the Panel's factual analysis, concluded that the European Communities had acted inconsistently with Article I:1 of the GATT 1994 through its "activity function rules" because they conferred an advantage upon bananas imported from a group of States (ACP States), and not upon bananas imported from other WTO Members, within the meaning of Article I:1.[16]

Canada – Autos

In *Canada – Autos*, Canada maintained an import duty exemption on imports of motor vehicles granted to manufacturers of motor vehicles which met certain requirements related to their production of motor vehicles in Canada. The Appellate Body emphasized that:

> *Article I:1 requires that '*any advantage*, favour, privilege or immunity granted by any Member to* any product *originating in or destined for any other country shall be accorded immediately and unconditionally to the like product* →

[11] *See Panel Report,* United States – *Denial of Most-Favoured-Nation Treatment as to Non-Rubber Footwear from Brazil ("US – Non Rubber Footwear"), adopted 19 June 1992, BISD 39S/128, para. 6.9; Appellate Body Report,* EC – *Bananas III, para. 206.*

[12] *Panel Report,* US – *Non Rubber Footwear, para. 6.8.*

[13] *Panel Report,* United States – *Customs User Fee ("US – Customs User Fee"), adopted 2 February 1988, BISD 35S/245, para. 122.*

[14] *Panel Report,* European Economic Communities – *Imports of Beef from Canada ("EEC – Beef from Canada"), adopted 10 March 1981, BISD 28S/92, paras. 4.2 and 4.3.*

[15] *Appellate Body Report, EC – Bananas III, para. 206.*

[16] *Appellate Body Report, EC – Bananas III, para. 206.*

> *originating in or destined for the territories of* all other Members*.' (emphasis added) The words of Article I:1 refer not to* some *advantages granted 'with respect to' the subjects that fall within the defined scope of the Article, but to '*any advantage*'; not to* some *products, but to '*any product *'; and not to like products from* some *other Members, but to like products originating in or destined for '*all other *' Members.*[17]

2.3.2 Are the products "like"?

Article I:1 of the GATT 1994 provides that an advantage granted to a product originating in or destined for any other country shall be accorded to other "like products" originating in or destined for the territories of all other WTO Members.

The MFN treatment obligation only applies to "like products". Discrimination between imported products is prohibited only if the products at issue are "like". Accordingly, products that are not "like" may be treated differently.

Like Products

The concept of "like products" is also found in numerous other articles of the GATT 1994, namely, Articles II:2(a), III:2, III:4, VI:1(a), IX:1, XI:2(c), XIII:1, XVI:4 and XIX:1. However, the concept of "like products" is not defined anywhere in the GATT 1994. The meaning of this concept has been examined in a number of GATT and WTO reports. It is generally accepted though that the concept of "like products" has different meanings depending on the context in which it is found. In *Japan – Alcoholic Beverages II*, the Appellate Body compared the concept of "likeness" to an accordion:

> *The accordion of 'likeness' stretches and squeezes in different places as different provisions of the* WTO 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.*[18]

Criteria

In *Spain – Unroasted Coffee*, the issue before the Panel was whether different types of unroasted coffee were "like" within the meaning of Article I:1 of the GATT 1994. The Panel considered the characteristics of the products, their end-use and tariff regimes of other Members.[19]

> *The Panel examined all arguments that had been advanced during the proceedings for the justification of a different tariff treatment for various groups and types of unroasted coffee. It noted that these arguments mainly* →

[17] *Appellate Body Report,* Canada – *Certain Measures Affecting the Automotive Industry ("Canada – Autos"), WT/DS139/AB/R, WT/DS142/AB/R, adopted 19 June 2000, para. 79.*
[18] *Appellate Body Report,* Japan – *Alcoholic Beverages II, p. 21.*
[19] *Panel Report,* Spain – *Tariff Treatment of Unroasted Coffee ("Spain – Unroasted Coffee"), adopted 11 June 1981, BISD 28S/102, para. 4.11.*

> *related to organoleptic differences resulting from geographical factors, cultivation methods, the processing of the bean, and the genetic factor. The Panel did not consider that such differences were sufficient reason to allow for a different tariff treatment. It pointed out that it was not unusual in the case of agricultural products that the taste and aroma of the end-product would differ because of one or several of the above-mentioned factors.*
>
> *The Panel furthermore found relevant to its examination of the matter that unroasted coffee was mainly, if not exclusively, sold in the form of blends, combining various types of coffee, and that coffee in its end-use, was universally regarded as a well-defined and single product intended for drinking.*
>
> *The Panel noted that no other contracting party applied its tariff regime in respect of unroasted, non-decaffeinated coffee in such a way that different types of coffee were subject to different tariff rates.*
>
> *In the light of the foregoing, the Panel concluded that unroasted, non decaffeinated coffee beans listed in the Spanish Customs Tariff ... should be considered as "like products" within the meaning of Article I:1.*[20]

Finally, Article I:1 applies also to products that are not subject to a tariff binding.[21]

2.3.3 Was the advantage accorded "immediately and unconditionally"?

Article I:1 of the GATT 1994 requires that any advantage granted by a WTO Member to any country must be accorded "immediately and unconditionally" to all other WTO Members. This means that once a WTO Member has granted an advantage to a country, it cannot impose conditions on other WTO Members for them to benefit from that same advantage. The WTO Member must extend the benefit of the advantage to all WTO Members unconditionally.

In *US – Non-Rubber Footwear*, the Panel explained:

> *The Panel ... considered that Article I:1 does nor permit balancing more favourable treatment under some procedure against less favourable treatment under others. If such a balancing were accepted, it would entitle a contracting party to derogate from the most-favoured-nation obligation in one case, in respect of one contracting party, on the ground that it accords more favourable treatment in some other case in respect of another contracting party. In the view of the Panel, such an interpretation of the most-favoured-nation obligation of Article I:1 would defeat the very purpose underlying the unconditionality of that obligation.*[22]

In *Indonesia – Autos*, the Panel found that under the Indonesia car programmes, customs duty and tax benefits were conditional on achieving a

[20] *Panel Report,* Spain – *Unroasted Coffee, paras. 4.11 ff.*
[21] *Panel Report,* Spain – *Unroasted Coffee, para. 4.3.*
[22] *Panel Report,* US – *Non-Rubber Footwear, para. 6.11.*

certain local content value for the finished car. The Panel concluded that these conditions were inconsistent with the provisions of Article I:1 which provides that tax and customs duty advantages accorded to products of one Member (in that case, on products from the Republic of Korea) be accorded to imported like products from other Members "immediately and unconditionally".[23]

In *Canada – Autos*, the Appellate Body found:

> *The measure maintained by Canada accords the import duty exemption to certain motor vehicles entering Canada from certain countries. These privileged motor vehicles are imported by a limited number of designated manufacturers who are required to meet certain performance conditions. In practice, this measure does not accord the same import duty exemption immediately and unconditionally to like motor vehicles of* all *other Members, as required under Article I:1 of the GATT 1994. The advantage of the import duty exemption is accorded to some motor vehicles originating in certain countries without being accorded to like motor vehicles from* all *other Members. Accordingly, we find that this measure is not consistent with Canada's obligations under Article I:1 of the GATT 1994.*[24]

In *US – Certain EC Products*, the United States increased the bonding requirements on certain products imported from the European Communities in order to secure the payment of additional import duties to be imposed in retaliation for the EC banana import regime. The Panel found that the additional bonding requirements violated the most-favoured-nation treatment obligation of Article I:1 of GATT 1994, as it was applicable only to imports from the European Communities, although identical products from other WTO Members were not the subject of such an additional bonding requirements. The Panel explained further, that the regulatory distinction (whether an additional bonding requirement is needed) was not based on any characteristic of the product but depended exclusively on the origin of the product and targeted exclusively some imports from the European Communities.[25]

2.4 National Treatment Obligation: Article III

NT Obligation

The national treatment obligation, commonly referred to as the NT obligation, requires WTO Members not to discriminate *against* imported products once the imported products have entered the domestic market. In other words, Country A should not treat products imported from Country B or C less favourably than its own "like" domestic products.

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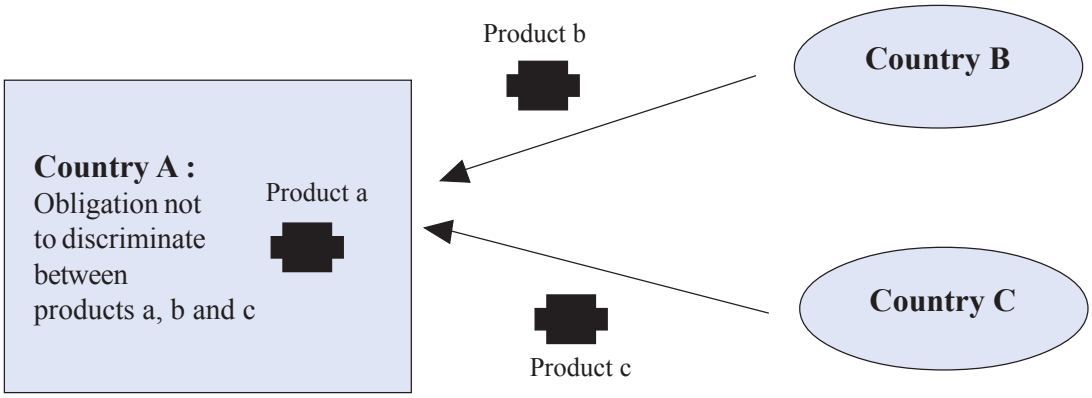
[23] *Panel Report,* Indonesia – *Certain Measures Affecting the Automobile Industry ("Indonesia – Autos"), WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R and Corr.1, 2, 3, and 4, adopted 23 July 1998, DSR 1998:VI, 2201, paras. 14.145-14.146.*

[24] *Appellate Body Report,* Canada – *Autos, para. 85.*

[25] *Panel Report,* United States – *Certain EC Products ("US – Certain EC Products"), WT/DS165/R, adopted 17 July 2000, as modified by the Appellate Body Report, WT/DS165/AB/R, para. 6.54.*



Article III GATT 1994

Article III of the GATT 1994 provides, in relevant part:

> **Article III***
>
> National Treatment on Internal Taxation and Regulation
>
> 1. *The [Members] 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 [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. Moreover, no [Member] 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.**
>
> ...
>
> 4. *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. 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.*

Purpose

Article III of the GATT 1994 prohibits discrimination between domestic and like imported products through the use of various internal measures enumerated in Article III:1, namely,

> *... 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, ...*

The purpose of Article III:1 is to ensure that such internal measures should "not be applied to imported or domestic products so as to afford protection to domestic production (Article III:1)".[26]

Japan – Alcoholic Beverages II

In *Japan – Alcoholic Beverages II*, the Appellate Body emphasized that the broad and fundamental purpose of Article III is to avoid protectionism and that toward this end,

> *... Article III obliges Members of the WTO to provide* equality of competitive conditions *for imported products in relation to domestic products.*[27]

Korea – Alcoholic Beverages

Moreover, in *Korea – Alcoholic Beverages*, the Appellate Body went on to explain further, that Article III aims at:

> *...avoiding protectionism, requiring equality of competitive conditions and protecting* expectations of equal competitive relationships.[28]

Scope of Article III

The Appellate Body also made clear that Article III of the GATT 1994, like Article I, is not limited to products that are the subject of tariff concessions under Article II of the GATT 1994.[29] However, Article III of the GATT 1994 is only concerned with internal measures and not border measures.

Internal Measures vs. Border Measures

Article III only concerns internal measures while other GATT provisions deal specifically with border measures, such as Article II on tariff concessions and Article XI on quantitative restrictions. When the measure is applied at the time or point of entry into the importing country, it may be difficult to distinguish border measures from internal measures. *Ad* Article III Note specifies:

> *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* →

[26] *Article III:1 of the GATT 1994 and Panel Report,* US – *Section 337, para. 5.10.*
[27] *Appellate Body Report,* Japan – *Alcoholic Beverages II, p. 16. See also Appellate Body Report, Korea – Taxes on Alcoholic Beverages ("Korea – Alcoholic Beverages"), WT/DS75/AB/R, WT/DS84/AB/R, adopted 17 February 1999, para. 119; Appellate Body Report,* Chile – *Taxes on Alcoholic Beverages ("Chile – Alcoholic Beverages"), WT/DS87/AB/R, WT/DS110/AB/R, adopted 12 January 2000, para. 67; Appellate Body Report,* European Communities – *Measures Affecting Asbestos and Asbestos-Containing Products ("EC – Asbestos"), WT/DS135/AB/R, adopted 5 April 2001, para. 97 and Panel Report,* Indonesia – *Autos, para. 14.108.*
[28] *Appellate Body Report,* Korea – *Alcoholic Beverages, para. 120.*
[29] *Appellate Body Report,* Japan – *Alcoholic Beverages II, pp. 16-17.*

> *requirement of the kind referred to in paragraph 1, and is accordingly subject to the provisions of Article III.*

For example, a ban on a product at the border for failure to meet public health standards would fall under Article III, and not Article XI, in spite of the fact that Article XI concerns specifically quantitative restrictions including total import bans. However, there can also be violations of both Articles III and XI in one single set of facts.[30]

Articles III:2 and III:4 GATT 1994

The general principle on non-discrimination in Article III:1 informs the rest of Article III. The following paragraphs of Article III set out specific non-discrimination obligations. Article III:2 of the GATT 1994 specifically concerns internal taxation, while Article III:4 deals with internal regulations. A further distinction needs be drawn. In Article III:2, the non-discrimination obligation regarding internal taxation applies not only to "like products" (first sentence), but also to "directly competitive or substitutable products" (second sentence). In contrast, the non-discrimination obligation regarding internal regulations in Article III:4 applies only to "like products".

Article III:1 GATT 1994

The relationship between Articles III:1, III:2 and III:4 of the GATT 1994 has been examined by the Appellate Body. Article III:1 provides the general principle that internal measures should not be applied so as to afford protection to domestic production. In *Japan – Alcoholic Beverages II*, the Appellate Body clarified that the function of this "general principle" is to " inform[] the rest of Article III". The Appellate Body went on to state:

> *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.*[31]

The Sections below examine more closely the obligations contained in Articles III:2, first sentence, Article III:2, second sentence and, Article III:4 of the GATT 1994.

2.5 *When is There a Violation of the National Treatment Obligation, under Article III:2, first sentence?*

Article III:2, first sentence, GATT 1994

Article III:2, first sentence, reads:

> *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* →

[30] *Panel Report,* India – *Measures Affecting the Automotive Sector ("India – Autos "), WT/DS146/R, WT/DS175/R and Corr.1, adopted 5 April 2002, para. 8.1.*
[31] *Appellate Body Report,* Japan – *Alcoholic Beverages II, p.18.*

taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products.

Two-Tier Test

As stated earlier, Article III:2 concerns only "internal tax or other internal charge of any kind". Once the measure at issue is an "internal tax or other internal charge of any kind", Article III:2, first sentence, sets out a two-tier test, which means that two questions need to be answered to determine whether there is a violation of Article III:2, first sentence:

(1) Whether imported and domestic products are "like products"; and

(2) Whether the imported products are taxed in excess of the domestic products.[32]

No Separate Finding under Article III:1

The Appellate Body found that it is not necessary to establish a protective application of the internal taxation measure, pursuant to Article III:1, separately from the specific elements or requirements of Article III:2, first sentence.[33] As the Appellate Body explained, this does not mean that the general principle against protectionism in Article III:1 does not apply to Article III:2, first sentence, but that Article III:2 is, in effect, an application of the general principle against protectionism.[34] The Panel clarified in *Argentina – Hides and Leather* that whenever imported products from one Member's territory are subject to taxes in excess of those applied to the like domestic products in the territory of another Member, this is deemed to "afford protection to domestic production" within the meaning of Article III:1.[35]

2.5.1 Have internal taxes been applied?

Internal Taxes

Article III:2, first sentence, concerns only "internal taxes and other charges of any kind" which are applied "directly or indirectly" on products. Internal taxes on products such as value added taxes (VAT), sales taxes and excise duties are covered by Article III:2, first sentence. However, income taxes or import duties are not covered by Article III:2, first sentence, since they do not constitute internal taxes on products. Whether internal taxes are "applied directly or indirectly" on products should be understood to mean whether these taxes were applied "on or in connection with" products. The term "charges" denotes a "pecuniary burden" or a "liability to pay money laid on a person".[36]

Penalty provisions coupled with a domestic content requirement may be qualified as "internal taxes or other charges of any kind" within the meaning

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[32] *As reflected in the Panel and the Appellate Body reports in* Canada – *Periodicals, p. 20.*
[33] *See Appellate Body Report,* Japan – *Alcoholic Beverages II, pp. 18-19.*
[34] *See Appellate Body Report,* Japan – *Alcoholic Beverages II, pp. 18-19.*
[35] *Panel Report,* Argentina – *Measures Affecting the Export of Bovine Hides and Import of Finished Leather ("Argentina – Hides and Leather"), WT/DS155/R and Corr.1, adopted 16 February 2001, para. 11.137.*
[36] *The New Shorter Oxford English Dictionary, Vol. I, Oxford (1993), p. 374.*

of Article III:2, first sentence.[37] Security deposits are not fiscal measures if they are enforced for a purchase requirement.[38] Border tax adjustments are fiscal measures by which the exporting country waives or reimburses taxes and the importing country imposes taxes in accordance with the destination principle. They enable exported products to be relieved of some or all of the tax charged in the exporting country in respect of similar domestic products sold to consumers on the home market. They also enable imported products sold to consumers to be charged with some or all of the tax charged in the importing country in respect of similar domestic products. Such border tax adjustments fall within the scope of application of Article III:2.[39]

No Aim and Effect Test

The aim pursued by the government imposing the tax measure is not relevant in determining whether the measure constitutes an internal tax within the meaning of Article III:2. In *Japan – Alcoholic Beverages II*, the Appellate Body stated that Members may pursue any given policy objective through their tax measures, provided that they do so in compliance with Article III:2.

Tax Administration *Measures*

In *Argentina – Hides and Leather,* Argentina required the pre-payment of certain taxes on the importation of goods. The Panel found that such "pre-payment" constituted a mechanism for the collection of the taxes which also provided for the imposition of charges.[40] The Panel concluded that the tax measure was not designed to achieve efficient tax administration and collection, but rather took the form of an "internal charge" applied to products and therefore, fell within the scope of Article III:2, first sentence. Therefore, "tax administration" measures are not systematically excluded from Article III:2. They must be examined closely.[41]

2.5.2 Are the imported and domestic products "like"?

"Like Products"

The national treatment obligation under Article III:2, first sentence, only applies to "like products". The concept of "like products" is not defined anywhere in the GATT 1994, and it does not contain any guidance as to the characteristics that must be considered in determining "likeness". However, numerous GATT and WTO dispute settlement reports have examined and applied the concept of "like products" in Article III:2, first sentence.

Japan – Alcoholic Beverages II

In *Japan – Alcoholic Beverages II*, the Appellate Body examined in detail the scope of the concept of "like products" within the meaning of Article III:2, first sentence. The issue was whether shochu and vodka could be considered to be "like products". The Appellate Body opted for a narrow interpretation of the concept of "like products" in the first sentence of Article III:2:

[37] *Panel Report,* United States – *Measures Affecting the Importation, Internal Sale and Use of Tobacco, ("US – Tobacco"), adopted 4 October 1994, DS44/R, para. 82.*
[38] *Panel Report,* EEC Measures on Animal Feed Proteins *("EEC – Animal Feed Proteins"), adopted 14 March 1978, BISD 25S/49, para. 4.4.*
[39] *See Report of the Working Party,* Border Tax Adjustment*, adopted 2 December 1970, BISD 18S/97.*
[40] *Panel Report,* Argentina – *Hides and Leather*, *para. 11.143.*
[41] *Panel Report,* Argentina – *Hides and Leather*, *para. 11.144.*

> *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.*[42]

The Appellate Body also confirmed the basic approach for determining "likeness" set out in the 1970 Report of the Working Party on *Border Tax Adjustments*.

> *... 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'.*[43]

Although acknowledging the helpfulness of this approach in *Japan – Alcoholic Beverages II*, the Appellate Body emphasized that the range of "like products" in Article III:2, first sentence, is meant to be narrower than the range of products contemplated in some other provisions of the GATT 1994 and other Multilateral Trade Agreements of the WTO Agreement.[44] The Appellate Body also stated that determining whether products are "like" always involves "an unavoidable element of individual, discretionary judgement".[45] The Appellate Body said further that "[n]o 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"."[46]

No Aim and Effect Test

Two Panel Reports attempted to introduce the aim and effect test in assessing the likeness of products by ruling that in determining whether two products subject to different treatment are like products, it is necessary to consider whether the product differentiation at issue was being made "so as to afford protection to domestic production".[47] This approach was explicitly rejected in 1996 by the Panel in *Japan – Alcoholic Beverages II*,[48] and the Appellate

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[42] *Appellate Body Report,* Japan – *Alcoholic Beverages II, pp. 19-20.*
[43] *Report of the Working Party,* Border Tax Adjustments*, para. 18 and Appellate Body Report,* Japan *– Alcoholic Beverages II, pp. 19-20.*
[44] *Appellate Body Report,* Japan – *Alcoholic Beverages II, pp. 19-20.*
[45] *Appellate Body Report,* Japan – *Alcoholic Beverages II, pp. 19-20.*
[46] *Appellate Body Report,* Japan – *Alcoholic Beverages II, pp. 19-20.*
[47] *See Panel Report,* United States – *Measures Affecting Alcoholic and Malt Beverages ("US – Malt Beverages"), adopted 19 June 1992, BISD 39S/206, paras.5.25 and 5.26 and the unadopted Panel Report,* United States – *Taxes on Automobiles, ("US – Automobile Taxes), circulated 11 October 1994, DS31/R, paras. 5.8 ff.*
[48] *See Panel Report,* Japan – *Taxes on Alcoholic Beverages ("Japan – Alcoholic Beverages II "), WT/DS8/R, WT/DS10/R, WT/DS11/R, adopted 1 November 1996, as modified by the Appellate Body Report, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, DSR 1996:I, 125.*

Body also implicitly confirmed the Panel's rejection of the aim and effect test.[49]

In *Japan – Alcoholic Beverages,* the Panel concluded that shochu and vodka were "like" on the basis of the following reasoning:

Example of Likeness Analysis

> *... The Panel noted that vodka and shochu shared most physical characteristics. In the Panel's view, except for filtration, there is virtual identity in the definition of the two products. The Panel noted that a difference in the physical characteristic of alcoholic strength of two products did not preclude a finding of likeness especially since alcoholic beverages are often drunk in diluted form. The Panel then noted that essentially the same conclusion had been reached in the 1987 Panel Report, which*
>
> *"... agreed with the arguments submitted to it by the European Communities, Finland and the United States that Japanese shochu (Group A) and vodka could be considered as 'like' products in terms of Article III:2 because they were both white/clean spirits, made of similar raw materials, and the end-uses were virtually identical".*
>
> *Following its independent consideration of the factors mentioned in the 1987 Panel Report, the Panel agreed with this statement. ... [The Panel] noted that (i) vodka and shochu were currently classified in the same heading in the Japanese tariffs, (although under the new Harmonized System (HS) Classification that entered into force on 1 January 1996 and that Japan plans to implement, shochu appears under tariff heading 2208.90 and vodka under tariff heading 2208.60); and (ii) vodka and shochu were covered by the same Japanese tariff binding at the time of its negotiation. Of the products at issue in this case, only shochu and vodka have the same tariff applied to them in the Japanese tariff schedule (see Annex 1). The Panel noted that, with respect to vodka, Japan offered no further convincing evidence that the conclusion reached by the 1987 Panel Report was wrong, not even that there had been a change in consumers' preferences in this respect. ... Consequently, in light of the conclusion of the 1987 Panel Report and of its independent consideration of the issue, the Panel concluded that vodka and shochu are like products. In the Panel's view, only vodka could be considered as like product to shochu since, apart from commonality of end-uses, it shared with shochu most physical characteristics. Definitionally, the only difference is in the media used for filtration. Substantial noticeable differences in physical characteristics exist between the rest of the alcoholic beverages at dispute and shochu that would disqualify them from being regarded as like products. More specifically, the use of additives would disqualify liqueurs, gin and genever; the use of ingredients would disqualify rum; lastly, appearance (arising from manufacturing processes) would disqualify whisky and brandy.....*[50]

Tariff classification and tariff bindings

On the use of tariff classification to determine "likeness", the Appellate Body in the appeal in *Japan – Alcoholic Beverages II* explained that a uniform tariff classification of products can be relevant in determining what are "like products", if sufficiently detailed. Uniform classification in tariff nomenclatures based on the Harmonized System (the "HS") was recognized in GATT 1947

[49] *Appellate Body Report,* Japan – *Alcoholic Beverages II, p. 16.*
[50] *Panel Report,* Japan – *Alcoholic Beverages II, para. 6.23.*

practice as providing a useful basis for confirming "likeness" in products. However, as regards tariff bindings, the Appellate Body cautioned:

> *[T]here 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. 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.*[51]

2.5.3 Are the imported products taxed "in excess of" the domestic products?

Article III:2, first sentence, provides that internal taxes on imported products should not be "in excess of" the internal taxes applied to "like" domestic products.

No Threshold

In *Japan – Alcoholic Beverages II*, the Appellate Body ruled that "[e]ven the smallest amount in excess is too much".[52] The Appellate Body added that Article III:2, first sentence, does not require to apply a "trade effects test", nor does it stipulate a *de minimis* standard.[53]

Equal Competitive Relationship

With regard to the absence of a "trade effects test", the Appellate Body stated:

> *... 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.*

On the absence of a *de minimis* standard, the Panel found in *US – Superfund* :

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[51] *Appellate Body Report,* Japan – *Alcoholic Beverages II, pp. 21-22.*
[52] *Appellate Body Report,* Japan – *Alcoholic Beverages II, p. 23.*
[53] *Appellate Body Report,* Japan – *Alcoholic Beverages II, p. 23.*

No de minimis standard

> *The rate of tax applied to the imported products is 3.5 cents per barrel higher than the rate applied to the like domestic products. ... The tax on petroleum is ... inconsistent with the United States' obligations under Article III:2.*[54]

In *Argentina –Hides and Leather,* the Panel rejected the argument that the tax burden differential between imported and domestic products would only exist for a 30-day period and therefore was *de minimis*.[55] In that case, the dispute concerned the Argentine tax collection system which required the pre-payment of taxes with respect to all import transactions but only with respect to internal sales made by certain taxable persons, the so-called "*agentes de percepción"*. The Panel ruled that the identity and circumstances of the persons involved in sales transactions could not serve as a justification for tax burden differentials.[56] The Panel also maintained that Article III:2, first sentence, requires a comparison of actual tax burdens. Recalling the purpose of Article III:2, first sentence, which is to ensure equality of competitive conditions between imported and like domestic products, the Panel explained that this Article is concerned with the economic impact on the competitive opportunities of imported and like domestic products, and not with taxes or charges as such or the policy purposes pursued with them.[57] Therefore, in the view of the Panel, tax burdens imposed on the taxed products should be the object of comparison.[58] The Panel stated:

> *...Were it otherwise, Members could easily evade its disciplines. Thus, even where imported and like domestic products are subject to identical tax rates, the actual tax burden can still be heavier on imported products. This could be the case, for instance, where different methods of computing tax bases lead to a greater actual tax burden for imported products.*[59]

It should be noted that the Panel in *EEC – Animal Feed Proteins* ruled that an internal regulation which merely exposes imported products to a risk of discrimination constitutes, by itself, a form of discrimination within the meaning of Article III[60].

In *Argentina – Hides and Leather*, the Panel also ruled that Article III:2, first sentence, does not permit Members to balance more favourable tax treatment of imported products in some instances against less favourable tax treatments of imported products in other instances.[61]

Finally, in *Indonesia – Autos*, the Panel found that differences in taxes which are based only upon the nationality of producers or the origin of the party and

[54] *Panel Report, United States – Taxes on Petroleum and Certain Imported Products, ("US – Superfund"), adopted 17 June 1987, BISD 34S/136, para. 5.1.1.*
[55] *Panel Report,* Argentina – *Hides and Leather, para. 11.245.*
[56] *Panel Report,* Argentina – *Hides and Leather, para. 11.220.*
[57] *Panel Report,* Argentina – *Hides and Leather, para. 11.182.*
[58] *Panel Report,* Argentina – *Hides and Leather, para. 11.182.*
[59] *Panel Report,* Argentina – *Hides and Leather, para. 11.183.*
[60] *Panel Report,* EEC – *Animal Feed Proteins, paras. 5.57, 5.60 and 5.76.*
[61] *Panel Report, Argentina – Hides and Leather, para. 11.260.*

components contained in the products are inconsistent with the national treatment obligation in Article III:2, first sentence.

2.6 When is There a Violation of the National Treatment Obligation, under Article III:2, second sentence?

Article III:2, second sentence, reads:

Article III :2, second sentence, GATT 1994

> *Moreover, no [Member] 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.*

As discussed earlier, Article III:1 sets out the general principle that internal taxes and other internal charges:

> *...should not be applied to imported or domestic products so as to afford protection to domestic production.*

Moreover, the *Ad* Article III Note provides that:

> *[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.*

Order of Analysis

Article III:2, second sentence, can only be resorted to if the measure at issue is not inconsistent with Article III:2, first sentence. Therefore, one must always apply first the test under Article III:2, first sentence. If the answer to one question is negative, then there is a need to examine further whether the measure is consistent with Article III:2, second sentence.[62] The Appellate Body stated on two occasions that Article III:2, second sentence, contemplates a "broader category of products" than Article III:2, first sentence.[63]

Three-Tier Test

As stated earlier, Article III:2 concerns only "internal tax or other internal charge of any kind". Once the measure at issue is an "internal tax or other internal charge of any kind", and after it has been determined that it is not inconsistent with the first sentence of Article III, the second sentence of Article III sets out a different test. It is a three-tier test, which means that three questions need to be answered to determine whether there is a violation of Article III:2, second sentence. In *Japan – Alcoholic Beverages*, the Appellate Body stated:

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[62] *Appellate Body Report, Canada – Certain Measures Concerning Periodicals ("Canada – Periodicals"), WT/DS31/AB/R, adopted 30 July 1997, , pp. 22-23.*

[63] *Appellate Body Report,* Japan – *Alcoholic beverages II, p. 25; Appellate Body Report,* Canada – *Periodicals, p. 19.*

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.[64]

2.6.1 Have internal taxes been applied ?

Both Articles III:2, first and second sentence, concern "internal taxes or other internal charges". This phrase has been interpreted consistently notwithstanding its position in the first or second sentence of Article III. Section 2.5.1 above includes discussion of this phrase.

2.6.2 Are the imported and domestic products "directly competitive or substitutable"?

"directly competitive or substitutable"

The national treatment obligation in Article III:2, second sentence, applies to "directly competitive or substitutable products", which is a broader category than "like products" in Article III:2, first sentence.

No perfect substitutability

In *Canada – Periodicals*, the Appellate Body ruled that products do not have to be perfectly substitutable in order to be "directly competitive or substitutable", because a case of "perfect substitutability" would fall under Article III:2, first sentence.[65]

First and second sentence of ArticleII:2

On the relationship between the concept of "like products" of Article III:2, first sentence, and the concept of "directly competitive or substitutable products" of Article III:2, second sentence, the Appellate Body stated:

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[64] *Appellate Body Report,* Japan – *Alcoholic Beverages II, p.24. See also Appellate Body Report,* Canada – *Periodicals, pp. 24-25, and Appellate Body Report,* Chile – *Alcoholic Beverages, para. 47.*

[65] *Appellate Body Report,* Canada – *Periodicals, p. 28.*

> *"Like" products are a subset of directly competitive or substitutable products: all like products are, by definition, directly competitive or substitutable products, whereas not all 'directly competitive or substitutable' products are "like". The notion of like products must be construed narrowly but the category of directly competitive or substitutable products is broader. While perfectly substitutable products fall within Article III:2, first sentence, imperfectly substitutable products can be assessed under Article III:2, second sentence.*[66]

Korea – Alcoholic Beverages

In *Korea – Alcoholic Beverages*, the Appellate Body stated that it considers products to be "directly competitive or substitutable" when they are interchangeable or if they offer alternative ways of satisfying a particular need or taste.[67] The Appellate Body also said that in examining whether products are "directly competitive or substitutable", an analysis of *latent* as well as *extant* demand is required, since "competition in the market place is a dynamic, evolving process".[68] Furthermore, the Appellate Body reminded that past panels had acknowledged that consumer behaviour could be influenced by protectionist internal taxation, and concluded that it may be highly relevant to examine latent demand.[69]

Criteria

As for the factors to be taken into account in establishing whether products are "directly competitive or substitutable", they include, in addition to their physical characteristics, common end-use and tariff classifications, the nature of the compared products and the competitive conditions in the relevant market.[70]

Korea – Alcoholic Beverages

In *Korea – Alcoholic Beverages*, the Appellate Body considered an examination of the competitive conditions in the market, and the cross-price elasticity of demand in that market, as a means for establishing whether products are "directly competitive or substitutable".[71] Cross-price elasticity studies attempt to predict the change in demand that would result from a change in the price of a product following, *inter alia*, from a change in the relative tax burdens on domestic and imported products.[72] However, the Appellate Body carefully clarified that cross-price elasticity of demand for products is not the decisive criterion in determining whether these products are "directly competitive or substitutable".[73] The Appellate Body supported the Panel's emphasis on the "quality" or "nature" of competition rather than the "quantitative overlap of competition".[74] The Appellate Body also shared the Panel's reluctance to rely on quantitative analyses of competitive relationship. In its view, an approach that focuses solely on the quantitative overlap of competition would, in essence, result in making the cross-price elasticity the

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[66] *Appellate Body Report,* Korea – *Alcoholic Beverages, para. 118.*
[67] *Appellate Body Report,* Korea – *Alcoholic Beverages, para. 114-116.*
[68] *Appellate Body Report,* Korea – *Alcoholic Beverages, para. 120.*
[69] *Appellate Body Report,* Korea – *Alcoholic Beverages, para. 120.*
[70] *See Appellate Body Report in* Japan – *Alcoholic Beverages II, p. 24.*
[71] *Appellate Body Report,* Korea – *Alcoholic Beverages, para. 121.*
[72] *See Appellate Body Report,* Korea – *Alcoholic Beverages, para. 121.*
[73] *Appellate Body Report,* Korea – *Alcoholic Beverages, para. 134.*
[74] *Appellate Body Report,* Korea – *Alcoholic Beverages, para. 134.*

decisive criterion in deciding whether products are "directly competitive or substitutable".[75]

The Appellate Body considered, in *Korea – Alcoholic Beverages*, that the market situation in other Members may be taken into consideration in determining whether products are "directly competitive or substitutable". The market situation in other Members is particularly relevant when demand on that market has been influenced by regulatory barriers to trade or to competition, on the condition that the other market display characteristics similar to the market at issue. As the Appellate Body stated, the determination of whether products are "directly competitive or substitutable" can only be determined on a case-by-case basis, taking account of all relevant facts.[76]

In examining whether products are "directly competitive or substitutable", it is not always necessary to examine products on an item-by-item basis. Products can be grouped together for the purpose of this examination. However, as the Appellate Body said, whether and to what extent products can be grouped is a matter to be decided on a case-by-case basis.[77]

2.6.3 *Are the imported and domestic products "not similarly taxed"?*

***de minimis* Standard**

In order to determine whether there is a violation of Article III:2, second sentence, it must also be found that the products at issue are "not similarly taxed". As opposed to Article III:2, first sentence, which provides that even the slightest tax difference suffices for a finding of WTO-inconsistency, Article III:2, second sentence, provides that the tax differential has to be more than *de minimis* in order to support a conclusion that the internal tax imposed on imported products is WTO-inconsistent.

Japan – Alcoholic Beverages

As the Appellate Body said in *Japan – Alcoholic Beverages II* :

> *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 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. And,*

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[75] *Appellate Body Report,* Korea – *Alcoholic Beverages, para. 134.*
[76] *Appellate Body Report,* Korea – *Alcoholic Beverages, para. 137.*
[77] *Appellate Body Report,* Korea – *Alcoholic Beverages, paras. 143-144.*

> *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.*[78]

In the event that only some imported products are similarly taxed as compared with the domestic products, while other imported products are taxed similarly, the Appellate Body found that such dissimilar taxation of even some imported products as compared to directly competitive and substitutable domestic products is inconsistent with Article III:2, second sentence.[79]

2.6.4 Is the internal tax measure applied "so as to afford protection to domestic production"?

Separate Examination

The last requirement of the test under Article III:2, second sentence, is whether the internal taxes are applied "so as to afford protection to domestic production". The Appellate Body specified that this requirement is separate from the requirement of "not similarly taxed", and that accordingly, it must be examined separately. Therefore, if imported and domestic products are "not similarly taxed", then a further inquiry must be made in order to determine whether the tax measure has been taken "so as to afford protection to domestic production".[80]

Result not intention
Intention Result

As the Appellate Body said, the examination of whether the tax measure was applied "so as to afford protection to domestic production" does not require to examine the actual intent of the legislator or regulator to engage in some form of protectionism.[81] It is the result of the application of a measure that matters under Article III:2, second sentence.[82]

In particular, the element "so as to afford protection to domestic production", requires a comprehensive and objective analysis of the structure and application of the measure at issue on domestic as compared to imported products.[83] The underlying criteria used in a particular tax measure, its structure, and its overall application may ascertain whether it is applied in a way that affords protection to domestic production.[84] Even if the aim of the same measure as such may not be easily found, the protective application of a tax measure may often be discerned "from the design, the architecture and the revealing structure of a measure".[85]

[78] *Appellate Body Report* , Japan – *Alcoholic Beverages II, pp. 26-27.*
[79] *Appellate Body Report,* Canada – *Periodicals, pp. 25-29.*
[80] *Appellate Body Report,* Japan Alcoholic Beverages II, *p. 27.*
[81] *Appellate Body Report,* Japan – *Alcoholic Beverages II, pp. 29-30.*
[82] *See Appellate Body Report,* Japan – *Alcoholic Beverages II, pp. 29-30. It should be noted however, that the Appellate Body seemed to give some importance to statements made by the representatives of the Canadian Government about the policy objectives of the tax measure at issue. See Appellate Body Report,* Japan – *Alcoholic Beverages II, footnote 20.*
[83] *Appellate Body Report,* Japan Alcoholic Beverages II, *p. 29.*
[84] *Appellate Body Report,* Japan Alcoholic Beverages II, *p. 29. See also Appellate Body Report,* Chile – *Alcoholic Beverages.*

This means that if the lower brackets of a tax measure cover almost exclusively domestic products, while the higher brackets cover almost exclusively imported products, the tax measure may be deemed to be applied so as to afford protection to domestic production. Such an analysis does not require the examination of the subjective intent of the legislator or regulator, but rather the criteria, the structure and the overall application of the tax measure.

2.7 When is There a Violation of the National Treatment Obligation, under Article III:4?

The national treatment obligation of Article III concerns internal laws and regulations as well as internal taxation. Article III:4 deals specifically with internal laws and regulations.

Article III:4 reads:

Article III :4 GATT 1994

> *4. 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. 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.*

Three-Tier Test

In order to determine whether there is a violation of Article III:4, three questions need to be answered:

(1) whether the measure at issue is a "law, regulation or requirementaffecting their internal sale, offering for sale, purchase, transportation, distribution or use";

(2) whether the imported and domestic products at issue are "like products";

(3) whether the imported products are accorded "less favourable" treatment than that accorded to like domestic products. [86]

No Separate Examination under Article III:1

It should be noted that Article III:4 does not make any specific reference to the element of "so as to afford protection to domestic production" in Article III:1. Therefore, Article III:4, like Article III:2, first sentence, does not require a separate examination of whether the measure at issue is applied "so as to afford protection to domestic production".[87]

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[85] *Appellate Body Report,* Japan Alcoholic Beverages II*, p. 27. See also Appellate Body Report,* Chile – *Alcoholic Beverages.*

[86] *See Appellate Body Report,* Korea – *Measures Affecting Imports of Fresh, Chilled and Frozen Beef ("Korea – Beef"), WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, para. 133.*

[87] *See Appellate Body Report,* EC – *Bananas III, para. 216.*

However, Article III:1 and the element of "so as to afford protection to domestic production" provide "particular contextual significance in interpreting Article III:4, as it sets forth the 'general principle' pursued by that provision".[88]

2.7.1 Have laws, regulations or requirements affecting the sale and use of products been applied?

Covered Measures

Article III:4 applies to "all laws, regulations and requirements affecting [the] internal sale, offering for sale, purchase, transportation, distribution or use[of products]". In general terms, the national treatment obligation of Article III:4 concerns regulation affecting the sale and use of products.

"affecting"

The scope of application of Article III:4 has been interpreted broadly. The use of the term "affecting" has been interpreted to mean that Article III:4 should cover not only laws and regulations which directly govern the conditions of sale or purchase but also any laws and regulations which might adversely modify the conditions of competition between the domestic and imported products on the internal markets.[89]

Procedural Laws and Regulations

Moreover, it has been found that Article III:4 covers *procedural* laws, regulations and requirements as well as *substantive* laws, regulations and requirements. The Panel in *US – Section 337* explained that enforcement procedures cannot be separated from the substantive provisions they serve to enforce.[90] The Panel also said that if procedural provisions of internal law were not covered by Article III:4, WTO Members could escape the national treatment obligation by enforcing consistent substantive law through inconsistent procedures less favourable to imported products than to like national products.[91]

GATT case law has further refined the scope of application of Article III:4. For example, it specified that Article III:4 applies to minimum price requirements applicable to domestic and imported beer[92], to limitations on points of sale for imported alcoholic beverages[93], to the practice to limit listing of imported beer to six-pack size[94], to the requirement that imported beer and wine be sold only through in-state wholesalers or other middlemen[95], to a ban on all cigarette advertising[96], to additional marking requirements such as an obligation to add the name of the producer or the place of origin or the formula

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[88] *Appellate Body Report,* EC – *Asbestos, para. 93.*
[89] *Panel Report,* Italian Discrimination Against Imported AgriculturalMachinery *("Italian Agricultural Machinery"), adopted 23 October 1958, BISD 7S/60, para. 12.*
[90] *Panel Report,* United States – *Section 337 of the Tariff Act of 1930 ("US – Section 337"), adopted 7 November 1989, BISD 36S/345, para. 5.10.*
[91] *Panel Report,* US – *Section 337, para. 5.10.*
[92] *Panel Report,* Canada – *Import Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies ("Canada – Provincial Marketing Agencies (1992)"), adopted 18 February 1992, BISD 39S/27, para.5.30.*
[93] *Panel Report,* Canada – *Provincial Marketing Agencies (1992), para. 4.26.*
[94] *Panel Report,* Canada – *Provincial Marketing Agencies (1992), para. 5.4.*
[95] *Panel Report,* US – *Malt Beverages, para. 5.32.*
[96] *Panel Report, Thailand – Restrictions on Importation of and Internal Taxes on Cigarettes ("Thailand – Cigarettes"), adopted 7 November 1990, BISD 37S/200, para. 77.*

of the product[97] and, to practices concerning internal transportation of beer.[98]

WTO reports also defined the scope of application of Article III:4. For instance, the Appellate Body agreed with the Panel that Article III:4 was applicable to the European Communities' import licensing requirements at issue in *EC – Bananas III*. The Appellate Body ruled:

> *At issue in this appeal is not whether* any *import licensing requirement, as such, is within the scope of Article III:4, but whether the EC procedures and requirements for the* distribution *of import licenses for imported bananas among eligible operators* within *the European Communities are within the scope of this provision. ... These rules go far beyond the mere import licence requirements needed to administer the tariff quota for third-country and non-traditional ACP bananas or Lomé Convention requirements for the importation of bananas. These rules are intended, among other things, to cross-subsidize distributors of EC (and ACP) bananas and to ensure that EC banana ripeners obtain a share of the quota rents. As such, these rules affect 'the internal sale, offering for sale, purchase, ...' within the meaning of Article III:4, and therefore fall within the scope of this provision*[99]

In *Canada – Autos*, the Panel used a broad interpretation of the term "affecting" by referring to measures which have an effect on imported goods. The Panel ruled that a measure can be considered to be a measure affecting the internal sale or use of imported products even if it is not shown that under current circumstances the measure has an impact on the decisions of private parties to buy imported products.[100]

"requirements"

Article III:4 also covers "requirements" which may apply to isolated cases. Although most cases dealing with Article III:4 concern laws and regulations, Article III:4 covers "requirements" which may apply to isolated cases only. However, it should be noted that both measures that apply across-the-board and measures that apply to isolated cases only are covered by Article III:4.[101] Furthermore, a "requirement" within the meaning of Article III:4 does not necessarily need to be imposed by government. Action by a private party can constitute a "requirement" under the purview of Article III:4, insofar as there is a nexus between that action and the action of a government such that the government must be held responsible for that action.[102] For instance, in *Canada – Autos*, the Panel had to decide whether commitments undertaken by Canadian motor vehicle manufacturers in letters addressed to the Canadian Government to increase Canadian value added in the production of motor vehicles, qualified as "requirements" under Article III:4. The Panel said:

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[97] *Working Party Report,* Certificates of Origin, Marks of Origin, Consular Formalities*, adopted 17 November 1956, BISD 5S/102, para. 13.*

[98] *Panel Report,* Canada – *Provincial Marketing Agencies (1992), para. 5.12; and Panel Report,* US – *Malt beverages, para. 5.50.*

[99] *Appellate Body Report,* EC – *Bananas III, para. 220*

[100] *See Panel Report,* Canada – *Autos, paras. 10.80 and 10.84.*

[101] *See Panel Report,* Canada – *Administration of the Foreign Investment Review Act ("Canada – FIRA "), adopted 7 February 1984, BISD 30S/140, para. 5.5.*

[102] *See Panel Report,* Canada – *Autos, paras. 10.80 and 10.84.*

> *We do not believe that such a nexus can exist only if a government makes undertakings of private parties legally enforceable, as in the situation considered by the Panel on* Canada – FIRA*, or if a government conditions the grant of an advantage on undertakings made by private parties, as in the situation considered by the Panel on* EEC – Parts and Components*. We note in this respect that the word 'requirement' has been defined to mean '1. The action of requiring something; a request. 2. A thing required or needed, a want, a need. Also the action or an instance of needing or wanting something. 3. Something called for or demanded; a condition which must be complied with.' The word 'requirements' in its ordinary meaning and in light of its context in Article III:4 clearly implies government action involving a demand, request or the imposition of a condition but in our view this term does not carry a particular connotation with respect to the legal form in which such government action is taken. In this respect, we consider that, in applying the concept of "requirements" in Article III:4 to situations involving actions by private parties, it is necessary to take into account that there is a broad variety of forms of government action that can be effective in influencing the conduct of private parties.*[103]

2.7.2 Are the imported and domestic products "like"?

"Like Products"

The non-discrimination obligation in Article III:4 applies only to "like products", as in Articles I:1 and III:2, first sentence, both discussed above.

EC – Asbestos

The Appellate Body examined thoroughly the meaning of the concept of "like products" in Article III:4 in *EC – Asbestos*. The Appellate Body reminded that the concept of "like products" in Article III:2, first sentence, is to be construed "narrowly".[104] However, the Appellate Body was of the opinion that the concept of "like products" in Article III:4 does not suggest a similarly narrow reading of "like" essentially because Article III:2 distinguishes "like products" from "competitive and substitutable products", while Article III:4 is only concerned with "like products". Thus, the Appellate Body concluded that given the textual difference between Articles III:2 and III:4, the "accordion" of "likeness" stretches in a different manner in Article III:4.[105]

Article III:1

As regards the effect of the "general principle" against protectionism in Article III:1 on the interpretation of Article III:4, the Appellate Body said that:

> *...[I]n endeavouring to ensure "equality of competitive conditions", the "general principle" in Article III 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."*[106]

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[103] *Panel Report,* Canada – *Autos, paras. 10.106-10.107.*
[104] *See Appellate Body Report,* EC – *Asbestos, para. 95. See Appellate Body Report,* Japan Alcoholic Beverages II*, pp. . 19-20 and Appellate Body Report,* Canada – *Periodicals, pp. 20-23.*
[105] *Appellate Body Report, EC – Asbestos, paras. 94-96.*
[106] *Appellate Body Report,* EC – *Asbestos, para. 98.*

The Appellate Body went on to state:

> *As products that are in a competitive relationship in the marketplace could be affected through treatment of* imports *"less favourable" than the treatment accorded to* domestic *products, it follows that the word "like" in Article III:4 is to be interpreted to apply to products that are in such a competitive relationship. Thus, 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.*
>
> *... [W]e [] conclude that the product scope of Article III:4, although broader than the* first *sentence of Article III:2, is certainly* not *broader than the* combined *product scope of the* two *sentences of Article III:2 of the GATT 1994.*
>
> *We recognize that, by interpreting the term "like products" in Article III:4 in this way, we give that provision a relatively broad product scope – although no broader than the product scope of Article III:2.*[107]

Criteria

The Appellate Body in *EC – Asbestos* also enumerated criteria to be taken into account to determine whether products are "like" within the meaning of Article III:4. The Appellate Body said:

> *As in Article III:2, in this determination, "[n]o one approach ... will be appropriate for all cases." Rather, an assessment utilizing "an unavoidable element of individual, discretionary judgement" has to be made on a case-by-case basis. The Report of the Working Party on* Border Tax Adjustments *outlined an approach for analyzing "likeness" that has been followed and developed since by several panels and the Appellate Body. This approach has, in the main, consisted of employing four general criteria in analyzing "likeness": (i) the properties, nature and quality of the products; (ii) the end-uses of the products; (iii) consumers' tastes and habits – more comprehensively termed consumers' perceptions and behaviour – in respect of the products; and (iv) the tariff classification of the products. We note that these four criteria comprise four categories of "characteristics" that the products involved might share: (i) the physical properties of the products; (ii) the extent to which the products are capable of serving the same or similar end-uses; (iii) 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; and (iv) the international classification of the products for tariff purposes.*[108]

Not an Exhaustive List

However, it should be noted that this list is by no means exhaustive. These criteria are meant to be "simply tools to assist in the task of sorting and examining the relevant evidence".[109] This means that all pertinent evidence should always be examined, and not only evidence related to any of these criteria. In *EC – Asbestos*, the Appellate Body disagreed with the Panel's refusal to consider the health risks posed by asbestos in its determination of

[107] *Appellate Body Report,* EC – *Asbestos, paras. 97-100.*
[108] *Appellate Body Report,* EC – *Asbestos, para. 101.*
[109] *Appellate Body Report,* EC – *Asbestos, para. 102.*

"likeness". The Appellate Body said:

> *...neither the text of Article III:4 nor the practice of panels and the Appellate Body suggest that any evidence should be excluded* a priori *from a panel's examination of "likeness". Moreover, as we have said, in examining the "likeness" of products, panels must evaluate* all *of the relevant evidence. We are very much of the view that evidence relating to the health risks associated with a product may be pertinent in an examination of "likeness" under Article III:4 of the GATT 1994. We do not, however, consider that the evidence relating to the health risks associated with chrysotile asbestos fibres need be examined under a* separate *criterion, because we believe that this evidence can be evaluated under the existing criteria of physical properties, and of consumers' tastes and habits, ...*[110]

Carcinogenicity or toxicity

Therefore, the Appellate Body concluded that the physical properties of chrysotile asbestos fibres include their carcinogenicity or toxicity, and this aspect must be considered in determining "likeness" under Article III:4. The Appellate Body also said that "evidence relating to health risks may be relevant in assessing the *competitive relationship in the market place* between allegedly 'like' products".[111]

As for the end-uses and consumer's habits, the Appellate Body stated in *EC – Asbestos* :

> *Evidence of this type is of particular importance under Article III of the GATT 1994, precisely because that provision is concerned with competitive relationships in the marketplace. If there is – or could be –* no *competitive relationship between products, a Member cannot intervene, through internal taxation or regulation, to protect domestic production. Thus, evidence about the extent to which products can serve the same end-uses, and the extent to which consumers are – or would be – willing to choose one product instead of another to perform those end-uses, is highly relevant evidence in assessing the "likeness" of those products under Article III:4 of the GATT 1994.*
>
> *We consider this to be especially so in cases where the evidence relating to properties establishes that the products at issue are physically quite different. In such cases, in order to overcome this indication that products are* not *"like", a higher burden is placed on complaining Members to establish that, despite the pronounced physical differences, there is a competitive relationship between the products such that* all *of the evidence, taken together, demonstrates that the products are "like" under Article III:4 of the GATT 1994.*[112]

As regards the element of consumers' tastes and habits, the Appellate Body said that they are highly relevant with respect to asbestos fibres or substitutes, even where commercial parties, such as manufacturers, are involved, since

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[110] *Appellate Body Report,* EC – *Asbestos, para. 113.*
[111] *Appellate Body Report,* EC – *Asbestos, para. 115. It should be noted that one Appellate Body Member wrote a "concurring opinion" on this issue in which he disagreed with the two other Members of the Division that the competitive relationship is decisive in the determination of "likeness" of products under Article III:4.*
[112] *Appellate Body Report,* EC – *Asbestos, paras. 117-118.*

the health risks associated with asbestos fibres may well influence their decision to use them or not.[113]

Although the concept of "like products" in *EC – Asbestos* was interpreted broadly, it is not so broad to include chrysotile asbestos fibers and substitutes as "like products".

US – Gasolinea

In *US – Gasoline*, the Panel found that chemically-identical imported and domestic gasoline were "like products" because "chemically-imported and domestic gasoline by definition have exactly the same physical characteristics, end-uses, tariff classification and are perfectly substitutable".[114] The Panel did not examine the aim and effect of the regulatory distinction in determining "likeness".

US – Tuna

Finally, the Panel in the unadopted report on *US – Tuna* found that differences in process and production methods of products are not relevant in determining "likeness":

> *Article III:4 calls for a comparison of the treatment of imported tuna* as a product *with that of domestic tuna* as a product*. Regulations governing the taking of dolphins incidental to the taking of tuna could not possibly affect tuna as a product. Article III:4 therefore obliges the United States to accord treatment to Mexican tuna no less favourable than that accorded to United States tuna, whether or not the incidental taking of dolphins by Mexican vessels corresponded to that of United States vessels.*[115]

This approach has attracted some criticism from scholars and environmentalists.[116]

2.7.3 Was the treatment less favourable?

In order to determine whether the measure at issue is inconsistent with Article III:4, not only must it distinguish between "like products", it has also to accord "less favourable treatment" to the like imported product than it accords to the group of like domestic products.

In *US – Section 337*, the Panel interpreted "treatment no less favourable" to require "effective equality of competitive opportunities". Panels and the

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[113] *Appellate Body Report,* EC – *Asbestos, para. 122.*

[114] *Panel Report,* United States – *Standards for Reformulated and Conventional Gasoline ("US – Gasoline"), WT/DS2/R, adopted 20 May 1996, as modified by the Appellate Body Report, WT/DS2/AB/R, DSR 1996:I, 29, para. 6.17.*

[115] *Unadopted Panel Report,* United States – *Restrictions on Imports of Tuna ("US – Tuna/Dolphin"), circulated 3 September 1991, BISD 39S/155, para. 5.15.*

[116] *For a discussion of the product-process distinction, please refer to Robert E. Hudec, "Chapter 12: The Product-Process Doctrine in the GATT/WTO Jurisprudence" in Marco Bronckers and Reinhard Quick,* New Directions in International Economic Law: Essays in Honour of John H. Jackson*, Kluwer Law International, 2000, pp.187-218; and Robert Howse and Donald Regan, "The Product/Process Distinction – An Illusory Basis for Disciplining 'Unilateralism' in Trade Policy", European Journal of International Law, Vol. 11, No. 2, 2000, pp. 249-289.*

Appellate Body have consistently used this approach in later GATT and WTO reports.[117]

In *US - Gasoline*, the Panel found that the measure at issue accorded to imported gasoline less favourable treatment than to domestic gasoline on the basis that sellers of domestic gasoline were authorized to use an individual baseline, while sellers of imported gasoline had to use the more onerous statutory baseline.[118]

Formal Difference in Treatment

In *Korea – Beef,* the dispute concerned a dual retail distribution system for the sale of beef under which imported beef was *inter alia* to be sold in specialized stores selling only imported beef or in separate sections of supermarkets. The Appellate Body found that such a measure was inconsistent with the Republic of Korea's obligations under Article III:4 of the GATT 1994. The Appellate Body emphasized that a formal difference in treatment between domestic and imported products is neither necessary nor sufficient for a violation of Article III:4. Different treatment of imported products in a formal manner does not necessarily constitute less favourable treatment. Conversely, absence of formal difference in treatment does not necessarily mean that there is no less favourable treatment. As the Appellate Body stated in that case:

> *We observe ... 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 "treatment no less favourable" means, as we have previously said, according* conditions of competition *no less favourable to the imported product than to the like domestic product. ...*
>
> *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.*[119]

No Balancing Allowed

In *US – Gasoline*, the Panel explained that "[the] wording [of Article III:4] does not allow less favourable treatment dependent on the characteristics of the producer and the nature of the data held by it".[120] The Panel also rejected the argument made by the United States that the regulation at issue treated

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[117] *See, inter alia, Panel Report,* Canada – *Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies ("Canada – Provincial Liquor Boards (US) "), adopted 18 February 1992, BISD 39S/27, paras. 5.12-5.14 and 5.30-5.31; Panel Report,* US - Malt Beverages*, para. 5.30; Panel Report,* US - Gasoline*, para. 6.10; Panel Report,* Canada – *Periodicals, p. 75; Panel Report,* European Communities – *Regime for the Importation, Sale and Distribution of Bananas – Complaint by the United States ("EC – Bananas III (US) "), WT/DS27/R/USA, adopted 25 September 1997, as modified by the Appellate Body Report, WT/DS27/AB/R, DSR 1997:II, 943, paras. 7.179-7.180; and Panel Report,* Japan – *Measures Affecting Consumer Photographic Film and Paper ("Japan – Film "), WT/DS44/R, adopted 22 April 1998, DSR 1998:IV, 1179, para. 10.379.*

[118] *See Panel Report,* US – *Gasoline, para. 6.10.*

[119] *Appellate Body Report,* Korea –*Beef, paras. 135-137.*

[120] *Panel Report,* US – *Gasoline, para. 6.11.*

imported products "equally overall" and was therefore consistent with Article III:2. The Panel noted that this argument amounted to claiming that less favourable treatment of particular imported products in some instances could be offset or balanced by more favourable treatment of particular products in others.[121] However, under Articles I:1, III:2 and III:4, such "balancing" is not admissible.[122]

In GATT and WTO case law, a wide variety of measures have been found inconsistent with the national treatment obligation of Article III:2, apart from the measures at issue in *US – Section 337*, *Korea – Beef* and *US - Gasoline*. They include minimum price requirements,[123] regulations concerning internal transportation,[124] the allocation system for tariff quota for bananas,[125] and the Canadian Value Added requirements in the automobile industry.[126]

2.8 Test Your Understanding

1. **What are the two elements of the non-discrimination principle in international trade law? What is the difference between the most-favoured-nation treatment obligation and the national treatment obligation?**
2. **What is the objective of the most-favoured-nation treatment obligation? When is there a violation of the most-favoured-nation treatment obligation? Is the concept of "advantage" limited to internal taxes, laws, regulations and requirements? Is the concept of "like products" interpreted consistently in the different provisions of the GATT 1994? What are the criteria to determine whether two products are "like" within the meaning of Article I:1of the GATT 1994? Once a WTO Member has granted an advantage to a country, can it impose conditions on other WTO Members for them to benefit from that same advantage?**
3. **What is the objective of the national treatment obligation? Is the national treatment obligation limited to products subject to tariff concessions under Article II of the GATT 1994? Does Article II apply to internal measures only?**
4. **When is there a violation of Article III, first sentence? Can tax administration measures qualify as "internal taxes or charges" within the meaning of this Article? How does one assess whether products are "like" within the meaning of Article III:2, first sentence? What is the minimum amount of the internal tax or charge for which the imported products are considered to be taxed "in excess of" the domestic products? Does Article III:2, first sentence, require a separate examination of whether the measure**

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[121] *Panel Report,* US – *Gasoline, para. 6.14.*
[122] *See Panel Report,* US – *Section 337, para. 6.14.*
[123] *See Panel Report,* Canada – *Provincial Marketing Agencies.*
[124] *See Panel Report,* US – *Malt Beverages.*
[125] *See Appellate Body Report,* EC – *Bananas III.*
[126] *See Appellate Body Report,* Canada – *Autos.*

at issue is applied "so as to afford protection to domestic production"?

5. **When can an interpreter consider Article III:2, second sentence? When is there a violation of Article III:2, second sentence? How does the concept of "directly competitive or substitutable" differ from the concept of "like products"? What is the minimum amount of the internal tax or charge for which the imported and domestic products are considered to be "not similarly taxed"? Does Article III:2, second sentence, require a separate examination of whether the measure at issue is applied "so as to afford protection to domestic production"?**
6. **When is there a violation of Article III:4? What types of measures does Article III:4 apply to? How different is the concept of "like products" interpreted in Article III:4 as compared with other GATT provisions? What criteria need be taken into consideration in determining whether products are "like" under Article III:4? Does Article III:4 require a separate examination of whether the measure at issue is applied "so as to afford protection to domestic production"?**