PART II

ARTICLE III

NATIONAL TREATMENT ON INTERNAL TAXATION AND REGULATION

I. TEXT OF ARTICLE III AND INTERPRETATIVE NOTE AD ARTICLE III

Article III*

National Treatment on Internal Taxation and Regulation

1. The contracting parties recognize that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products, and internal quantitative regulations requiring the mixture, processing or use of products in specified amounts or proportions, should not be applied to imported or domestic products so as to afford protection to domestic production.*

2. The products of the territory of any contracting party imported into the territory of any other contracting party shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products. Moreover, no contracting party shall otherwise apply internal taxes or other internal charges to imported or domestic products in a manner contrary to the principles set forth in paragraph 1.*

3. With respect to any existing internal tax which is inconsistent with the provisions of paragraph 2, but which is specifically authorized under a trade agreement, in force on April 10, 1947, in which the import duty on the taxed product is bound against increase, the contracting party imposing the tax shall be free to postpone the application of the provisions of paragraph 2 to such tax until such time as it can obtain release from the obligations of such trade agreement in order to permit the increase of such duty to the extent necessary to compensate for the elimination of the protective element of the tax.

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

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

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

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

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

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

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

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

Interpretative Note *Ad* Article III from Annex I

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

Paragraph 1

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

Paragraph 2

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

Paragraph 5

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

II. INTERPRETATION AND APPLICATION OF ARTICLE III

A. SCOPE AND APPLICATION OF ARTICLE III

1. General

(1) Scope of Article III

The 1958 Panel Report on "Italian Discrimination against Imported Agricultural Machinery," which examined an Italian law providing special credit terms for the purchase of agricultural machinery produced in Italy, notes that the Panel examined the argument of Italy that "the General Agreement was a trade agreement and its scope was limited to measures governing trade ... the commitment undertaken by the CONTRACTING PARTIES under [Article III:4] was limited to qualitative and quantitative regulations to which goods were subjected, with respect to their sale or purchase on the domestic market."[1] The Panel found as follows.

> "The Panel ... noted that if the Italian contention were correct, and if the scope of Article III were limited in the way the Italian delegation suggested to a specific type of law and regulations, the value of the bindings under Article II of the Agreement and of the general rules of non-discrimination as between imported and domestic products could be easily evaded.
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> "The Panel recognized ... that it was not the intention of the General Agreement to limit the right of a contracting party to adopt measures which appeared to it necessary to foster its economic development or to protect a domestic industry, provided that such measures were permitted by the General Agreement. The GATT offered a number of possibilities to achieve these purposes through tariff measures or otherwise. The Panel did not appreciate why the extension of the credit facilities in question to the purchasers of imported tractors as well as domestically produced tractors would detract from the attainment of the objectives of the Law, which aimed at stimulating the purchase of tractors mainly by small farmers and co-operatives in the interests of economic development. If, on the other hand, the objective of the Law, although not specifically stated in the text thereof, were to protect the Italian agricultural machinery industry, the Panel considered that such protection should be given in ways permissible under the General Agreement rather than by the extension of credit exclusively for purchases of domestically produced agricultural machinery."[2]

The 1984 Panel Report on "Canada - Administration of the Foreign Investment Review Act" examined written purchase and export undertakings under the Foreign Investment Review Act of Canada, submitted by investors regarding the conduct of the business they were proposing to acquire or establish, conditional on approval by the Canadian government of the proposed acquisition or establishment. Written undertakings are legally binding on the investor if the investment is allowed. The Panel noted:

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[1] L/833, adopted 23 October 1958, 7S/60, 63, para. 6.
[2] *Ibid*., 7S/64-65, paras. 15-16.

"... the Panel does not consider it relevant nor does it feel competent to judge how the foreign investors are affected by the purchase requirements, as the national treatment obligations of Article III of the General Agreement do not apply to foreign persons or firms but to imported products and serve to protect the interests of producers and exporters established on the territory of any contracting party".[3]

(2) Purpose of Article III

The 1958 Panel Report on "Italian Discrimination against Imported Agricultural Machinery" provides that "It was considered ... that the intention of the drafters of the Agreement was clearly to treat the imported products in the same way as the like domestic products once they had been cleared through customs. Otherwise indirect protection could be given".[4]

The Panel Report on "United States - Section 337 of the Tariff Act of 1930" notes that "... the purpose of Article III ... is to ensure that internal measures 'not be applied to imported or domestic products so as to afford protection to domestic production' (Article III:1)".[5] The same Panel "rejected any notion of balancing more favourable treatment of some imported products against less favourable treatment of other imported products. ... Such an interpretation would lead to great uncertainty about the conditions of competition between imported and domestic products and thus defeat the purposes of Article III".[6]

The 1987 Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances" notes that "Article III:2, first sentence, obliges contracting parties to establish certain competitive conditions for imported products in relation to domestic products. Unlike some other provisions in the General Agreement, it does not refer to trade effects".[7] See further on page 128. Concerning another issue examined by the panel, the same panel report provides:

"... The general prohibition of quantitative restrictions under Article XI ... and the national treatment obligation of Article III ... have essentially the same rationale, namely to protect expectations of the contracting parties as to the competitive relationship between their products and those of the other contracting parties. Both articles are not only to protect current trade but also to create the predictability needed to plan future trade".[8]

The 1991 Panel Report on "United States - Restrictions on Imports of Tuna," which has not been adopted, notes with regard to Article III:

"... While restrictions on importation are prohibited by Article XI:1, contracting parties are permitted by Article III:4 and the Note Ad Article III to impose an internal regulation on products imported from other contracting parties provided that it: does not discriminate between products of other countries in violation of the most-favoured-nation principle of Article I:1; is not applied so as to afford protection to domestic production, in violation of the national treatment principle of Article III:1; and accords to imported products treatment no less favourable than that accorded to like products of national origin, consistent with Article III:4....

"The text of Article III:1 refers to the application to imported or domestic products of 'laws, regulations and requirements affecting the internal sale ... of *products*' and 'internal quantitative regulations requiring the mixture, processing or use of *products*'; it sets forth the principle that such regulations on *products* not be applied so as to afford protection to domestic production. Article III:4 refers solely to laws, regulations and requirements affecting the internal sale, etc. of *products*. This suggests that Article III covers only measures affecting products as such. Furthermore, the text of the Note Ad Article III refers to a measure 'which applies to an imported *product* and the like domestic

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[3] L/5504, adopted 7 February 1984, 30S/140, 167, para. 6.5.
[4] L/833, adopted on 23 October 1958, 7S/60, 63-64, para. 11.
[5] L/6439, adopted on 7 November 1989, 36S/345, 385, para. 5.10.
[6] 36S/387, para. 5.14.
[7] L/6175, adopted 17 June 1987, 34S/136, 158, para. 5.1.9.
[8] *Ibid.*, 34S/160, para. 5.2.2.

product and is collected or enforced in the case of the imported *product* at the time or point of importation'. This suggests that this Note covers only measures applied to imported products that are of the same nature as those applied to the domestic products, such as a prohibition on importation of a product which enforces at the border an internal sales prohibition applied to both imported and like domestic products.

"A previous panel had found that Article III:2, first sentence, 'obliges contracting parties to establish certain competitive conditions for imported *products* in relation to domestic *products*'.[9] Another panel had found that the words 'treatment no less favourable' in Article III:4 call for effective equality of opportunities for imported *products* in respect of the application of laws, regulations or requirements affecting the sale, offering for sale, purchase, transportation, distribution or use of *products*, and that this standard has to be understood as applicable to each individual case of imported *products*.[10] It was apparent to the Panel that the comparison implied was necessarily one between the measures applied to imported products and the measures applied to like domestic products".[11]

The 1992 Panel Report on United States - Measures Affecting Alcoholic and Malt Beverages" noted with respect to the application of the Article III rules which compare the tax treatment accorded to "like products":

"The basic purpose of Article III is to ensure, as emphasized in Article III:1,

'that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, purchase, transportation, distribution or use of products ... should not be applied to imported or domestic products so as to afford protection to domestic production'.

"The purpose of Article III is thus not to prevent contracting parties from using their fiscal and regulatory powers for purposes other than to afford protection to domestic production. Specifically, the purpose of Article III is not to prevent contracting parties from differentiating between different product categories for policy purposes unrelated to the protection of domestic production. The Panel considered that the limited purpose of Article III has to be taken into account in interpreting the term 'like products' in this Article. Consequently, in determining whether two products subject to different treatment are like products, it is necessary to consider whether such product differentiation is being made 'so as to afford protection to domestic production'. While the analysis of 'like products' in terms of Article III:2 must take into consideration this objective of Article III, the Panel wished to emphasize that such an analysis would be without prejudice to the 'like product' concepts in other provisions of the General Agreement, which might have different objectives and which might therefore also require different interpretations".[12]

In the same Report, referring to regulatory treatment of "like products",

"... The Panel recalled ... its earlier statement on like product determinations and considered that, in the context of Article III, it is essential that such determinations be made not only in the light of such criteria as the products' physical characteristics, but also in the light of the purpose of Article III, which is to ensure that internal taxes and regulations 'not be applied to imported or domestic products so as to afford protection to domestic production'. The purpose of Article III is not to harmonize the internal taxes and regulations of contracting parties, which differ from country to country. In light of these considerations, the Panel was of the view that the particular level at which the distinction between high alcohol and low alcohol beer is made in the various states does not affect its reasonings and findings.

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[9]A footnote to this paragraph refers to the Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances", adopted 17 June 1987, BISD 34S/136, 158, para. 5.1.9.

[10]A footnote to this paragraph refers to the Panel Report on "United States - Section 337 of the Tariff Act of 1930," adopted 7 November 1989, BISD 36S/345, 386-7, paras. 5.11, 5.14.

[11]DS21/R, 3 September 1991, 39S/155, 193-194, paras. 5.9, 5.11-5.12.

[12]DS23/R, adopted 19 June 1992, 39S/206, 276, para. 5.25.

"The Panel recognized that the treatment of imported and domestic products as like products under Article III may have significant implications for the scope of obligations under the General Agreement and for the regulatory autonomy of contracting parties with respect to their internal tax laws and regulations: once products are designated as like products, a regulatory product differentiation, e.g. for standardization or environmental purposes, becomes inconsistent with Article III even if the regulation is not 'applied … so as afford protection to domestic production'. In the view of the Panel, therefore, it is imperative that the like product determination in the context of Article III be made in such a way that it not unnecessarily infringe upon the regulatory authority and domestic policy options of contracting parties".[13]

(3) Relevance of tariff concessions

The first Report of the Working Party on "Brazilian Internal Taxes" notes that "The working party agreed that a contracting party was bound by the provisions of Article III whether or not the contracting party in question had undertaken tariff commitments in respect of the goods concerned".[14]

In the 1990 Panel Report on "EEC - Regulation on Imports of Parts and Components," in connection with the Panel's examination of whether anti-circumvention duties levied by the EEC were import duties under Article II or internal taxes under Article III:

"… The Panel recalled that the distinction between import duties and internal charges is of fundamental importance because the General Agreement regulates ordinary customs duties, other import charges and internal taxes differently: the imposition of 'ordinary customs duties' for the purpose of protection is allowed unless they exceed tariff bindings; all other duties or charges of any kind imposed on or in connection with importation are in principle prohibited in respect of bound items (Article II:1(b)). By contrast, internal taxes that discriminate against imported products are prohibited, whether or not the items concerned are bound (Article III:2)".[15]

(4) Relevance of policy purpose of internal measures

The 1952 Panel Report on "Special Import Taxes Instituted by Greece" states: "It appeared to the Panel that the principal question arising for determination was whether or not the Greek tax was an internal tax or charge on imported products within the meaning of paragraph 2 of Article III. If the finding on this point were affirmative, the Panel considered that it would be subject to the provisions of Article III whatever might have been the underlying intent of the Greek Government in imposing the tax".[16]

See also the discussion of eligibility for border tax adjustment in the 1987 Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances".[17] See also the material above from the 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages"[18], and the unadopted Panel Report of 1994 on "United States - Taxes on Automobiles."[19]

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[13] *Ibid*., 39S/293-294, paras. 5.71-5.72.
[14] GATT/CP.3/42, adopted 30 June 1949, II/181, 182, para. 4.
[15] L/6657, adopted on 16 May 1990, 37S/132, 191-192, para. 5.4.
[16] G/25, adopted 3 November 1952, 1S/48, 49, para. 5.
[17] L/6175, adopted 17 June 1987, 34S/136, para. 5.2.3ff; see below at page 147.
[18] DS23/R, adopted 19 June 1992, 39S/206, 276, 293-294, paras. 5.25, 5.71-5.72.
[19] DS31/R, dated 11 October 1994, paras. 5.5-5.16, 5.23-5.36.

(5) Relevance of trade effects

The 1949 Working Party Report on "Brazilian Internal Taxes" notes that

> "... the delegate of Brazil submitted the argument that if an internal tax, even though discriminatory, does not operate in a protective manner the provisions of Article III would not be applicable. He drew attention to the first paragraph of Article III, which prescribes that such taxes should not be applied 'so as to afford protection to domestic production'.... The delegate of Brazil .... suggested that where there were no imports of a given commodity or where imports were small in volume, the provisions of Article III did not apply. [The majority of the working party] argued that the absence of imports from contracting parties during any period of time that might be selected for examination would not necessarily be an indication that they had no interest in exports of the product affected by the tax, since their potentialities as exporters, given national treatment, should be taken into account. These members of the working party therefore took the view that the provisions of the first sentence of Article III, paragraph 2, were equally applicable whether imports from other contracting parties were substantial, small or non-existent".[20]

The 1987 Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances" found, *inter alia*, that an excise tax on petroleum was imposed at a higher rate on imported products than on the like domestic product, and therefore was inconsistent with Article III:2, first sentence (see page 150 below); the Panel examined the argument of the United States that the tax differential of 3.5 US cents per barrel was so small that it did not nullify or impair benefits accruing to Canada, the EEC and Mexico under the General Agreement. The Panel noted with respect to Article III:2:

> "An acceptance of the argument that measures which have only an insignificant effect on the volume of exports do not nullify or impair benefits accruing under Article III:2, first sentence, implies that the basic rationale of this provision - the benefit it generates for the contracting parties - is to protect expectations on export volumes. That, however, is not the case. Article III:2, first sentence, obliges contracting parties to establish certain competitive conditions for imported products in relation to domestic products. Unlike some other provisions in the General Agreement, it does not refer to trade effects. The majority of the members of the Working Party on the 'Brazilian Internal Taxes' therefore correctly concluded that the provisions of Article III:2, first sentence, 'were equally applicable, whether imports from other contracting parties were substantial, small or non-existent' (BISD Vol. II/185). The Working Party also concluded that 'a contracting party was bound by the provisions of Article III whether or not the contracting party in question had undertaken tariff commitments in respect of the goods concerned' (BISD Vol. II/182), in other words, the benefits under Article III accrue independent of whether there is a negotiated expectation of market access or not. Moreover, it is conceivable that a tax consistent with the national treatment principle (for instance, a high but non-discriminatory excise tax) has a more severe impact on the exports of other contracting parties than a tax that violates that principle (for instance a very low but discriminatory tax). The case before the Panel illustrates this point: the United States could bring the tax on petroleum in conformity with Article III:2, first sentence, by raising the tax on domestic products, by lowering the tax on imported products or by fixing a new common tax rate for both imported and domestic products. Each of these solutions would have different trade results, and it is therefore logically not possible to determine the difference in trade impact between the present tax and one consistent with Article III:2, first sentence, and hence to determine the trade impact resulting from the non-observance of that provision. For these reasons, Article III:2, first sentence, cannot be interpreted to protect expectations on export volumes; it protects expectations on the competitive relationship between imported and domestic products. A change in the competitive relationship contrary to that provision must consequently be regarded ipso facto as a nullification or impairment of benefits accruing under the General Agreement. A demonstration that a measure inconsistent with Article III:2, first sentence, has no or insignificant effects would therefore in the view of the Panel not be a sufficient demonstration that the benefits accruing under that provision had not been nullified or impaired even if such a rebuttal were in principle permitted".[21]

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[20]GATT/CP.3/42, adopted 30 June 1949, II/181, 185, para. 16.
[21]L/6175, adopted 17 June 1987, 34S/136, 158, para. 5.1.9.

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" examined an argument that since only 1.5 per cent of domestic beer in the United States was eligible for a reduction in the excise tax on beer and less than one per cent of domestic beer benefited from the tax reduction, "the federal excise tax neither discriminated against imported beer nor provided protection to domestic production".

> "The Panel noted the United States argument that the total number of barrels currently subject to the lower federal excise tax rate represented less than one per cent of total domestic beer production, that over 99 per cent of United States beer was subject to the same federal excise tax as that imposed on imported beer, and that therefore the federal excise tax neither discriminated against imported beer nor provided protection to domestic production. The Panel further noted that although Canada did not accept the United States estimate that the tax exemption applied to only one per cent of United States production, it pointed out that this figure nonetheless equalled total Canadian exports of beer to the United States. In accordance with previous panel reports adopted by the CONTRACTING PARTIES, the Panel considered that Article III:2 protects competitive conditions between imported and domestic products but does not protect expectations on export volume. In the view of the Panel, the fact that only approximately 1.5 per cent of domestic beer in the United States is eligible for the lower tax rate cannot justify the imposition of higher internal taxes on imported Canadian beer than on competing domestic beer. The prohibition of discriminatory taxes in Article III:2, first sentence, is not conditional on a 'trade effects test' nor is it qualified by a *de minimis* standard. ... Thus, in the view of the Panel, the fact that only approximately 1.5 per cent of domestic beer in the United States is eligible for the lower tax rate does not immunize this United States measure from the national treatment obligation of Article III."[22]

The same Panel examined a similar argument with respect to paragraph 4 of Article III.

> "With respect to Vermont and Virginia, the Panel noted that certain imported wines cannot be sold in state-operated liquor stores whereas the like domestic wine can. The Panel recalled the United States argument that the number of state-operated sales outlets was relatively small compared to the number of private outlets. The Panel considered that although Canadian wine has access to most of the available sales outlets in these states, it is still denied competitive opportunities accorded to domestic like products with respect to sales in state-operated outlets. Therefore, the Panel considered that the Vermont and Virginia measures are inconsistent with Article III:4."[23]

In 1994, the Panel on "United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco" noted, in relation to an argument regarding a difference in the amount of nonrefundable marketing assessment, termed "budget deficit assessment" ("BDA") charged on imported tobacco and on domestically produced tobacco:

> "The Panel ... recalled the U.S. argument that the discriminatory impact of the BDA differential was so small as to be of no commercial consequence. Here, the Panel noted that previous panels had rejected arguments of de minimis trade consequences and had found that the size of the trade impact of a measure was not relevant to its consistency with Article III.[24] The CONTRACTING PARTIES had recognized that Article III protected expectations on the competitive relationship between imported and domestic products, not export volumes.[25] In accordance with these past panel rulings, the Panel considered that it was not permissible to impose higher internal taxes on imported products than on like domestic products,

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[22]DS23/R, adopted 19 June 1992, 39S/206, 270-271, para. 5.6.

[23]*Ibid.*, 39S/292, para. 5.65.

[24]The footnote to this sentence in the panel report provides: "See, *e.g.*, report of the panel on United States - Taxes on Petroleum and Certain Imported Substances, adopted on 17 June 1987, BISD 34S/136, 155-159; report of the panel on United States - Section 337 of the Tariff Act of 1930, adopted on 7 November 1989, BISD 36S/345, 386-387".

[25]The footnote to this sentence in the panel report refers to the panel report on "United States - Taxes on Petroleum and Certain Imported Substances", adopted on 17 June 1987, BISD 34S/136, 158 ("Article III:2, first sentence, obliges contracting parties to establish certain competitive conditions for imported products in relation to domestic products. Unlike some other provisions of the General Agreement, it does not refer to trade effects") and also to the panel report on "United States - Measures Affecting Alcoholic and Malt Beverages", adopted on 19 June 1992, BISD 39S/206, 271.

even where the difference was minimal or of no commercial consequence.[26] The Panel thus rejected this particular U.S. defense of the BDA.

> "... the Panel concluded that the BDA subjected imported tobacco to an internal tax or charge in excess of that applied to like domestic tobacco."[27]

(6) Application of Article III to regional and local governments and authorities within the territory of a contracting party

See the Note *ad* Article III:1, which provides that the application of paragraph 1 to internal taxes imposed by local governments and authorities within the territory of a contracting party is subject to the provisions of the final paragraph of Article XXIV, and adds certain qualifying conditions. This Note was added at the Havana Conference. In response to a request for an explanation of which internal taxes might be considered "technically inconsistent with the letter but not inconsistent with the spirit of Article III" in terms of the Note, the representative of Colombia replied that "the first part of the interpretative note had been drafted to cover certain problems of Colombia connected with domestic products, subject to prices fixed by local public monopolies, which could not be taxed in the same manner as the like imported products, which were subject to a consumption tax, without grave political and administrative consequences".[28]

The 1992 Panel Report on "Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies" considered measures of provincial liquor boards which applied both to beer originating outside Canada and beer from other provinces of Canada. A note to the Panel findings provides that "Throughout these findings the reference to domestic beer is a reference to the domestic beer which receives the most favourable treatment by Canada in the province in question, that is in most instances the beer brewed in that province".[29]

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" observed with respect to differential excise taxes levied by US states:

> "The Panel did not consider relevant the fact that many of the state provisions at issue in this dispute provide the same treatment to products of other states of the United States as that provided to foreign products. The national treatment provisions require contracting parties to accord to imported products treatment no less favourable than that accorded to any like domestic product, whatever the domestic origin. Article III consequently requires treatment of imported products no less favourable than that accorded to the most-favoured domestic products".[30]

The same Panel also examined the listing requirements of state-operated liquor stores in certain states.

> "Having regard to the past panel decisions and the record in the instant case, the present Panel was of the view that the listing and delisting practices here at issue do not affect importation as such into the United States and should be examined under Article III:4. The Panel further noted that the issue is not whether the practices in the various states affect the right of importation as such, in that they clearly apply to both domestic (out-of-state) and imported wines; rather, the issue is whether the listing and delisting practices accord less favourable treatment – in terms of competitive opportunities – to imported wine than that accorded to the like domestic product. Consequently, the Panel decided to analyze the state listing and delisting practices as internal measures under Article III:4."[31]

See also generally Article XXIV:12.

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[26]The footnote to this sentence in the panel report refers to the panel report on "United States - Taxes on Petroleum and Certain Imported Substances", adopted on 17 June 1987, BISD 34S/136, 158-159.

[27]DS44/R, adopted on 4 October 1994, paras. 99-100.

[28]E/CONF.2/C.3/SR.40, p. 2; see also E/CONF.2/C.3/A/W.30, p. 1.

[29]DS17/R, adopted 18 February 1992, 39S/27, 75, note to finding in para. 5.4 applying Article III:4.

[30]DS23/R, adopted 19 June 1992, 39S/206, 274, para. 5.17.

[31]*Ibid.*, 39S/292, para. 5.63.

(7) Application of Article III with regard to State trading monopolies

During discussions in Sub-Committee A of the Third Committee at the Havana Conference, it was agreed that "state monopolies importing products for commercial resale were not excepted from the provisions of Article 18".[32] Also during the Havana Conference, in order to make it clear that an internal tax levied by a State monopoly, if treated as a negotiable monopoly margin, would not fall within the scope of Article 18 [III], the following Interpretative Note was added to Article 31 of the Charter:[33]

> "The maximum import duty referred to in paragraph 2 and 4 [of Article 31] would cover the margin which has been negotiated or which has been published or notified to the Organization, whether or not collected, wholly or in part, at the custom house as an ordinary customs duty".[34]

The 1988 Panel Report on "Canada - Import, Distribution and Sale of Alcoholic Drinks by Canadian Provincial Marketing Agencies" examined, *inter alia*, mark-up practices of provincial marketing agencies, or "liquor boards" which have a monopoly of the supply and distribution of alcoholic beverages in Canada.

> "The Panel ... noted that the retail prices charged by the provincial liquor boards for imported alcoholic beverages were composed of the invoice price; *plus* federal customs duties collected at the bound rates; *plus* standard freight to a set destination; *plus* additional price increases ('mark-ups') which were sometimes higher on imported than on like domestic alcoholic beverages ('differential mark-ups'); *plus* federal and provincial sales taxes. ...
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> "... It noted that federal and provincial sales taxes were levied on alcoholic beverages and asked itself whether the fiscal elements of mark-ups, which produced revenue for the provinces, could also be justified as 'internal taxes conforming to the provisions of Article III', noting that Article III:2 itself referred, not only to internal taxes, but also to 'other internal charges'. The Panel was of the view that to be so considered, the fiscal element of mark-ups must of course meet the requirements of Article III, e.g. they must not be applied to imported or domestic products so as to afford protection to domestic production. The Panel also considered it important that, if fiscal elements were to be considered as internal taxes, mark-ups would also have to be administered in conformity with other provisions of the General Agreement, in particular Article X dealing with the Publication and Administration of Trade Regulations."[35]

In regard to its examination of the listing practices of provincial liquor boards:

> "... the Panel saw great force in the argument that Article III:4 was also applicable to state-trading enterprises at least when the monopoly of the importation and monopoly of the distribution in the domestic markets were combined, as was the case of the provincial liquor boards in Canada. This interpretation was confirmed *e contrario* by the wording of Article III:8(a)".[36]

The 1989 Panel Report on "Thailand - Restrictions on Importation of and Internal Taxes on Cigarettes" notes as follows:

> "The Panel ... examined how Thailand might restrict the *supply* of cigarettes in a manner consistent with the General Agreement. The Panel noted that contracting parties may maintain governmental monopolies, such as the Thai Tobacco Monopoly, on the importation and domestic sale of products.[37] The Thai Government may use this monopoly to regulate the overall supply of cigarettes, their prices and their retail availability provided it thereby does not accord imported cigarettes less favourable treatment

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[32]E/CONF.2/C.3/A/W.50, p. 1.
[33]Havana Reports, p. 67, para. 74.
[34]Havana Charter, Interpretative Note to Article 31. The General Agreement contains no corresponding interpretative note.
[35]L/6304, adopted 22 March 1988, 35S/37, 87, para. 4.11 and 88-89, para. 4.20.
[36]L/6304, adopted on 22 March 1988, 35S/37, 90, para. 4.26.
[37]Note 1 on page 37S/225 provides: "Cf. Articles III:4, XVII and XX(d)".

than domestic cigarettes or act inconsistently with any commitments assumed under its Schedule of Concessions.[38]

The 1992 Panel Report on "Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies" found as follows concerning Article III.

> "The Panel ... turned to Canada's argument that its right to deliver imported beer to the points of sale was an inherent part of Canada's right to establish an import monopoly in accordance with Article XVII of the General Agreement which was not affected by its obligations under Article III:4. The Panel noted that the issue before it was not whether Canada had the right to create government monopolies for the importation, internal delivery and sale of beer. The Panel fully recognized that there was nothing in the General Agreement which prevented Canada from establishing import and sales monopolies that also had the sole right of internal delivery. The only issue before the Panel was whether Canada, having decided to establish a monopoly for the internal delivery of beer, might exempt domestic beer from that monopoly. The Panel noted that Article III:4 did not differentiate between measures affecting the internal transportation of imported products that were imposed by governmental monopolies and those that were imposed in the form of regulations governing private trade. Moreover, Articles II:4, XVII and the Note Ad Articles XI, XII, XIII, XIV and XVIII clearly indicated the drafters' intention not to allow contracting parties to frustrate the principles of the General Agreement governing measures affecting private trade by regulating trade through monopolies. Canada had the right to take, in respect of the privately delivered beer, the measures necessary to secure compliance with laws consistent with the General Agreement relating to the enforcement of monopolies. This right was specifically provided for in Article XX(d) of the General Agreement. The Panel recognized that a beer import monopoly that also enjoyed a sales monopoly might, in order properly to carry out its functions, also deliver beer but it did not for that purpose have to prohibit unconditionally the private delivery of imported beer while permitting that of domestic beer. For these reasons the Panel *found* that Canada's right under the General Agreement to establish an import and sales monopoly for beer did not entail the right to discriminate against imported beer inconsistently with Article III:4 through regulations affecting its internal transportation."[39]

With respect to the issue of mark-ups:

> "The Panel noted that Canada taxed both imported and domestic beer by assessing mark-ups through the liquor boards and by levying provincial sales taxes and the federal Goods and Services Tax at the retail level. ...
>
> "The Panel noted that, according to Article III:2, first sentence, imported products
>
> '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'.
>
> "The Panel considered that this provision applied not only to the provincial and federal sales taxes but also to the mark-ups levied by the liquor boards because they also constituted internal governmental charges borne by products".[40]

The Panel also found that the following requirements maintained by Canadian provincial liquor boards fell under Article III:4: the practice of the liquor boards of Ontario to limit listing of imported beer to the six-pack size while according listings in different package sizes to domestic beer; restrictions on private delivery of beer, including levies for delivering imported beer; and application of minimum prices to domestic and imported beer.

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[38]DS10/R, adopted on 7 November 1990, 37S/200, 225, para. 79. Note 2 on page 37S/225, to this sentence, provides: "Cf. Articles III:2 and 4 and II:4".

[39]DS17/R, adopted 18 February 1992, 39S/27, 79-80, para. 5.15.

[40]*Ibid.,* 39S/83, paras. 5.23-5.24.

In the 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" the Panel found that listing and delisting requirements maintained by liquor stores operated by certain US states fell under Article III:4.[41]

See also the Note *Ad* Article XVII:1.

(8) Mandatory versus discretionary legislation; non-enforcement

The 1987 Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances" examined excise taxes on imported petroleum and certain imported chemical substances ("Superfund taxes"), which had been enacted as a revenue source for the US "Superfund" hazardous-waste cleanup program. The tax on certain imported substances, enacted in October 1986, provided that it would not enter into effect until 1 January 1989; regulations implementing it had not been drafted or put into effect.

> "The Panel noted that the United States objected to an examination of this tax because it did not go into effect before 1 January 1989, and - having no immediate effect on trade and therefore not causing nullification or impairment - fell outside the framework of Article XXIII. The Panel examined this point and concluded the following.
>
> "... The general prohibition of quantitative restrictions under Article XI ... and the national treatment obligation of Article III ... have essentially the same rationale, namely to protect expectations of the contracting parties as to the competitive relationship between their products and those of the other contracting parties. Both articles are not only to protect current trade but also to create the predictability needed to plan future trade. That objective could not be attained if contracting parties could not challenge existing legislation mandating actions at variance with the General Agreement until the administrative acts implementing it had actually been applied to their trade. Just as the very existence of a regulation providing for a quota, without it restricting particular imports, has been recognized to constitute a violation of Article XI:1, the very existence of mandatory legislation providing for an internal tax, without it being applied to a particular imported product, should be regarded as falling within the scope of Article III:2, first sentence. The Panel noted that the tax on certain imported substances had been enacted, that the legislation was mandatory and that the tax authorities had to apply it after the end of next year and hence within a time frame within which the trade and investment decisions that could be influenced by the tax are taken. The Panel therefore concluded that Canada and the EEC were entitled to an investigation of their claim that this tax did not meet the criteria of Article III:2, first sentence."[42]

The 1987 Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances" also examined, with respect to the tax on certain imported substances, the requirement that importers supply sufficient information regarding the chemical inputs of taxable substances to enable the tax authorities to determine the amount of tax to be imposed; otherwise a penalty tax would be imposed in the amount of five per cent ad valorem, or a different rate to be prescribed by the Secretary of the Treasury which would equal the amount that would be imposed if the substance were produced using the predominant method of production. The Panel noted concerning the penalty rate:

> "... the Superfund Act permits the Secretary of the Treasury to prescribe by regulation, in lieu of the 5 per cent rate, a rate which would equal the amount that would be imposed if the substance were produced using the predominant method of production.... These regulations have not yet been issued. Thus, whether they will eliminate the need to impose the penalty tax and whether they will establish complete equivalence between domestic and imported products, as required by Article III:2, first sentence, remain open questions. From the perspective of the overall objectives of the General Agreement it is regrettable that the Superfund Act explicitly directs the United States tax authorities to impose a tax inconsistent with the national treatment principle but, since the Superfund Act also gives them the possibility to avoid the need to impose that tax by issuing regulations, the existence of the penalty rate

[41]DS23/R, adopted 19 June 1992, 39S/206, 291-293, paras. 5.62-5.69.
[42]L/6175, adopted 17 June 1987, 34S/136, 160, paras. 5.2.1-5.2.2.

provisions as such does not constitute a violation of the United States obligations under the General Agreement. The Panel noted with satisfaction the statement of the United States that, given the tax authorities' regulatory authority under the Act, 'in all probability the 5 per cent penalty rate would never be applied'".[43]

In the 1990 Panel Report on "EEC - Regulation on Imports of Parts and Components" the Panel also examined an argument of Japan concerning the anti-circumvention provision in the EEC anti-dumping legislation:

"Japan considers not only the measures taken under the anticircumvention provision but also the provision itself to be violating the EEC's obligations under the General Agreement. Japan therefore asked the Panel to recommend to the CONTRACTING PARTIES that they request the EEC not only to revoke the measures taken under the provision but also to withdraw the provision itself. The Panel therefore examined whether the mere existence of the anti-circumvention provision is inconsistent with the General Agreement. The Panel noted that the anti-circumvention provision does not mandate the imposition of duties or other measures by the EEC Commission and Council; it merely authorizes the Commission and the Council to take certain actions. Under the provisions of the General Agreement which Japan claims to have been violated by the EEC contracting parties are to avoid certain measures; but these provisions do not establish the obligation to avoid legislation under which the executive authorities may possibly impose such measures. ...

"In the light of the above the Panel found that the mere existence of the anti-circumvention provision in the EEC's anti-dumping Regulation is not inconsistent with the EEC's obligations under the General Agreement. Although it would, from the perspective of the overall objectives of the General Agreement, be desirable if the EEC were to withdraw the anti-circumvention provision, the EEC would meet its obligations under the General Agreement if it were to cease to apply the provision in respect of contracting parties".[44]

The 1990 Panel Report on "Thailand - Restrictions on Importation of and Internal Taxes on Cigarettes" examined, *inter alia*, whether excise taxes which could be levied by Thai authorities on foreign cigarettes, as well as the exemption from Thai business and municipal taxes accorded in respect of cigarettes made from domestic leaf, were consistent with Article III. While the ceiling tax rates permitted under law were higher for imported than for domestic cigarettes, and the tax rate applied until 11 July 1990 varied in proportion to foreign tobacco content, the Thai Ministry of Finance had issued a regulation on 11 July 1990 to provide a uniform excise tax rate for all cigarettes. On 18 August 1990 Thailand modified its regulations to exempt all cigarettes from business and municipal taxes.

"... The United States argued that it was not sufficient under Article III for the rates effectively levied to be the same; the maximum rates that could be levied under the legislation also had to be non-discriminatory. The Panel noted that previous panels had found that legislation mandatorily requiring the executive authority to impose internal taxes discriminating against imported products was inconsistent with Article III:2, whether or not an occasion for its actual application had as yet arisen; legislation merely giving the executive the possibility to act inconsistently with Article III:2 could not, by itself, constitute a violation of that provision.[45] The Panel agreed with the above reasoning and found that the possibility that the Tobacco Act might be applied contrary to Article III:2 was not sufficient to make it inconsistent with the General Agreement.[46]

"... The Panel observed that the new Thai measure, by eliminating business and municipal taxes on cigarettes, removed the internal taxes imposed on imported cigarettes in excess of those applied to

[43] *Ibid.,* 34S/163-164, para. 5.2.9.

[44] L/6657, adopted 16 May 1990, 37S/132, 198-199, para. 5.25-5.26.

[45] A footnote to this paragraph refers to Report of the Panel on "EEC - Regulation on Imports of Parts and Components" (L/6657 at paragraph 5.25, adopted on 16 May 1990). Report of the panel on "United States - Taxes on Petroleum and Certain Imported Substances" (BISD 34S/160, 164, adopted on 17 June 1987).

[46] DS10/R, adopted on 7 November 1990, 37S/200, 227, para. 84.

domestic cigarettes. The Panel noted that, as in the case of the excise tax, the Tobacco Act continued to enable the executive authorities to levy the discriminatory taxes. However, the Panel, recalling its findings on the issue of excise taxes, found that the possibility that the Tobacco Act might be applied contrary to Article III:2 was, by itself, not sufficient to make it inconsistent with the General Agreement."[47]

The Panel concluded that "The current regulations relating to the excise, business and municipal taxes on cigarettes are consistent with Thailand's obligations under Article III of the General Agreement".[48]

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" examined arguments that certain legislation, while it might be mandatory, was not actually being enforced. With respect to legislation exempting local producers from requirements to distribute through wholesalers, which the Panel ruled was inconsistent with Article III:4 (see page 178):

"The Panel then proceeded to consider the United States argument that the provisions in the state of Illinois permitting manufacturers to sell directly to retailers were not given effect. In this regard, the Panel recalled the decisions of the CONTRACTING PARTIES on the relevance of the non-application of laws in dispute. Recent panels addressing the issue of mandatory versus discretionary legislation in the context of both Articles III:2 and III:4[49] concluded that legislation mandatorily requiring the executive authority to take action inconsistent with the General Agreement would be inconsistent with Article III, whether or not the legislation were being applied, whereas legislation merely giving the executive authority the possibility to act inconsistently with Article III would not, by itself, constitute a violation of that Article. The Panel agreed with the above reasoning and concluded that because the Illinois legislation in issue allows a holder of a manufacturer's license to sell beer to retailers, without allowing imported beer to be sold directly to retailers, the legislation mandates governmental action inconsistent with Article III:4".[50]

With respect to the local option law in the state of Mississippi, which the Panel found to be inconsistent with Article III:4 (see page 178):

"The Panel then proceeded to consider the United States argument that the Mississippi law was not being applied. In this regard, the Panel recalled its previous discussion of this issue. ... The Panel noted that the option law in Mississippi provides discretion only for the reinstatement of prohibition, but not for the discriminatory treatment of imported wines. The Panel concluded, therefore, that because the Mississippi legislation in issue, which permits native wines to be sold in areas of the state which otherwise prohibit the sale of alcoholic beverages, including imported wine, mandates governmental action inconsistent with Article III:4, it is inconsistent with that provision whether or not the political subdivisions are currently making use of their power to reinstate prohibition".[51]

With respect to the Massachusetts and Rhode Island "price affirmation" (maximum price) laws:

"In respect of the United States contention that the Massachusetts measure was not being enforced and that the Rhode Island measure was only nominally enforced, the Panel recalled its discussion of mandatory versus discretionary laws in the previous section. The Panel noted that the price affirmation measures in both Massachusetts and Rhode Island are mandatory legislation. Even if Massachusetts may not currently be using its police powers to enforce this mandatory legislation, the measure continues to be mandatory legislation which may influence the decisions of economic operators. Hence, a non-enforcement of a mandatory law in respect of imported products does not ensure that imported beer and wine are not treated less favourably than like domestic products to which the law does not apply. Similarly, the contention that

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[47]*Ibid.*, 37S/227 para. 86.

[48]*Ibid.*, 37S/228 para. 88.

[49]Note 11 to this paragraph refers to the Report of the Panel on "Thailand - Restrictions on Importation of and Internal Taxes on Cigarettes", adopted on 7 November 1990, BISD 37S/200, 227; Report of the Panel on "EEC - Regulation on Imports of Parts and Components", adopted on 16 May 1990, BISD 37S/132, 198; and Report of the Panel on "United States - Taxes on Petroleum and Certain Imported Substances", adopted on 17 June 1987, BISD 34S/136, 160.

[50]DS23/R, adopted 19 June 1992, 39S/206, 281-282, para. 5.39.

[51]*Ibid.,* 39S/289, para. 5.57.

Rhode Island only 'nominally' enforces its mandatory legislation a fortiori does not immunize this measure from Article III:4. The mandatory laws in these two states by their terms treat imported beer and wine less favourably than the like domestic products. Accordingly, the Panel found that the mandatory price affirmation laws in Massachusetts and Rhode Island are inconsistent with Article III:4, irrespective of the extent to which they are being enforced".[52]

See also the material on discretionary legislation, measures not yet in effect, and measures no longer in effect, under Article XXIII.

2. Interpretative Note Ad Article III: measures imposed at the time or point of importation

(1) "collected or enforced ... at the time or point of importation"

The Interpretative Note *ad* Article III was added at Havana. It makes clear that the mere fact that an internal charge or regulation is collected or enforced in the case of the imported product at the time or point of importation does not prevent it from being an "internal tax or other internal charge" and from being subject to the provisions of Article III. During discussions at Havana on the proposal to add the Note, it was stated that "the proposed additional paragraph was intended to cover cases where internal excise taxes were, for administrative reasons, collected at the time of importation, as well as 'mixing' regulations also enforced at that stage".[53] The Report of Sub-Committee A of the Third Committee at the Havana Conference, which considered Article 18 of the Charter (on national treatment), states as follows:

"The delegations of Chile, Lebanon, and Syria inquired whether certain charges imposed by their countries on imported products would be considered as internal taxes under Article 18. The Sub-Committee, while not attempting to give a general definition of internal taxes, considered that the particular charges referred to are import duties and not internal taxes because according to the information supplied by the countries concerned (a) they are collected at the time of, and as a condition to, the entry of the goods into the importing country, and (b) they apply exclusively to imported products without being related in any way to similar charges collected internally on like domestic products. The fact that these charges are described as internal taxes in the laws of the importing country would not in itself have the effect of giving them the status of internal taxes under the Charter".[54]

See also the discussion of border tax adjustments below at page 144.

The 1978 Panel Report on "EEC - Measures on Animal Feed Proteins" examined an EEC scheme requiring importers and producers of vegetable proteins to purchase and denature surplus skimmed milk powder from EEC intervention stocks. The scheme allowed persons subject to this requirement to provide a security deposit or a bank guarantee instead of documents providing proof of the purchase and the denaturing of the skimmed milk powder; the deposit or guarantee was refunded interest-free upon presentation of the required documents but forfeited otherwise. The Panel examined the argument that this security deposit scheme was a charge enforced at the border under Article II:2(a) and the Note *ad* Article III.

"The Panel was of the opinion that the security deposit was not of a fiscal nature because, if it had been, it would have defeated the stated purpose of the EEC Regulation which was to increase utilization of denatured skimmed milk powder. In addition the revenue from the security deposit accrued to EEC budgetary authorities only when the buyer of vegetable proteins had not fulfilled the purchase obligations. The Panel further noted that less than 1 per cent of the security deposits paid, were not released, indicating compliance with the purchase obligation. The Panel therefore considered that the security deposit, including

[52]*Ibid.*, 39S/290, para. 5.60; see also similar finding with respect to non-enforcement of New Hampshire statute requiring preferential treatment for listing of wine manufactured or bottled in New Hampshire, *ibid.*, 39S/292, para. 5.66.

[53]E/CONF.2/C.3/SR.11 p. 1; proposal at E/CONF.2/C.3/1/Add.21. See also E/CONF.2/C.3/A/W.33, p. 1.

[54]Havana Reports, p. 62, para. 42; E/CONF.2/C.3/A/W.30, p. 2. The text of Article 18 as amended at Havana was taken into the General Agreement; see the discussion of negotiating history in section III below.

any associated cost, was only an enforcement mechanism for the purchase requirement and, as such, should be examined with the purchase obligation."[55]

The 1983 Panel Report on "United States - Imports of Certain Automotive Spring Assemblies" notes the view of Canada that "The institution of a bonding requirement, pursuant to Section 337 [of the Tariff Act of 1930] was applied to imports but did not apply to like domestic products and was thus inconsistent with the requirements of Article III:1 and 2. Even if the bonding requirement did not contravene Article III because it was a border measure as contended by the United States delegation, it would still contravene Article II:1(b), the last sentence of which had to be read in conjunction with paragraph 2 of the same Article"[56] and the view of the United States that "as a matter of GATT interpretation ... Article III:2 would not apply to temporary bonding requirements imposed as a condition of importation".[57] The Panel found Article XX(d) to apply and "considered that an examination of the United States action in the light of the other GATT provisions referred to ... above was not required".[58] The same statute was again examined in the 1989 panel decision on "United States - Section 337 of the Tariff Act of 1930".[59]

In the 1990 Panel Report on "EEC - Regulation on Imports of Parts and Components," the Panel examined the argument of the EEC that the anti-circumvention duties at issue were customs or other duties imposed "on or in connection with importation" under Article II:1(b), or internal taxes or charges falling under Article III:2. See the excerpts from this report below at page 200.[60]

(2) "which applies to an imported product and to the like domestic product"

The 1991 Panel Report on "United States - Restrictions on Imports of Tuna," which has not been adopted, examined the United States prohibition of imports of tuna and tuna products from Mexico under the provisions of the US Marine Mammal Protection Act (MMPA) relating to fishing of yellowfin tuna in the Eastern Tropical Pacific Ocean (ETP).

> "The Panel noted that Mexico had argued that the measures prohibiting imports of certain yellowfin tuna and yellowfin tuna products from Mexico imposed by the United States were quantitative restrictions on importation under Article XI, while the United States had argued that these measures were internal regulations enforced at the time or point of importation under Article III:4 and the Note Ad Article III, namely that the prohibition of imports of tuna and tuna products from Mexico constituted an enforcement of the regulations of the MMPA relating to the harvesting of domestic tuna.
>
> "The Panel examined the distinction between quantitative restrictions on importation and internal measures applied at the time or point of importation, and noted the following. While restrictions on importation are prohibited by Article XI:1, contracting parties are permitted by Article III:4 and the Note Ad Article III to impose an internal regulation on products imported from other contracting parties provided that it: does not discriminate between products of other countries in violation of the most-favoured-nation principle of Article I:1; is not applied so as to afford protection to domestic production, in violation of the national treatment principle of Article III:1; and accords to imported products treatment no less favourable than that accorded to like products of national origin, consistent with Article III:4. ...
>
> "The Panel noted that the United States had claimed that the direct import embargo on certain yellowfin tuna and certain yellowfin tuna products of Mexico constituted an enforcement at the time or point of importation of the requirements of the MMPA that yellowfin tuna in the ETP be harvested with fishing techniques designed to reduce the incidental taking of dolphins. The MMPA did not regulate tuna products as such, and in particular did not regulate the sale of tuna or tuna products. Nor did it prescribe fishing techniques that could have an effect on tuna as a product. This raised in the Panel's view the question of

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[55] L/4599, adopted on 14 March 1978, 25S/49, 64, para. 4.4.
[56] L/5333, adopted on 26 May 1983 subject to an understanding (C/M/168), 30S/107, 119, para. 35.
[57] *Ibid.*, 30S/123, para. 46.
[58] *Ibid.*, 30S/126, para. 61.
[59] L/6439, adopted on 7 November 1989, 36S/345.
[60] L/6657, adopted on 16 May 1990, 37S/132, 192-93, paras. 5.5-5.8.

whether the tuna harvesting regulations could be regarded as a measure that 'applies to' imported and domestic tuna within the meaning of the Note Ad Article III and consequently as a measure which the United States could enforce consistently with that Note in the case of imported tuna at the time or point of importation. The Panel examined this question in detail and found the following.

"The text of Article III:1 refers to the application to imported or domestic products of laws, regulations and requirements affecting the internal sale … of products and internal quantitative regulations requiring the mixture, processing or use of products; it sets forth the principle that such regulations on products not be applied so as to afford protection to domestic production. Article III:4 refers solely to laws, regulations and requirements affecting the internal sale, etc. of products. This suggests that Article III covers only measures affecting products as such. …

"A previous panel had found that Article III:2, first sentence, 'obliges contracting parties to establish certain competitive conditions for imported *products* in relation to domestic *products*'.[61] Another panel had found that the words 'treatment no less favourable' in Article III:4 call for effective equality of opportunities for imported *products* in respect of the application of laws, regulations or requirements affecting the sale, offering for sale, purchase, transportation, distribution or use of *products*, and that this standard has to be understood as applicable to each individual case of imported *products*.[62] It was apparent to the Panel that the comparison implied was necessarily one between the measures applied to imported products and the measures applied to like domestic products. …

"The Panel considered that, as Article III applied the national treatment principle to both regulations and internal taxes, the provisions of Article III:4 applicable to regulations should be interpreted taking into account interpretations by the CONTRACTING PARTIES of the provisions of Article III:2 applicable to taxes. The Panel noted in this context that the Working Party Report on Border Tax Adjustments, adopted by the CONTRACTING PARTIES in 1970, had concluded that

> '… there was convergence of views to the effect that taxes directly levied on products were eligible for tax adjustment … Furthermore, the Working Party concluded that there was convergence of views to the effect that certain taxes that were not directly levied on products were not eligible for adjustment, [such as] social security charges whether on employers or employees and payroll taxes'.

Thus, under the national treatment principle of Article III, contracting parties may apply border tax adjustments with regard to those taxes that are borne by products, but not for domestic taxes not directly levied on products (such as corporate income taxes). Consequently, the Note Ad Article III covers only internal taxes that are borne by products. The Panel considered that it would be inconsistent to limit the application of this Note to taxes that are borne by products while permitting its application to regulations not applied to the product as such.

"The Panel concluded from the above considerations that the Note Ad Article III covers only those measures that are applied to the product as such. The Panel noted that the MMPA regulates the domestic harvesting of yellowfin tuna to reduce the incidental taking of dolphin, but that these regulations could not be regarded as being applied to tuna products as such because they would not directly regulate the sale of tuna and could not possibly affect tuna as a product. Therefore, the Panel found that the import prohibition on certain yellowfin tuna and certain yellowfin tuna products of Mexico and the provisions of the MMPA under which it is imposed did not constitute internal regulations covered by the Note Ad Article III."[63]

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[61]The footnote to this sentence refers to the Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances", adopted on 17 June 1987, 34S/136, 158, para. 5.1.9.

[62]The footnote to this sentence refers to the Panel Report on "United States - Section 337 of the Tariff Act of 1930", adopted on 7 November 1989, 36S/345, 386-7, paras. 5.11, 5.14.

[63]DS21/R (unadopted) dated 3 September 1991, 39S/155, 193-195, paras. 5.8-5.14.

See also the references to this report at pages 164 and 175; in this connection see also the unadopted Panel Report of 1994 on "United States - Restrictions on Imports of Tuna"[64] and the related findings in the unadopted Panel Report of 1994 on "United States - Taxation of Automobiles".[65]

3. Paragraph 1

(1) "should not be applied to imported or domestic products so as to afford protection to domestic production"

The 1978 Panel Report on "EEC - Measures on Animal Feed Proteins" examined an EEC scheme requiring domestic producers or importers of oilseeds, cakes and meals, dehydrated fodder and compound feeds and importers of corn gluten feed to purchase a certain quantity of surplus skimmed milk powder held by intervention agencies and to have it denatured for use as feed for animals other than calves. The Panel, having concluded that these vegetable proteins and skimmed milk powder were substitutable in terms of their final use (see page 160), noted as follows.

> "... The Panel ... considered that the EEC Regulation was an 'internal quantitative regulation' in the sense of Article III:5. However, the Panel found that this 'internal quantitative regulation' as such was not related to "the mixture, processing or use ... in specified amounts or proportions" within the meaning of Article III:5 because, at the level of its application, the EEC Regulation introduced basically an obligation to purchase a certain quantity of skimmed milk powder and the purchase obligation falls under Article III:1.
>
> "Given the reference in Article III:5, second sentence, to Article III:1, the Panel then examined the consistency of the EEC Regulation as an internal quantitative regulation with provisions of Article III:1, particularly as to whether the Regulation afforded protection to domestic production. The Panel noted that the EEC Regulation considered, in its own terms, that denatured skimmed milk powder was an important source of protein which could be used in feedingstuffs. The Panel also noted that surplus stocks could originate either from domestic production or imports, but that the intervention agencies from which the buyers of vegetable proteins had to purchase a certain quantity of denatured skimmed milk powder only held domestically produced products. The Panel further noted that, although globally about 15 per cent of the EEC apparent consumption of vegetable protein was supplied from domestic sources, not all the individual products subject to the EEC measures were produced domestically in substantial quantities.
>
> "The Panel concluded that the measures provided for by the Regulation with a view to ensuring the sale of a given quantity of skimmed milk powder protected this product in a manner contrary to the principles of Article III:1 and to the provisions of Article III:5, second sentence."[66]

During the discussion in the Council of the 1981 Panel Report on "Spain - Measures concerning Domestic Sale of Soyabean Oil"[67] many contracting parties stated that neither the language of Article III nor past interpretations of that provision supported an interpretation that internal regulations which protect domestic production must have restrictive effects on directly competitive or substitutable products in order to be found contrary to Article III:1. Some representatives also noted that adverse effects could not only be measured by direct effects on import volume in the country maintaining the measure but could manifest themselves as well by other trade distorting consequences, including possible suppression of growth of trade. The Council took note of this panel report and of the statements made concerning it, and did not adopt the report.[68]

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[64]DS29/R, dated 16 June 1994, paras.5.8-5.10.
[65]DS31/R, dated 11 October 1994, paras. 5.51-5.55.
[66]L/4599, adopted 14 March 1978, 25S/49, 64-65, paras. 4.6-4.8.
[67]L/5142 and Corr.1, dated 17 June 1981, unadopted.
[68]C/M/152 p. 7-19; L/5161, L/5188.

The 1987 Panel Report on "Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages" examined, *inter alia*, the application of Article III:1.

> "... The Panel noted that, whereas under the first sentence of Article III:2 the tax on the imported product and the tax on the like domestic product had to be equal in effect, Article III:1 and 2, second sentence, prohibited only the application of internal taxes to imported or domestic products in a manner 'so as to afford protection to domestic production'. The Panel was of the view that also small tax differences could influence the competitive relationship between directly competing distilled liquors, but the existence of protective taxation could be established only in the light of the particular circumstances of each case and there could be a *de minimis* level below which a tax difference ceased to have the protective effect prohibited by Article III:2, second sentence. ... Since it has been recognized in GATT practice that Article III:2 protects expectations on the competitive relationship between imported and domestic products rather than expectations on trade volumes (see L/6175, paragraph 5.1.9), the Panel did not consider it necessary to examine the quantitative trade effects of this considerably different taxation for its conclusion that the application of considerably lower internal taxes by Japan on shochu than on other directly competitive or substitutable distilled liquors had trade-distorting effects affording protection to domestic production of shochu contrary to Article III:1 and 2, second sentence."[69]

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" notes as follows.

> "The Panel began its examination with Canada's claim that the application of a lower rate of federal excise tax on domestic beer from qualifying (small) United States producers, which lower rate was not available to imported beer, was inconsistent with Articles III:1 and III:2 of the General Agreement. The Panel noted that because Article III:1 is a more general provision than either Article III:2 or III:4, it would not be appropriate for the Panel to consider Canada's Article III:1 allegations to the extent that the Panel were to find United States measures to be inconsistent with the more specific provisions of Articles III:2 and III:4."[70]

The same Panel examined the argument that laws in certain states restricting the points of sale, distribution and labelling of beer above a certain per cent of alcohol by weight contravened Articles III:1 and III:4. Having found that low alcohol beer and high alcohol beer need not be considered as ' like products' in terms of Article III:4 (see page 171):

> "The Panel ... proceeded to examine whether the laws and regulations in the above-mentioned states affecting the alcohol content of beer are applied to imported or domestic beer so as to afford protection to domestic production in terms of Article III:1. In this context, the Panel recalled its finding in paragraph 5.74 regarding the alcohol content of beer and concluded that the evidence submitted to it does not indicate that the distinctions made in the various states with respect to the alcohol content of beer are applied so as to favour domestic producers over foreign producers. Accordingly, the Panel found that the restrictions on points of sale, distribution and labelling based on the alcohol content of beer maintained by the states of Alabama, Colorado, Florida, Kansas, Minnesota, Missouri, Oklahoma, Oregon and Utah are not inconsistent with Article III:1".[71]

With regard to the interpretation of paragraph 1 in the context of the second sentence of paragraph 2, see below under "a directly competitive or substitutable product" (page 159 and following). See also the discussion of this provision in the context of paragraph 5 of Article III.

See also the excerpt from the Working Party Report on "Brazilian Internal Taxes" above at page 128; see also above under "purpose of Article III".

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[69] L/6216, adopted on 10 November 1987, 34S/83, 122-123, para. 5.11.
[70] DS23/R, adopted 19 June 1992, 39S/206, 270, para. 5.2.
[71] *Ibid.*, 39S/295, para. 5.76.

(2) Note Ad paragraph 1: Application of paragraph 1 to internal taxes imposed by local governments and authorities

See above at page 130.

The Panel Report on "Canada - Measures Affecting the Sale of Gold Coins," which has not been adopted, examined the application of a retail sales tax on gold coins by the Province of Ontario, and the question of whether the Canadian federal government had, as required by Article XXIV:12, taken "such reasonable measures as may be available to it to ensure observance of the provisions of [the General Agreement]" by Ontario.

> "The Panel ... examined what meaning should be given to the term 'reasonable'. The Panel noted that the only indication in the General Agreement of what was meant by 'reasonable' was contained in the interpretative note to Article III:1, which defined the term 'reasonable measures' for the case of national legislation authorizing local governments to impose taxes. According to this note the question of whether the repeal of such enabling legislation would be a reasonable measure required by Article XXIV:12 should be answered by taking into account the spirit of the inconsistent local tax laws, on the one hand, and the administrative or financial difficulties to which the repeal of the enabling legislation would give rise, on the other. The basic principle embodied in this note is, in the view of the Panel, that in determining which measures to secure the observance of the provisions of the General Agreement are 'reasonable' within the meaning of Article XXIV:12, the consequences of their non-observance by the local government for trade relations with other contracting parties are to be weighed against the domestic difficulties of securing observance. While recognizing that this note refers to the case of national enabling legislation, the Panel considered that the basic principle embodied therein was applicable to the present case."[72]

4. Paragraph 2: internal taxes or other internal charges of any kind

(1) "directly or indirectly"

In initial discussions at the London session of the Preparatory Committee, it was suggested that while this phrase in the US Draft Charter referred to "taxes and other internal charges imposed on or in connection with like products", the rapporteurs in the Working Party on Technical Articles had used the phrase 'directly or indirectly' instead, owing to the difficulty of obtaining the exact equivalent in the French text.[73] In later discussions in Commission A at the London session of the Preparatory Committee, it was stated that the word "indirectly" would cover even a tax not on a product as such but on the processing of the product.[74]

(2) "internal taxes"

(a) Excise taxes, indirect taxes and consumption taxes

It was stated during discussions in the Third Committee at the Havana Conference that "the provisions relating to internal taxes were not designed to limit the degree of protection, but merely to determine the form which that protection should take. Any country was free to replace internal taxes by import tariffs which were subject to the negotiations referred to in Article 17. There was no general binding or limitations on tariffs as such".[75]

The 1987 Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances" examined excise taxes on imported petroleum and certain imported chemical substances ("Superfund taxes"), which had been enacted as a revenue source for the US "Superfund" hazardous-waste cleanup program.

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[72] L/5863, para. 69.
[73] Proposal by UK, EPCT/C.II/11; discussion at EPCT/C.II/W.5, p. 5.
[74] EPCT/A/PV/9 p. 19; EPCT/W/181, p. 3.
[75] E/CONF.2/C.3/SR.11, p. 3; Article 17 was the Charter article on multilateral trade negotiations, some elements of which were incorporated into Article XXVIIIbis.

"The Panel examined the tax on petroleum in the light of the obligations the United States assumed under the General Agreement and found the following: The tax on petroleum is an excise tax levied on imported and domestic goods. Such taxes are subject to the national treatment requirement of Article III:2, first sentence, which reads: 'The products of the territory of any contracting party imported into the territory of any other contracting party shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products'."[76]

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" examined, inter alia, excise taxes on beer and wine at the federal and state level in the United States, and the relationship between exemptions granted from such taxes and the exception in Article III:8(b): see below at page 195.

(b) Fiscal measures versus enforcement measures

The Panel Report on "United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco" examined a claim that the penalty provisions of the Domestic Marketing Assessment ("DMA") under Section 1106(a) of the US 1993 Budget Act, and rules of the U.S. Department of Agriculture ("USDA"), were inconsistent with the first sentence of Article III:2. These provisions, consisting of a nonrefundable marketing assessment and a requirement to purchase additional quantities of domestic burley and flue-cured tobacco, were applicable where a domestic manufacturer failed to provide a required certification of the percentage of domestically-produced tobacco used by it to produce cigarettes each year, or to use annually a minimum of 75 per cent domestic tobacco in the manufacture of cigarettes.

"In the Panel's view, the Article III:2 claim raised the question of whether the DMA's penalty provisions were separate fiscal measures or enforcement measures for the domestic content requirement of the DMA. The Panel noted in this regard that previous panels, consistent with the practice of international tribunals, had refrained from engaging in an independent interpretation of domestic laws, and had treated the interpretation of such laws as questions of fact.[77] The Panel considered that it should approach its analysis of the complainants' Article III:2 claims in conformity with this practice and, therefore, to treat the interpretation of Section 1106(a) of the 1993 Budget Act as a question of fact. As the basis for such an analysis, the Panel considered that it should seek guidance from the manner in which the United States, as author of the legislation, itself interpreted these provisions.

"The Panel considered as significant that the subsection of the DMA provision which set forth the additional marketing assessment and purchase requirements was entitled 'Penalties'. Thus, the ordinary meaning of the title of the provision suggested to the Panel that the additional assessment and purchase requirements were treated under U.S. domestic law as penalties, not as separate fiscal measures.

"The Panel recalled once again that the DMA provision, in relevant part, read as follows:

'*PENALTIES*. In General. Subject to subsection (f), a domestic manufacturer of cigarettes that has failed, as determined by the Secretary after notice and opportunity for a hearing, to use in the manufacture of cigarettes during a calendar year a quantity of tobacco grown in the United States that is at least 75 per cent of the total quantity of tobacco used by the manufacturer or to comply with subsection (a) [certification requirement], shall be subject to the requirements of subsections (c) [*nonrefundable marketing assessment*], (d) [*purchase of additional quantities of domestic burley tobacco*] and (e) [*purchase of additional quantities of domestic flue-cured tobacco*]'. *(emphasis added)*

[76] L/6175, adopted on 17 June 1987, 34S/136, 154, para. 5.1.1.

[77] The footnote to this sentence in the panel report provides: "See, *e.g.*, report of the panel on United States - Measures Affecting Alcoholic and Malt Beverages, adopted on 19 June 1992, BISD 39S/206, 284-287, 296-297".

"The Panel further recalled that USDA's Proposed Rules implementing Section 1106(a) of the 1993 Budget Act set out the penalty provisions under Section 723.502(b), entitled "Failure to Comply". The text of these Proposed Rules provided the following:

> 'Each domestic manufacturer of cigarettes who *fails to comply* with the requirements of this section *shall pay* a domestic marketing assessment and *shall purchase* loan stocks of tobacco in accordance with Sections 723.503 and 723.504'.[78] *(emphasis added)*

"The Panel noted in addition that the text accompanying the Proposed Rules suggested that the additional marketing assessment and purchase requirements were in the nature of penalties. For example, the Panel noted that the following explanation was provided:

> 'Section 320C(c) of the Act provides that *if the quantity of imported tobacco* used by a domestic manufacturer for making cigarettes for the year *exceeds 25 per cent, such manufacturer must pay a domestic marketing assessment* on each pound of imported tobacco used in excess of 25 per cent. In addition, as provided in section 320C(d) and (e), *such manufacturer must purchase tobacco* from the existing burley and flue-cured tobacco inventories of producer owned cooperative marketing associations in an amount equal to the weight of imported tobacco used in excess of 25 per cent'.[79] *(emphasis added)*

"The accompanying text further provided:

> 'Where a domestic content *violation* has occurred, the *compensatory* purchases of tobacco ... must be from the inventories of producer owned cooperative marketing associations that handle price support loans for tobacco'.[80] *(emphasis added)*

"It was thus the Panel's understanding that the U.S. Government treated these DMA provisions as penalty provisions for the enforcement of a domestic content requirement for tobacco, not as separate fiscal measures, and that such interpretation corresponded to the ordinary meaning of the terms used in the relevant statute and proposed rules. Further, it appeared that these penalty provisions had no separate *raison d'être* in the absence of the underlying domestic content requirement. The above factors suggested to the Panel that it would not be appropriate to analyze the penalty provisions separately from the underlying domestic content requirement.

"The Panel further noted that prior panel decisions also supported the view that the additional marketing assessment and purchase requirements should be treated as enforcement measures, and not be analyzed separately as internal charges. The Panel recalled that one such panel, in examining a regulation according to which buyers of vegetable proteins had the possibility of providing a security as an alternative to the required purchase of a certain quantity of skimmed milk powder, had determined that the security deposit was not a fiscal measure because, *inter alia,*

> 'the revenue from the security deposit accrued to EEC budgetary authorities only when the buyer of vegetable proteins had not fulfilled the purchase obligation. The Panel therefore considered that the security deposit, including any associated cost, was only an enforcement mechanism for the purchase requirement and, as such, should be examined with the purchase obligation'.[81]

"In a similar vein, another more recent panel had first examined the underlying measure at issue (differing systems for the internal distribution of imported and domestic beer), and considered it

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[78]The footnote to this sentence in the panel report refers to 59 Federal Register 1493, 1497 (11 January 1994).
[79]The footnote to this sentence in the panel refers to 59 Federal Register 1493, 1495 (11 January 1994).
[80]The footnote to this sentence in the panel report refers to 59 Federal Register 1493, 1495 (11 January 1994).
[81]The footnote to this paragraph in the panel report provides: "Report of the panel on EEC - Measures on Animal Feed Proteins, adopted on 14 March 1978, BISD 25S/49, 64. See also report of the panel on EEC - Programme of Minimum Import Prices, Licences and Surety Deposits for Certain Processed Fruits and Vegetables, adopted on 18 October 1978, BISD 25S/68, 98".

unnecessary to examine certain enforcement measures (charges on beer containers).[82] The Panel did not consider that there were any elements in the case before it which would justify a different approach from that adopted in these earlier cases.

"In view of the Panel's analysis in paragraphs 75-81 above, the Panel considered that the evidence did not support the complainants' claim that the DMA's penalty provisions were separate taxes or charges within the meaning of Article III:2.[83]

In this connection see also the unadopted Panel Report of 1994 on "United States - Taxes on Automobiles".[84]

(c) Income taxes, exemptions from income taxes and credits against income taxes

See also the material below at page 152 and under paragraph 8(b).

During discussions in Sub-Committee A of the Third Committee at the Havana Conference, which considered Article 18 of the Charter (on national treatment), it was stated that the sub-committee on Article 25 [XVI] "had implied that exemptions from income taxes would constitute a form of subsidy permissible under Article 25 [XVI] and therefore not precluded by Article 18." It was agreed that "neither income taxes nor import duties came within the scope of Article 18 [III] since this Article refers specifically to internal taxes on products".[85]

In October 1952, Austria brought a complaint that the Italian authorities granted a remission of income tax to firms that used domestically-produced ship's plate.[86]

The 1971 Working Party on the United States Temporary Import Surcharge held an exchange of views on the Job Development Tax Credit, a credit against United States income taxes which was allowed in the year that certain new capital equipment was placed in service, and was not allowed with respect to foreign-produced property ordered by the taxpayer while the import surcharge was in effect. Foreign-produced property was defined as property manufactured outside the US or property manufactured in the US with 50 per cent or more foreign components. Several members of the Working Party stated that the provision under which only goods of United States origin were eligible for the exemption from a direct tax was inconsistent with Article III of the GATT.[87]

In early 1987, the EEC brought a complaint concerning US income tax legislation passed in 1986 which, while eliminating provisions for certain tax credits and special depreciation for capital goods, permitted the temporary use of these provisions for passenger aircraft assembled in certain states of the US if ordered and delivered before a date in late 1986.[88]

(d) Border tax adjustments; border adjustment of taxes and charges

See paragraph 2(a) of Article II. See also the discussion of the Note *ad* Article III above.

The 1955 Report of Review Working Party II on Schedules and Customs Administration notes that during the Review Session of 1954-55, Germany (which at the time had a system of border tax adjustment for cascading internal indirect taxes) "proposed insertion of the following interpretative note to Article III:2:

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[82]The footnote to this sentence in the panel report refers to "Report of the panel on Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies, adopted on 18 February 1992, BISD 39S/27, 85".

[83]DS44/R, adopted on 4 October 1994, paras. 75-82.

[84]DS31/R, dated 11 October 1994, paras. 5.42-5.43.

[85]E/CONF.2/C.3/A/W/32, p. 1-2; statement repeated in Havana Reports, p. 63, para. 44. See also E/CONF.2/C.3/SR.13, p. 1.

[86]L/875; see SR.13/12, SR.15/17, SR.16/9, SR.17/5. The tax remission was extended for all purchases in May 1961: see SR.18/4.

[87]L/3575.

[88]L/6153, C/M/208, C/M/209.

"'the words 'internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products', as employed in the first sentence of paragraph 2, shall be construed to denote the overall charge, including the charges borne by like domestic products through being subjected to internal taxes or other internal charges at various stages of their production (charges borne by the raw materials, semifinished products, auxiliary materials, etc. incorporated in, and by the power consumed for the production of, the finished products)'.

"The Working Party considered the significance of the phrase 'internal taxes or other internal charges' in relation to taxes which are levied at various stages of production, and in particular whether the rule of national treatment would allow a government to tax imported products at a rate calculated to be the equivalent of the taxes levied at the various stages of production of the like domestic product or only at the rate of the tax levied at the last stage. Several representatives supported the former interpretation, while the representative of the United States, on the other hand, thought the reference to internal taxes covered only a tax levied on the final product competitive with the imported article. Against the latter view it was argued that that interpretation would establish a discrimination against countries which chose to levy taxes at various stages and in favour of those which levy a single turnover tax on finished products. Some other representatives were of the opinion that the equivalent of the taxes on the final product and on its components and ingredients would be permitted, but not taxes on power consumed in manufacture, etc. In view of these differences of opinion, the Working Party does not recommend the insertion of an interpretative note, it being understood that the principle of equality of treatment would be upheld in the event of a tax on imported products being challenged under the consultation or complaint procedure of the Agreement."[89]

The Working Party on "Border Tax Adjustments" in 1968-70 examined the tax adjustment practices of contracting parties, their trade effects and relevant provisions of the General Agreement, and in particular the changeover in certain countries from cascade tax systems to the value-added tax. The Working Party used the definition of border tax adjustments applied in the OECD: "any fiscal measures which put into effect, in whole or in part, the destination principle (i.e. which 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 and which 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)". The Working Party considered, on the import side, Articles II and III and on the export side, Article XVI; other articles deemed relevant included Articles I, VI and VII. The 1970 Report of the Working Party notes as follows:

"There was general agreement that the main provisions of the GATT represented the codification of practices which existed at the time these provisions were drafted, re-examined and completed. ...

"Most members argued that there seemed to have been a coherent approach when the relevant articles of the GATT were drafted and that there were no inconsistencies of substance between the different provisions even if the question of tax adjustments was dealt with in different articles. They added that the philosophy behind these provisions was the ensuring of a certain trade neutrality. ...

"The Working Party also noted that there were differences in the terms used in these articles, in particular with respect to the provisions regarding importation and exportation: for instance, the terms 'borne by' and 'levied on'. It was established that those differences in wording had not led to any differences in interpretation of the provisions. It was agreed that GATT principles on tax adjustment applied the principle of destination identically to imports and exports.

"It was further agreed that these provisions set maxima limits for adjustment (compensation) which were not to be exceeded, but below which each contracting party was free to differentiate in the degree of compensation applied, provided that such action was in conformity with other provisions of the General Agreement."[90]

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[89] L/329, adopted on 26 February 1955, 3S/205, 210-11, para. 10.

[90] L/3464, adopted on 2 December 1970, 18S/97, 99-100, paras. 8-11. See also documents L/3389 (Consolidated document on the

"On the question of eligibility of taxes for tax adjustment under the present rules, the discussion took into account the term 'directly or indirectly ...' (*inter alia* Article III:2). The Working Party concluded that there was convergence of views to the effect that taxes directly levied on products were eligible for tax adjustment. Examples of such taxes comprised specific excise duties, sales taxes and cascade taxes and the tax on value added. It was agreed that the TVA, regardless of its technical construction (fractioned collection), was equivalent in this respect to a tax levied directly - a retail or sales tax. Furthermore, the Working Party concluded that there was convergence of views to the effect that certain taxes that were not directly levied on products were not eligible for tax adjustment. Examples of such taxes comprised social security charges whether on employers or employees and payroll taxes.

"The Working Party noted that there was a divergence of views with regard to the eligibility for adjustment of certain categories of tax and that these could be sub-divided into

(a) 'Taxes occultes' which the OECD defined as consumption taxes on capital equipment, auxiliary materials and services used in the transportation and production of other taxable goods. Taxes on advertising, energy, machinery and transport were among the more important taxes which might be involved. It appeared that adjustment was not normally made for taxes occultes except in countries having a cascade tax;

(b) Certain other taxes, such as property taxes, stamp duties and registration duties ... which are not generally considered eligible for tax adjustment. Most countries do not make adjustments for such taxes ...

It was generally felt that while this area of taxation was unclear, its importance –as indicated by the scarcity of complaints reported in connexion with adjustment of taxes occultes –was not such as to justify further examination.

"The Working Party noted that there were some taxes which, while generally considered eligible for adjustment, presented a problem because of the difficulty of calculating exactly the amount of compensation. Examples of such difficulties were encountered in cascade taxes. ... Other examples included composite goods which, on export, contained ingredients for which the Working Party agreed in principle it was administratively sensible and sufficiently accurate to rebate by average rates for a given class of goods.

"It was generally agreed that countries adjusting taxes should, at all times, be prepared, if requested, to account for the reasons for adjustment, for the methods used, for the amount of compensation and to furnish proof thereof."[91]

Based on the recommendations of this Working Party the Council introduced a notification procedure on a provisional basis in December 1970, whereby contracting parties would report changes in their tax adjustments. The notifications are to report any major changes in tax adjustment legislation and practices involving international trade, and bring periodically up to date the information contained in the consolidated document on contracting parties' practices (L/3389) on tax adjustments drawn up in the course of the Working Party's work. Notifications under this procedure are currently distributed as addenda to document L/3518.[92]

The 1987 Panel Report on "Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages" examined the argument of Japan that different tax treatment of liqueurs and sparkling wines according to alcohol and extract contents was consistent with Article III:2.

"The Panel noted ... that GATT Article II:2 permitted the non-discriminatory taxation 'of an article from which the imported product has been manufactured or produced in whole or in part', and that such a

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examination of practices of contracting parties in relation to border tax adjustments); COM.IND/W/98; L/3272; Spec(68)57 and Add.1-2.

[91] *Ibid.*, 18S/100-101, paras. 14-17.

[92] 18S/108; see discussion on Notification in the GATT under Article X.

non-discriminatory alcohol tax on like alcoholic beverages with different alcohol contents could result in differential tax rates on like products. ... Having found that

- liqueurs and sparkling wines with high raw material contents, imported into Japan, were subject to internal taxes in excess of those applied to like domestic liqueurs and sparkling wines with lower raw material contents ... and that

- this differential taxation of like products depending on their extract and raw material content had not been, and apparently could not be, justified as resulting from a non-discriminatory internal tax on the raw material content concerned or as justifiable under any of the exception clauses of the General Agreement,

the Panel concluded that this imposition of higher taxes on 'classic' liqueurs and sparkling wines with higher raw material content was inconsistent with Article III:2, first sentence."[93]

The 1987 Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances" noted that the legislation at issue (the Superfund Amendments and Reauthorization Act) provided for an excise tax per ton on sale of certain chemicals. The legislation also provided for an excise tax on certain downstream imported chemical substances which were derivatives of taxable chemicals. The amount of the tax on any of the downstream imported substances was to equal the amount of the excise taxes which would have been imposed on the upstream chemicals used as materials in the production of the imported substance if those upstream chemicals had been sold in the United States for use in the manufacture of the downstream imported substance.

"The Panel noted that the United States justified the tax on certain imported substances as a border tax adjustment corresponding in its effect to the internal tax on certain chemicals from which these substances were derived ... The Panel further noted that the EEC considered the tax on certain chemicals not to be eligible for border tax adjustment because it was designed to tax polluting activities that occurred in the United States and to finance environmental programmes benefitting only United States producers. Consistent with the Polluter-Pays Principle, the United States should have taxed only products of domestic origin because only their production gave rise to environmental problems in the United States. ... The Panel therefore first examined whether the tax on certain chemicals was eligible for border tax adjustments.

"... As [the conclusions of the Border Tax Adjustments Working Party] clearly indicate, the tax adjustment rules of the General Agreement distinguish between taxes on products and taxes not directly levied on products; they do not distinguish between taxes with different policy purposes. Whether a sales tax is levied on a product for general revenue purposes or to encourage the rational use of environmental resources, is therefore not relevant for the determination of the eligibility of a tax for border tax adjustment. For these reasons the Panel concluded that the tax on certain chemicals, being a tax directly imposed on products, was eligible for border tax adjustment independent of the purpose it served. The Panel therefore did not examine whether the tax on chemicals served environmental purposes and, if so, whether a border tax adjustment would be consistent with these purposes. ...

"The Panel, having concluded that the tax on certain chemicals was in principle eligible for border tax adjustment, then examined whether the tax on certain imported substances meets the national treatment requirement of Article III:2, first sentence. This provision permits the imposition of an internal tax on imported products provided the like domestic products are taxed, directly or indirectly, at the same or a higher rate. Such internal taxes may be levied on imported products at the time or point of importation (Note ad Article III). Paragraph 2(a) of Article II therefore clarifies that a tariff concession does not prevent the levying of

[93] L/6216, adopted 10 November 1987, 34S/83, 120-121, para. 5.9(d).

> 'a charge equivalent to an internal tax imposed consistently with the provisions of paragraph 2 of Article III in respect of the like domestic product or in respect of an article from which the imported product has been manufactured or produced in whole or in part'.

"The drafters of the General Agreement explained the word 'equivalent' used in this provision with the following example:

> 'If a charge is imposed on perfume because it contains alcohol, the charge to be imposed must take into consideration the value of the alcohol and not the value of the perfume, that is to say the value of the content and not the value of the whole' (EPCT/TAC/PV/26, page 21).

"The tax on certain imported substances equals in principle the amount of the tax which would have been imposed under the Superfund Act on the chemicals used as materials in the manufacture or production of the imported substance if these chemicals had been sold in the United States for use in the manufacture or production of the imported substance. In the words which the drafters of the General Agreement used in the above perfume-alcohol example: The tax is imposed on the imported substances because they are produced from chemicals subject to an excise tax in the United States and the tax rate is determined in principle in relation to the amount of these chemicals used and not in relation to the value of the imported substance. The Panel therefore concluded that, to the extent that the tax on certain imported substances was equivalent to the tax borne by like domestic substances as a result of the tax on certain chemicals the tax mat the national treatment requirement of Article III:2, first sentence."[94]

The "Superfund" legislation also provided with respect to the tax on certain imported substances that importers would be required to provide sufficient information regarding the chemical inputs of taxable substances to enable the tax authorities to determine the amount of tax to be imposed; otherwise a penalty tax would be imposed in the amount of five per cent ad valorem, or a different rate to be prescribed by the Secretary of the Treasury which would equal the amount that would be imposed if the substance were produced using the predominant method of production. The Panel, examining this penalty rate, noted as follows.

"According to the Superfund Act, the tax on certain imported substances will however not necessarily be equal to the tax on the chemicals used in their production. If an importer fails to furnish the information necessary to determine the amount of tax to be imposed, a penalty tax of 5 per cent of the appraised value of the imported substance shall be imposed. Since the tax on certain chemicals subjects some of the chemicals only to a tax equivalent to 2 per cent of the 1980 wholesale price of the chemical, the 5 per cent penalty tax could be much higher than the highest possible tax that the importer would have to pay if he provided sufficient information.... The imposition of a penalty tax on the basis of the appraised value of the imported substance would not conform with the national treatment requirement of Article III: 2, first sentence, because the tax rate would in that case no longer be imposed in relation to the amount of taxable chemicals used in their production but the value of the imported substance. Thus it would not meet the requirement of equivalence which the drafters explained in the perfume-alcohol example mentioned in the preceding paragraph. ..."[95]

In the 1990 Panel Report on "EEC - Regulation on Imports of Parts and Components" the Panel examined the application of Article 13:10 of the EEC's anti-dumping regulation (Council Regulation No. 2176/84), under which anti-circumvention duties were levied on products assembled or produced in the EEC. Having found that the anti-circumvention duties were not customs duties within the meaning of Article II:1(b) (see excerpts starting at page 200), the Panel examined them in the light of the first sentence of Article III:2.

"The Panel noted that, in the cases in which anti-circumvention duties had been applied, the EEC followed sub-paragraph (c) of the anti-circumvention provision, according to which 'the amount of duty collected shall be proportional to that resulting from the application of the rate of the anti-dumping duty

[94] L/6175, adopted on 17 June 1987, 34S/136, 160-163, paras. 5.2.3, 5.2.4, 5.2.7, 5.2.8.
[95] *Ibid.*, 34S/163, para. 5.2.9.

applicable to the exporter of the complete products on the c.i.f. value of the parts or materials imported'. The Panel further noted that like parts and materials of domestic origin are not subject to any corresponding charge. The Panel therefore found that the anti-circumvention duties on the finished products subject imported parts and materials indirectly to an internal charge in excess of that applied to like domestic products and that they are consequently contrary to Article III:2, first sentence".[96]

In the 1994 Panel Report on "United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco", "The Panel ... turned to the claim of the United States that the internal tax on imported tobacco was a border tax adjustment applied consistently with Article III:2 due to the existence of a similar internal tax applied to domestic tobacco. Addressing this claim, the Panel noted that the BDA could only be subject to border tax adjustment if it were an internal tax or charge consistent with Article III:2".[97] See also the material from this report at page 153 concerning the claim that the "No Net Cost Assessments" on imported burley and flue-cured tobacco were permissible border tax adjustments consistent with Article III:2.[98]

See also under the Note *ad* Article III and see the discussion below of the phrase "in excess of those applied".

(3) "or other internal charges of any kind": charges on the transfer of payments for imports or exports

The Report of Sub-Committee A of the Third Committee at the Havana Conference, which considered Article 18 of the Charter, states as follows.

> "The Sub-Committee [A] considered that charges imposed in connection with the international transfer of payments for imports or exports, particularly the charges imposed by countries employing multiple currency practices, where such charges are imposed not inconsistently with the Articles of Agreement of the International Monetary Fund, would not be covered by Article 18. On the other hand, in the unlikely case of a multiple currency practice which takes the form of an internal tax or charge, such as an excise tax on an imported product not applied on the like domestic product, that practice would be precluded by Article 18. It may be pointed out that the possible existence of charges on the transfer of payments insofar as these are permitted by the International Monetary Fund is clearly recognized by Article 16."[99]

The foregoing passage was referred to in the 1952 Panel Report on "Special Import Taxes Instituted by Greece". In this connection, the Panel observed:

> "... the principal question arising for determination was whether or not the Greek tax was an internal tax or charge on imported products within the meaning of paragraph 2 of Article III. If the finding on this point were affirmative, the panel considered that it would be subject to the provisions of Article III whatever might have been the underlying intent of the Greek Government in imposing the tax. ... On the other hand, if the contention of the Greek Government were accepted that the tax was not in nature of a tax or charge on imported goods, but was a tax on foreign exchange allocated for the payment of imports, the question would arise whether this was a multiple currency practice, and, if so, whether it was in conformity with the Articles of Agreement of the International Monetary Fund. These matters would be for the determination of the International Monetary Fund. If the Fund should find that the tax system was a multiple currency practice and in conformity with the Articles of Agreement of the International Monetary Fund, it would fall outside the scope of Article III.

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[96]L/6657, adopted on 16 May 1990, 37S/132, 193, para. 5.9.

[97]DS44/R, adopted on 4 October 1994, para. 89; the footnote to this paragraph refers to the panel reports on "United States - Taxes on Petroleum and Certain Imported Substances", adopted on 17 June 1987, BISD 34S/136, 155-159, and "United States - Section 337 of the Tariff Act of 1930", adopted on 7 November 1989, BISD 36S/345, 386-387.

[98]DS44/R, adopted on 4 October 1994, paras. 102-112.

[99]Havana Reports, p. 62, para. 39, repeating an understanding arrived at during the Geneva session of the Preparatory Committee (see EPCT/174, p. 7). See also Havana discussion of this understanding at E/CONF.2/C.3/A/W.33, p. 3. The text of Article 18 as revised at Havana was taken into the GATT; see the discussion of negotiating history in section III below. Article 16 corresponded to Article I of the General Agreement.

"Even if it were found that the tax did not fall within the ambit of Article III the further question might arise under Article XV:4 whether the action of the Greek Government constituted frustration by exchange action of the intent of the provisions of Article III of the General Agreement".[100]

(4) "in excess of those applied"

The summary records of the Third Committee at the Havana Conference note the statement that "internal taxes on imported products could be increased if the tax on the domestic products was also increased; the requirement was that the tax should be the same on both imported and domestic products".[101]

The 1992 Panel Report on "Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies" notes with respect to taxes on beer containers:

"The Panel noted that Canada levied in the provinces of Manitoba and Ontario a charge on all beverage alcohol containers, domestic and imported, which were not part of a deposit/return system; in Nova Scotia, a charge was levied on non-refillable containers, domestic and imported, shipped to the liquor board. The United States considered these charges to be inconsistent with Article III since they were in practice applied only to imported beer because imported beer could not be delivered by the brewers to the points of sale and the establishment of a separate container collection system was, therefore, prohibitively expensive. The Panel noted that it was not the charges on containers as such that the United States considered to be inconsistent with Article III but rather their application in a situation where different systems for the delivery of beer to the points of sale applied to imported and domestic beer. The Panel, therefore, considered that its findings on restrictions on private delivery [see page 181 below] dealt with this matter".[102]

(a) Discriminatory rates of tax

In October 1955 the United Kingdom complained that the Italian government's imposition of a general turnover tax on pharmaceuticals at one rate for domestic products and a different and higher rate for imported products was inconsistent with Article III.[103]

The 1987 Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances," examining an excise tax on petroleum, found that "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".[104] See also the discussion of this case above under "Border tax adjustments".

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" "considered that the application of a lower rate of federal excise tax on domestic beer from qualifying United States producers, which lower rate is not available in the case of imported beer, constitutes less favourable treatment to the imported product in respect of internal taxes and is therefore inconsistent with the national treatment provision of Article III:2, first sentence". The Panel reached the same conclusion with respect to federal excise taxes on wine and cider and floor stocks of wine.[105]

(b) Methods of taxation

The 1987 Panel Report on "Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages" examined Japanese excise taxes on alcoholic beverages, which provided different tax rates for different types of beverages, different quality grades of the same beverage, and beverages above and

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[100]G/25, adopted on 3 November 1952, 1S/48, 49-50, paras. 5, 7, 8.
[101]E/CONF.2/C.3/SR.42, p. 4.
[102]DS17/R, adopted 18 February 1992, 39S/27, 85, para. 5.33.
[103]L/421, SR.10/5.
[104]L/6175, adopted on 17 June 1987, 34S/136, 155, para. 5.1.1.
[105]DS23/R, adopted on 19 June 1992, 39S/206, 270, 273, paras. 5.5 (beer), 5.14 (wine, cider and floor stocks of wine).

below a price threshold. The Panel compared the fiscal burden on the various alcoholic beverages that the Panel had determined to be "like products" or "directly competitive or substitutable products" (see below).

"... The Panel further found that the wording 'directly or indirectly' and 'internal taxes ... *of any kind*' implied that, in assessing whether there is tax discrimination, account is to be taken not only of the rate of the applicable internal tax but also of the taxation methods (e.g. different kinds of internal taxes, direct taxation of the finished product or indirect taxation by taxing the raw materials used in the product during the various stages of its production) and of the rules for the tax collection (e.g. basis of assessment).

"The Panel then examined the European Communities' contention ... that Japanese internal taxes on whiskies, brandies, still wines, sparkling wines, spirits and liqueurs imported from the EEC were in excess of those applied to like Japanese products, and reached the following conclusions:

"a) *Whiskies and brandies subject to the grading system:* The Panel noted that the Japanese specific tax rates on imported and Japanese whiskies/brandies special grade (2,098,100 yen/kl) were considerably higher than the Japanese specific tax rates on whiskies/brandies first grade (1,011,400 yen/kl) and second grade (296,200 yen/kl). The Panel was unable to find that these tax differentials corresponded to objective differences of the various distilled liquors, for instance that they could be explained as a non-discriminatory taxation of their respective alcohol contents. ... almost all whiskies/brandies imported from the EEC were subject to the higher rates of tax whereas more than half of whiskies/brandies produced in Japan benefited from considerably lower rates of tax. The Panel concluded, therefore, that (special and first grade) whiskies/brandies imported from the EEC were subject to internal Japanese taxes 'in excess of those applied ... to like domestic products' (i.e. first and second grade whiskies/brandies) in the sense of Article III:2, first sentence.

"b) *Wines, spirits and liqueurs subject to the 'mixed' system of specific tax and ad valorem tax:* The Panel noted that imported and domestic wines, whiskies, brandies, spirits and liqueurs were subject to *ad valorem* taxes in lieu of the specific tax when the manufacturer's selling price (CIF and customs duty for imported products) exceeded a specified threshold. ... The Panel was of the view that a 'mixed' system of specific and ad valorem liquor taxes was as such not inconsistent with Article III:2, which prohibits only discriminatory or protective taxation of imported products but not the use of differentiated taxation methods as such, provided the differentiated taxation methods do not result in discriminatory or protective taxation. ... since liquors above the non-taxable thresholds were subjected to *ad valorem* taxes in excess of the specific taxes on 'like' liquors below the threshold ... the imposition of ad valorem taxes on wines, spirits and liqueurs imported from the EEC, which are considerably higher than the specific taxes on 'like' domestic wines, spirits and liqueurs, was inconsistent with Article III:2, first sentence.

"c) *The different methods of calculating ad valorem taxes on imported and domestic liquors:* The Panel shared the view expressed by both parties that Article III:2 does not prescribe the use of any specific method or system of taxation. The Panel was further of the view that there could be objective reasons proper to the tax in question which could justify or necessitate differences in the system of taxation for imported and for domestic products. The Panel found that it could be also compatible with Article III:2 to allow two different methods of calculation of price for tax purposes. Since Article III:2 prohibited only discriminatory or protective tax burdens on imported products, what mattered was, in the view of the Panel, whether the application of the different taxation methods actually had a discriminatory or protective effect against imported products. The Panel could therefore not agree with the European Community's view that the mere fact that the so-called 'fixed subtraction system' was available only for domestic liquors constituted in itself a discrimination contrary to Article III:2 or 4".[106]

[106]L/6216, adopted 10 November 1987, 34S/83, 118-120, paras. 5.8-5.9.

The 1992 Panel Report on "Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies" noted with respect to the mark-ups charged by provincial liquor boards:

> "... The Panel ... considered that Article III:2 required that the computations of the base value for the purposes of assessing these charges be no less favourable for imported beer than for domestic beer. This requirement was met if this value was computed for both imported and domestic beer on the basis of the full cost of the beer, which in the case of the imported beer included charges for cost of services levied by the liquor boards consistently with the General Agreement.
>
> "The Panel further noted that Article III:2 applied to internal taxes levied on imported products, that is products on which duties levied in connection with importation had already been assessed. The Panel therefore *found* that Canada could, consistently with Article III:2, levy the provincial and federal sales taxes on the basis of the duty-paid value of imported beer.
>
> "In the light of these considerations the Panel *found* that Canada's methods of assessing mark-ups and taxes on imported beer were not inconsistent with Article III:2".[107]

See also the material on border tax adjustments at page 144 *et seq*.

(c) Exemption or remission of taxes

In 1950 the Netherlands brought a complaint concerning the "utility" system in the United Kingdom, under which goods satisfying certain quality and price criteria were exempted from the UK purchase tax, but imported articles of comparable quality and price were not so exempted. Other representatives stated that the utility system applied only to goods produced in the UK, and that the purchase tax was collected on many imported goods where the identical UK product was exempted. The UK representative agreed that this discrimination had a protective effect. In 1952 the UK authorities notified that the system had been changed so as to exempt from purchase tax all listed textiles, clothing and footwear below specified price levels.[108]

The 1985 Panel Report on "Canada - Measures Affecting the Sale of Gold Coins," which has not been adopted, examined taxes imposed by the Province of Ontario on the Maple Leaf (Canadian) and Krugerrand (South African) gold coins. Having found that the Maple Leaf and Krugerrand were "like products" (see below), the Panel found that "Ontario had exempted the Maple Leaf gold coin from its retail sales tax but not the Krugerrand gold coin. The internal taxes to which Krugerrand gold coins imported into Canadian territory were subject in Ontario were thus in excess of those applied to a like domestic product".[109]

In the 1994 dispute on "United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco", the Panel examined the "No Net Cost Assessment" ("NNCA"), a tax applied to both domestic and imported burley and flue-cured tobacco, the proceeds of which were deposited in an account used to reimburse the U.S. Government for any losses resulting from the operation of the domestic tobacco price-support programme.

> "The Panel recalled the claim of the complainants that the NNCA was inconsistent with Article III:2, first sentence, because the net charge of the NNCA on imported tobacco was greater than that on like domestic tobacco. The Panel further recalled the complainants' claim that the NNCA was inconsistent with Article III:2, second sentence, because the NNCA charged on imported tobacco reduced the cost of the price support programme to the domestic tobacco producer, without providing any benefit to imported tobacco. The Panel also recalled the defense of the United States that the NNCA was a border tax adjustment consistent with Article III.
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> ...

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[107]DS17/R, adopted 18 February 1992, 39S/27, 83, paras. 5.24-5.26.

[108]GATT/CP.5/12 (Netherlands complaint), GATT/CP.5/SR.20, p. 1-5 (discussion at Fifth Session), GATT/CP.6/SR.7 (interim report by UK), G/18 (UK notification of elimination of discrimination).

[109]L/5863, para. 51.

"In examining the parties' claims as to the NNCA in the light of Article III:2, first sentence, the Panel first noted that the record indicated, and all parties to the dispute agreed, that the tax applied to imported burley and flue-cured tobacco was not in excess of –indeed was identical to –the tax applied to domestic burley and flue-cured tobacco, respectively.

"The Panel then examined the complainants' claim that the net rate of the NNCA on imported tobacco was higher than that of the NNCA on domestic tobacco because the latter in effect benefitted from a tax remission through the operation of the tobacco price support programme.

"On this point, the Panel first noted that Article III is concerned with ensuring national treatment of products, not of producers.[110] The Panel then noted that the same rate of tax was imposed via the NNCA on both imported and domestic tobacco. Both in the case of imported and domestic burley and in the case of imported and domestic flue-cured, respectively, the identical rate of tax was paid to the CCC on each pound of such tobacco sold in the United States. What was different in the case of domestic tobacco subject to NNCAs was that its producers benefitted from the U.S. Government's tobacco price support programme. In the view of the Panel, this distinction did not transform the NNCA paid on domestic tobacco into a remission of a tax on a product. The Panel here agreed with the United States that whether or not the use of the revenue derived from the NNCA might ultimately benefit domestic rather than imported tobacco was not relevant to the Panel's analysis under Article III:2.

"The Panel noted, moreover, that Article III:8(b) explicitly recognizes that

> '[t]he provisions of this Article shall not prevent the payment of subsidies exclusively to domestic producers, including *payments to domestic producers derived from the proceeds of internal taxes or charges* applied consistently with the provisions of this Article and subsidies effected through governmental purchases of domestic products.' *(emphasis added)*

"It appeared to the Panel that the complainants were in essence arguing that Article III:2 was violated because U.S. producers benefitted from a payment of a subsidy derived from the proceeds of the internal tax, but that importers did not benefit in a like manner.

"The Panel was cognizant of the fact that a remission of a tax on a product and the payment of a producer subsidy out of the proceeds of such a tax could have the same economic effects. However, the Panel noted that the distinction in Article III:8(b) is a formal one, not one related to the economic impact of a measure. Thus, in view of the explicit language of Article III:8(b), which recognizes that the product-related rules of Article III 'shall not prevent the payment of subsidies exclusively to domestic producers', the Panel did not consider, as argued by the complainants, that the payment of a subsidy to tobacco producers out of the proceeds of the NNCA resulted in a form of tax remission inconsistent with Article III:2.[111]

...

"... the Panel rejected the complainants' claims of inconsistency of the NNCA with Article III:2, first and second sentence. In addition, the Panel concurred with the United States that the NNCAs on imported burley and flue-cured tobacco were permissible border tax adjustments consistent with Article III:2."[112]

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[110]The footnote to this paragraph in the panel report notes: "See report of the panel on United States - Section 337 of the Tariff Act of 1930, adopted on 7 November 1989, BISD 36S/345, 387, citing report of the panel on United States - Taxes on Petroleum and Certain Imported Substances, adopted on 17 June 1987, BISD 34S/136, 158."

[111]The footnote to this paragraph notes: "See report of the panel on United States - Measures Affecting Alcoholic and Malt Beverages, adopted on 19 June 1992, BISD 39S/206, 271-273 for a discussion of the reasons for the distinction in GATT between tax exemptions and remissions on the one hand and producer subsidies on the other."

[112]DS44/R, adopted on 4 October 1994, paras. 103, 105-109, 112.

(d) Exposure of imported products to a risk of discrimination

The 1994 Panel Report on "United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco" notes, in relation to the budget deficit assessment ("BDA") charge assessed on domestic and imported tobacco:

> "The Panel recalled that the BDA, applicable to all domestic tobacco for which price support was available, was calculated at the rate of one per cent of the average price support level for each such tobacco type in the previous crop year. The Panel then recalled that the BDA on all types of imported tobacco was calculated as the average of the BDA on domestic burley and domestic flue-cured tobacco.
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> "The Panel further noted that the application of these two different statutorily prescribed formulas to tobacco in the current year, at least in the case of flue-cured tobacco, resulted in an internal tax on imported tobacco that was higher than that on like domestic tobacco. ...
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> ...
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> "The Panel thus considered that this imposition of an internal tax on imported flue-cured tobacco at a higher rate than on domestic flue-cured tobacco, as well as the fact that some domestic tobacco was entirely exempt from such tax, each presented cases of less favourable tax treatment inconsistent with Article III:2, first sentence.[113]
>
> "The Panel recognized that a change in the price support levels for domestic burley and flue-cured tobacco could result in a given year in the elimination of the discriminatory tax treatment against imported flue-cured tobacco. However, beyond the immediate circumstance of a higher assessment on imported flue-cured tobacco than on like domestic tobacco, the Panel considered that the U.S. statutorily prescribed averaging method for calculation of the BDA on imported tobacco contained an inherent risk of a higher assessment on some types of imported tobacco than on like domestic tobacco. The Panel agreed with the argument of the complainants that, mathematically, given the statutorily mandated averaging formula, the BDA would always be higher on imported tobacco than on one type of domestic tobacco so long as there was any price differential between the average support price of burley and flue-cured tobacco.
>
> "The Panel noted that an internal regulation which merely exposed imported products to a risk of discrimination had previously been recognized by a GATT panel to constitute, by itself, a form of discrimination, and therefore less favourable treatment within the meaning of Article III.[114] The Panel agreed with this analysis of risk of discrimination as enunciated by this earlier panel.
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> "The Panel thus considered that the system for calculation of the BDA on imported tobacco itself, not just the manner in which it was currently applied, was inconsistent with Article III:2 because it carried with it the risk of discriminatory treatment of imports in respect of internal taxes.
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> "The Panel recalled the U.S. defense that even if the BDA was higher on imported flue-cured tobacco than on like domestic tobacco, the method of calculation of the BDA for imports –averaging the BDA on domestic burley and flue-cured tobacco –was a reasonable method and should not be subject to challenge before this Panel. However, the Panel could not see how such a method of calculation could be termed 'reasonable' in the context of the General Agreement if it mandated and inevitably resulted in discriminatory treatment of imported tobacco in respect of internal taxes. The Panel recalled in this regard that a prior GATT panel had ruled that in assessing whether there was tax discrimination, account was to be taken not only of the rate of the applicable internal tax but also of the taxation methods,

[113]The footnote to this sentence notes: "See, *e.g.*, report of the panel on United States - Taxes on Petroleum and Certain Imported Substances, adopted on 17 June 1987, BISD 34S/136, 155; report of the panel on United States - Measures Affecting Alcoholic and Malt Beverages, adopted on 19 June 1992, BISD 39S/206, 270".

[114]The footnote to this sentence notes: "See, *e.g.*, report of the panel on EEC - Payments and Subsidies Paid to Processors and Producers of Oilseeds and Related Animal Feed Protein, adopted on 25 January 1990, BISD 37S/86, 125".

including the basis of assessment.[115] Another Article III panel had ruled that more favourable treatment as to some products could not be balanced against less favourable treatment as to others.[116] It had noted that '[s]uch an interpretation would lead to great uncertainty about the conditions of competition between imported and domestic products and thus defeat the purposes of Article III'.[117] The Panel agreed with these earlier rulings and rejected the U.S. defense of 'reasonableness' of the BDA's method of calculation. In accordance with the national treatment provisions of Article III:2, each pound of tobacco imported into the United States had to be accorded treatment no less favourable in respect of internal taxes than that accorded to like domestic tobacco."[118]

In this connection see also the unadopted Panel Report of 1994 on "United States - Taxes on Automobiles".[119]

(5) "like domestic products"

See also the material on "like product" under Article I and paragraph 4 of Article III.

The 1970 Working Party Report on "Border Tax Adjustments" observed that "With regard to the interpretation of the term 'like or similar products', which occurs some sixteen times throughout the General Agreement, it was recalled that considerable discussion had taken place ... but that no further improvement of the term had been achieved. The Working Party concluded that problems arising from the interpretation of the terms 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. ..."[120]

The 1985 Panel Report on "Canada - Measures Affecting the Sale of Gold Coins," which has not been adopted, examined taxes imposed by the Province of Ontario on the Maple Leaf (Canadian) and Krugerrand (South African) gold coins.

"The Panel ... examined the Ontario measure in the light of the provisions of Article III and reached the following conclusions: (a) Both the Maple Leaf and the Krugerrand are legal tender in their respective countries of origin. However, they are normally purchased as investment goods. The Panel therefore considered that the Maple Leaf and Krugerrand gold coins were not only means of payment but also 'products' within the meaning of Article III:2. (b) The Maple Leaf and Krugerrand gold coins are produced to very similar standards, have the same weight in gold, and therefore compete directly with one another in international markets. The Panel therefore considered that the Maple Leaf and Krugerrand gold coins were 'like' products within the meaning of Article III:2, first sentence."[121]

The 1987 Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances" examined, *inter alia*, a tax on petroleum, applied at US$0.082 per barrel for "crude oil received at a United States refinery" and US$0.117 per barrel for "petroleum products entered into the United States for consumption, use or warehousing". The panel findings note as follows.

"... The CONTRACTING PARTIES have not developed a definition of the term 'like products' in [Article III:2, first sentence]. In the report of the Working Party on Border Tax Adjustments, adopted by the CONTRACTING PARTIES in 1970, it was suggested that the problems arising from the interpretation of

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[115]The footnote to this sentence refers to the panel report on "Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages", adopted on 10 November 1987, BISD 34S/83, 118-120.

[116]The footnote to this sentence refers to the panel report on "United States - Section 337 of the Tariff Act of 1930", adopted on 7 November 1989, BISD 36S/345, 387.

[117]The footnote to this sentence refers to the panel report on "United States - Section 337 of the Tariff Act of 1930", adopted on 7 November 1989, BISD 36S/345, 387.

[118]DS44/R, adopted on 4 October 1994, paras. 92-93, 95-98.

[119]DS31/R, dated 11 October 1994, paras. 5.10, 5.14, 5.27-5.32.

[120]L/3464, adopted on 2 December 1970, 18S/97, 102, para. 18.

[121]L/5863, para. 51.

this term should be examined on a case-by-case basis and that one of the possible methods for determining whether two products were like products was to compare their end-uses in a given market (BISD 18S/102). The domestic products subject to the tax are: crude oil, crude oil condensates, and natural gasoline. The imported products subject to the tax are: crude oil, crude oil condensates, natural gasoline, refined and residual oil, and certain other liquid hydrocarbon products. The imported and domestic products are thus either identical or, in the case of imported liquid hydrocarbon products, serve substantially identical end-uses. The imported and domestic products subject to the tax on petroleum are therefore in the view of the Panel 'like products' within the meaning of Article III:2. ..."[122]

In the 1987 Panel Report on "Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages" the Panel examined the arguments of the parties regarding the application of Article III:2 to the liquor tax system applied to various types of domestic and imported alcoholic beverages in Japan.

"The *text of the first sentence of Article III:2* clearly indicates that the comparison to be made is between internal taxes on imported products and 'those applied ... to like domestic products'. The wording 'like' products (in the French text: 'produits similaires') has been used also in other GATT Articles on non-discrimination (*e.g.* Article I:1) in the sense not only of 'identical' or 'equal' products but covering also products with similar qualities (see, for instance, the 1981 Panel Report on Tariff Treatment by Spain of Imports of Unroasted Coffee, BISD 28S/102, 112).

"The *context of Article III:2* shows that Article III:2 supplements, within the system of the General Agreement, the provisions on the liberalization of customs duties and of other charges by prohibiting discriminatory or protective taxation against certain products from other GATT contracting parties. The Panel found that this context had to be taken into account in the interpretation of Article III:2. For instance, the prohibition under GATT Article I:1 of different tariff treatment for various types of 'like' products (such as unroasted coffee, see BISD 28S/102, 112) could not remain effective unless supplemented by the prohibition of different internal tax treatment for various types of 'like' products. Just as Article I:1 was generally construed, in order to protect the competitive benefits accruing from reciprocal tariff bindings, as prohibiting 'tariff specialization' discriminating against 'like' products, only the literal interpretation of Article III:2 as prohibiting 'internal tax specialization' discriminating against 'like' products could ensure that the reasonable expectation, protected under GATT Article XXIII, of competitive benefits accruing under tariff concessions would not be nullified or impaired by internal tax discrimination against like products. It had therefore been correctly stated in another Panel Report recently adopted by the CONTRACTING PARTIES that 'Article III:2, first sentence, obliges contracting parties to establish certain competitive conditions for imported products in relation to domestic products' (L/6175, paragraph 5.1.9). And it had been for similar reasons that, during the discussion in the GATT Council of the panel report on Spain's restrictions on the domestic sale of soyabean oil which had not been adopted by the Council, several contracting parties, including Japan, had emphasized 'with regard to Article III:4 that the interpretation of the term "like products" in the Panel Report as meaning 'more or less the same product' was too strict an interpretation' (C/M/152 at page 16).

"The *drafting history* confirms that Article III:2 was designed with 'the intention that internal taxes on goods should not be used as a means of protection' ... This accords with the broader objective of Article III 'to provide equal conditions of competition once goods had been cleared through customs' (BISD 7S/64), and to protect thereby the benefits accruing from tariff concessions. This object and purpose of Article III:2 of promoting non-discriminatory competition among imported and like domestic products could not be achieved if Article III:2 were construed in a manner allowing discriminatory and protective internal taxation of imported products in excess of like domestic products.

"*Subsequent GATT practice* in the application of Article III further shows that past GATT panel reports adopted by the CONTRACTING PARTIES have examined Article III:2 and 4 by determining, firstly, whether the imported and domestic products concerned were 'like' and, secondly, whether the internal taxation or other regulation discriminated against the imported products ... Past GATT practice has

[122]L/6175, adopted on 17 June 1987, 34S/136, 154-155, para. 5.1.1.

clearly established that 'like' products in terms of Article III:2 are not confined to identical products but cover also other products, for instance if they serve substantially identical end-uses. ...

"The Panel concluded that the ordinary meaning of Article III:2 in its context and in the light of its object and purpose supported the past GATT practice of examining the conformity of internal taxes with Article III:2 by determining, firstly, whether the taxed imported and domestic products are 'like' or 'directly competitive or substitutable' and, secondly, whether the taxation is discriminatory (first sentence) or protective (second sentence of Article III:2). The Panel decided to proceed accordingly also in this case."[123]

"The CONTRACTING PARTIES have never developed a general definition of the term 'like products' in Article III:2. Past decisions on this question have been made on a case-by-case basis after examining a number of relevant factors. ... The Panel was aware of the more specific definition of the term 'like product' in Article 2:2 of the 1979 Antidumping Agreement ... but did not consider this very narrow definition for the purpose of antidumping proceedings to be suitable for the different purpose of GATT Article III:2. The Panel decided, therefore, to examine the table of 'like products' submitted by the EEC [in the dispute] on a product-by-product basis using the above-mentioned criteria as well as others recognized in previous GATT practice (see BISD 25S/49, 63), such as the Customs Cooperation Council Nomenclature (CCCN) for the classification of goods in customs tariffs which has been accepted by Japan. The Panel found that the following alcoholic beverages should be considered as 'like products' in terms of Article III:2 in view of their similar properties, end-uses and usually uniform classification in tariff nomenclatures:

- imported and Japanese-made *gin*;
- imported and Japanese-made *vodka*;
- imported and Japanese-made *whisky* (including all grades classified as 'whisky' in the Japanese Liquor Tax Law) and 'spirits similar to whisky in colour, flavour and other properties' as described in the Japanese Liquor Tax Law;
- imported and Japanese-made *grape brandy* (including all grades classified as 'brandy' in the Japanese Liquor Tax Law);
- imported and Japanese-made *fruit brandy* (including all grades classified as 'brandy' in the Japanese Liquor Tax Law);
- imported and Japanese-made *'classic' liqueurs* (not including, for instance, medicinal liqueurs);
- imported and Japanese-made unsweetened *still wine*;
- imported and Japanese-made *sparkling wines*."[124]

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" examined the excise tax exemption accorded by the state of Mississippi to wine made from scuppernong grapes (*vitis rotundifolia*).

"The Panel ... examined the claim by Canada that the state of Mississippi applied a lower tax rate to wines in which a certain variety of grape was used, contrary to Articles III:1 and III:2. The Panel recalled the United States argument that the tax provision in Mississippi was applicable to all qualifying wine produced from the specified variety of grape, regardless of the point of origin.

"The Panel considered that Canada's claim depends upon whether wine imported from Canada is 'like' the domestic wine in Mississippi made from the specified variety of grape, within the meaning of Article III:2. In this regard, the Panel noted that the CONTRACTING PARTIES have not developed a general definition of the term 'like products', either within the context of Article III or in respect of other Articles of the General Agreement. Past decisions on this question have been made on a case-by-case basis after examining a number of relevant criteria, such as the product's end-uses in a given

[123] L/6216, adopted on 10 November 1987, 34S/83, 113-115, para. 5.5.
[124] *Ibid.*, 34S/115-116, para. 5.6.

market, consumers tastes and habits, and the product's properties, nature and quality. The Panel considered that the like product determination under Article III:2 also should have regard to the purpose of the Article."

> "The basic purpose of Article III is to ensure, as emphasized in Article III:1,
>
> 'that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, purchase, transportation, distribution or use of products ... should not be applied to imported or domestic products so as to afford protection to domestic production'.

"The purpose of Article III is thus not to prevent contracting parties from using their fiscal and regulatory powers for purposes other than to afford protection to domestic production. Specifically, the purpose of Article III is not to prevent contracting parties from differentiating between different product categories for policy purposes unrelated to the protection of domestic production. The Panel considered that the limited purpose of Article III has to be taken into account in interpreting the term 'like products' in this Article. Consequently, in determining whether two products subject to different treatment are like products, it is necessary to consider whether such product differentiation is being made 'so as to afford protection to domestic production'. While the analysis of 'like products' in terms of Article III:2 must take into consideration this objective of Article III, the Panel wished to emphasize that such an analysis would be without prejudice to the 'like product' concepts in other provisions of the General Agreement, which might have different objectives and which might therefore also require different interpretations.

"Applying the above considerations to the Mississippi wine tax, the Panel noted that the special tax treatment accorded in the Mississippi law to wine produced from a particular type of grape, which grows only in the southeastern United States and the Mediterranean region, is a rather exceptional basis for a tax distinction. Given the limited growing range of the specific variety of grape, at least in North America, the Panel was of the view that this particular tax treatment implies a geographical distinction which affords protection to local production of wine to the disadvantage of wine produced where this type of grape cannot be grown. The Panel noted that a previous panel concerning Article III treatment of wines and alcoholic beverages found imported and Japanese unsweetened still wines to be like products. The Panel agreed with the reasoning of this previous panel and was of the view that tariff nomenclatures and tax laws, including those at the United States federal and state level, do not generally make such a distinction between still wines on the basis of the variety of grape used in their production. The Panel noted that the United States did not claim any public policy purpose for this Mississippi tax provision other than to subsidize small local producers. The Panel concluded that unsweetened still wines are like products and that the particular distinction in the Mississippi law in favour of still wine of a local variety must be presumed, on the basis of the evidence submitted to the Panel, to afford protection to Mississippi vintners. Accordingly, the Panel found that the lower rate of excise tax applied by Mississippi to wine produced from the specified variety of grape, which lower rate is not available to the imported like product from Canada, is inconsistent with Article III:2, first sentence."[125]

See also the similar treatment of "like product" in the same Panel Report with respect to an Article III:4 claim regarding regulation of beer according to alcohol content (cited below at page 171).

In the 1994 Panel Report on "United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco", the panel examined

> "The Panel recalled the complainants' subsidiary argument under Article III:2, second sentence, as to the protective effect of the differing tax liability mandated by the BDA. On this point, the Panel noted that the second sentence of Article III:2 is subsidiary to the first sentence thereof: the second sentence only becomes relevant where a contracting party is '*otherwise* apply[ing] internal taxes or other internal charges to imported or domestic products in a manner contrary to the principles set forth in paragraph 1', *i.e.* 'so as to afford protection to domestic production'. However, in the present case,

[125]DS23/R, adopted 19 June 1992, 39S/206, 276-277, paras. 5.23-5.26.

because the Panel had already determined that the BDA was inconsistent with Article III:2, first sentence, the Panel considered that it would not be necessary to examine the consistency of the BDA with Article III:2, second sentence."[126]

In this connection see also the unadopted Panel Report of 1994 on "United States - Taxes on Automobiles".[127]

(6) "a directly competitive or substitutable product" (Ad Article III paragraph 2)

During discussions in Commission A in the Geneva session of the Preparatory Committee, the following explanation was offered of this provision.

"... Let us suppose that ... Country A gets a ... binding of oranges from Country B. Now Country B after that can proceed to put on an internal duty of any height at all on oranges, seeing that it grows no oranges itself. But by putting on that very high duty on oranges, it protects the apples which it grows itself. The consequence is that the binding duty which Country A has secured from Country B on its oranges is made of no effect, because in fact the price of oranges is pushed up so high by this internal [tax] that no one can buy them. The consequence is that the object of that binding is defeated".[128]

An ad-hoc Sub-committee which then examined the national treatment provisions of the draft Charter, and redrafted that article, included the following in its report.

"The Sub-committee considered a suggestion by the Sub-committee on Articles 25 [XI] and 27 [XIII] that the expression 'directly competitive or substitutable' used in [Article III] should conform with the wording adopted for Article 25(2)(c) [XI:2(c)]. In view of the difference in significance between the somewhat comparable expressions used in Articles 15 [III] and Article 25 [XI], it was the opinion of the Sub-committee that there was no necessity for the language of the two articles to be identical in this respect."[129]

The Report of Sub-Committee A of the Third Committee at the Havana Conference, which considered Article 18 of the Charter (on national treatment), states that

"The Sub-Committee (A) agreed that a general tax, imposed for revenue purposes, uniformly applicable to a considerable number of products, which conformed to the requirements of the first sentence of paragraph 2 would not be considered to be inconsistent with the second sentence. ... It was agreed further that a tax applying at a uniform rate to a considerable number of products was to be regarded as a tax of the kind referred to in the preceding paragraph ... notwithstanding the fact that the legislation under which the tax was imposed also provided for other rates of tax applying to other products".[130]

The summary records of discussions in the Third Committee at the Havana Conference include the following statements.

- It was stated by one of the drafters that

"... the second sentence of [the Article], far from being a departure from the principle of national treatment, was intended to strengthen that principle and prevent its abuse. Illustrating the case of tung oil and linseed oil, which could be considered as competitive and substitutable, he stated that the United States, under the first sentence of paragraph 1 of the Article, would be required to apply the same taxation policy to a domestic product as to a like imported product. The first sentence was, however,

[126]DS44/R, adopted on 4 October 1994, para. 101.
[127]DS31/R, dated 11 October 1994, paras. 5.4-5.16, 5.23-5.32, 5.33-5.37.
[128]EPCT/A/PV/9, p. 7.
[129]EPCT/174, p. 6.
[130]Havana Reports, p. 62, para. 40-41.

qualified by the second because if no substantial domestic production existed, a tax could not be placed on tung oil in order to protect linseed oil which was not similarly taxed".[131]

- It was stated that it would not be permissible to impose a tax on imported natural rubber in order to assist the production of synthetic rubber.[132]

The 1978 Panel Report on "EEC - Measures on Animal Feed Proteins" examined an EEC Regulation requiring domestic producers or importers of oilseeds, cakes and meals, dehydrated fodder and compound feeds and importers of corn gluten feed to purchase a certain quantity of surplus skimmed milk powder held by intervention agencies and to have it denatured for use as feed for animals other than calves. The Panel concluded that skimmed milk powder and vegetable proteins for animal feedingstuffs could not be considered as "like products" (see page 171):

> "The Panel noted that the General Agreement made a distinction between 'like products' and 'directly competitive and substitutable' products. The Panel therefore also examined whether these products should be considered as directly competitive and substitutable within the meaning of Article III. In this regard the Panel noted that both the United States and the EEC considered most of these products to be substitutable under certain conditions. The Panel also noted that the objective of the EEC Regulation during the period of its application, in its own terms, was to allow for increased utilization of denatured skimmed milk powder as a protein source for use in feedingstuffs for animals other than calves. Furthermore, the Panel noted that the security deposit had been fixed at such a level as to make it economically advantageous to buy denatured skimmed milk powder rather than to provide the security, thus making denatured skimmed milk powder competitive with these products. The Panel concluded that vegetable proteins and skimmed milk powder were technically substitutable in terms of their final use and that the effects of the EEC measures were to make skimmed milk powder competitive with these vegetable proteins".[133]

In the 1987 Panel Report on "Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages," as noted above the Panel concluded that "the ordinary meaning of Article III:2 in its context and in the light of its object and purpose supported the past GATT practice of examining the conformity of internal taxes with Article III:2 by determining, firstly, whether the taxed imported and domestic products are 'like' or 'directly competitive or substitutable' and, secondly, whether the taxation is discriminatory (first sentence) or protective (second sentence of Article III:2)."[134]

> "... In the view of the Panel there existed - even if not necessarily in respect of all the economic uses to which the product may be put - direct competition or substitutability among the various distilled liquors, among various liqueurs, among unsweetened and sweetened wines, and among sparkling wines. The increasing imports of 'Western-style' alcoholic beverages into Japan bore witness to this lasting competitive relationship and to the potential products substitution through trade among various alcoholic beverages. Since consumer habits vis-a-vis these products varied in response to their respective prices, their availability through trade and their other competitive inter-relationships, the Panel concluded that the following alcoholic beverages could be considered to be '*directly competitive or substitutable products*' in terms of Article III:2, second sentence:
>
> > imported and Japanese-made distilled liquors, including all grades of whiskies/brandies, vodka and shochu Groups A and B, among each other; imported and Japanese-made liqueurs among each other; imported and Japanese-made unsweetened and sweetened wines among each other; and imported and Japanese-made sparkling wines among each other.[135]

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[131] E/CONF.2/C.3/SR.11 p. 1 and Corr.2.
[132] E/CONF.2/C.3/SR.11 p. 3.
[133] L/4599, adopted on 14 March 1978, 25S/49, 63-64, para. 4.3.
[134] L/6216, adopted 10 November 1987, 34S/83, 115, para. 5.5.
[135] *Ibid.*, 34S/117, para. 5.7.

"... The Panel noted that shochu was not subject to ad valorem taxes and that the specific tax rates on shochu were many times lower than the specific tax rates on whiskies, brandies and other spirits. The Panel noted that, whereas under the first sentence of Article III:2 the tax on the imported product and the tax on the like domestic product had to be equal in effect, Article III:1 and 2, second sentence, prohibited only the application of internal taxes to imported or domestic products in a manner 'so as to afford protection to domestic production'. The Panel was of the view that also small tax differences could influence the competitive relationship between directly competing distilled liquors, but the existence of protective taxation could be established only in the light of the particular circumstances of each case and there could be a *de minimis* level below which a tax difference ceased to have the protective effect prohibited by Article III:2, second sentence. ... Since it has been recognized in GATT practice that Article III:2 protects expectations on the competitive relationship between imported and domestic products rather than expectations on trade volumes (see L/6175, paragraph 5.1.9), the Panel did not consider it necessary to examine the quantitative trade effects of this considerably different taxation for its conclusion that the application of considerably lower internal taxes by Japan on shochu than on other directly competitive or substitutable distilled liquors had trade-distorting effects affording protection to domestic production of shochu contrary to Article III:1 and 2, second sentence."[136]

A request for consultations in 1989 by the EEC concerning "Chile - Internal Taxes on Spirits" states that "The Government of Chile levies an additional sales tax of 70% on imported whisky, compared with the rate of 25% for pisco. In the view of the European Communities this situation constitutes a breach of Chile's obligations under Article III:2 ... Whisky and pisco, while they may not be 'like products', are directly competitive or substitutable products, and in this connection the panel on Japanese customs duties, taxes etc. on alcoholic drinks (L/6216) has made very clear findings and constitutes a precedent applicable in the present instance to Chilean taxation of spirits".[137]

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages," in examining an excise tax exemption accorded by the state of Mississippi to wine made from scuppernong grapes (*vitis rotundifolia*), found that the lower excise tax rate applying to such wine was inconsistent with Article III:2, first sentence, and further noted as follows:

"... The Panel wished to point out that even if the wine produced from the special variety of grape were considered unlike other wine, the two kinds of wine would nevertheless have to be regarded as 'directly competitive' products in terms of the Interpretative Note to Article III:2, second sentence, and the imposition of a higher tax on directly competing imported wine so as to afford protection to domestic production would be inconsistent with that provision".[138]

See also the material above at page 139-140 on paragraph 1 of Article III.

(7) Taxes collected or enforced at the point of importation

See the discussion above at page 136 *et seq.* of the Interpretative Note ad Article III.

5. Paragraph 3

Paragraph 3 of Article III was inserted into the General Agreement in 1948 when the original text of Article III was replaced by the text of Article 18 of the Havana Charter. The corresponding provision in the Charter had been inserted at the Havana Conference in response to a proposal by Venezuela.[139] It was stated during discussions at the Havana Conference that "if the import duty on the product in question was not bound, the margin of protection afforded by internal taxation could be transferred to the customs duty; even if

[136] *Ibid.*, 34S/122-123, para. 5.11; the reference is to the "Superfund" case.
[137] DS9/1, communication dated 31 October 1989.
[138] DS23/R, adopted 19 June 1992, 39S/206, 277, para. 5.26.
[139] Venezuelan proposal: E/CONF.2/C.3/6/Corr.2; see discussion at E/CONF.2/C.3/A/W.22, W.30.

it were bound, under paragraph 3 of Article 18 [III] it was possible to postpone the transfer until such time as it was possible for the member to obtain a release from its trade agreement obligations".[140]

Paragraph 3 of Article III applies only to the situation in which a contracting party may maintain discriminatory internal taxes on a particular item, but cannot simply transfer the discriminatory element into an import tariff because the tariff on the item in question is bound in a bilateral trade agreement that was in existence on 10 April 1947 (the opening date for the Second Session (at Geneva) of the Preparatory Committee for the Havana Conference). Paragraph 3 permits maintenance of the internal tax discrimination until the contracting party in question can obtain a release from its *bilateral* obligations with respect to the tariff.

6. Paragraph 4

(1) "treatment no less favourable"

Australia complained in 1955 that a Hawaiian regulation requiring firms which sold imported eggs to display a placard stating: "We sell foreign eggs" violated paragraph 4 of Article III.[141] The complaint was withdrawn when a domestic court decision declared the law unconstitutional and contrary to paragraph 4 of Article III.[142]

The 1958 Panel Report on "Italian Discrimination against Imported Agricultural Machinery", which examined the consistency with Article III:4 of an Italian law providing special credit facilities to farmers for the purchase of agricultural machinery produced in Italy:

> "The Panel ... had the impression that the contention of the Italian Government might have been influenced in part by the slight difference of wording which existed between the French and the English texts of paragraph 4 of Article III. The French text which had been submitted to the Italian Parliament for approval provided that the imported products '*ne seront pas soumis à un traitement moins favorable*' whereas the English text reads 'the imported product shall be accorded treatment no less favourable'. It was clear from the English text that any favourable treatment granted to domestic products would have to be granted to like imported products and the fact that the particular law in question did not specifically prescribe conditions of sale or purchase appeared irrelevant in the light of the English text. It was considered, moreover, that the intention of the drafters of the Agreement was clearly to treat the imported products in the same way as the like domestic products once they had been cleared through customs. Otherwise indirect protection could be given".[143]

The 1978 Panel Report on "EEC - Measures on Animal Feed Proteins" examined an EEC Regulation requiring domestic producers or importers of oilseeds, cakes and meals, dehydrated fodder and compound feeds and importers of corn gluten feed to purchase a certain quantity of surplus skimmed milk powder held by intervention agencies and to have it denatured for use as feed for animals other than calves. The Regulation was not applied to domestic producers of corn gluten, and was not applicable to animal, fish and synthetic proteins. The Panel examined the consistency with Article III:4 of these aspects of the Regulation and of the requirement to produce either a protein certificate (certifying the purchase and denaturing of a certain quantity of milk powder) or a security deposit.

> "The Panel ... examined whether the EEC measures accorded imported products less favourable treatment than that accorded to like products of EEC origin within the meaning of Article III:4. In this regard the Panel noted the economic considerations, including the level of domestic production and of the applicable security deposit, put forward by the EEC to justify the application of the measures to corn gluten of foreign origin only. The Panel was not convinced that these considerations justified the non-application of these measures to domestic corn gluten and therefore concluded that the measures accorded

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[140] E/CONF.2/C.3/SR.40, p. 3.
[141] L/411.
[142] SR.10/13.
[143] L/833, adopted on 23 October 1958, 7S/60, 63-64, para. 11.

imported corn gluten less favourable treatment than that accorded corn gluten of national origin in violation of Article III:4.

"The Panel also examined whether the fact that the EEC measures were not applicable to animal, fish and synthetic proteins was consistent with the provisions of Article III:4. Having regard to its own conclusion with regard to 'like products', the Panel was satisfied that animal, fish and synthetic proteins could not be considered as 'like products' for the sake of Article III:4. Since the obligations under Article III:4 relate to 'like products', the Panel concluded that the non-application of the EEC measures to these products was not inconsistent with the EEC obligations under the Article.

"The Panel examined whether the protein certificate requirement and other specific administrative requirements accorded to imported products treatment less favourable than that accorded to 'like products' of EEC origin in respect of the purchase, sale and distribution of the products in the EEC within the meaning of Article III:4. The Panel was of the opinion that these requirements should be considered as enforcement mechanisms to ensure that the obligation, of either purchasing a certain quantity of denatured skimmed milk powder or of providing a security, had been complied with. The Panel noted that the protein certificate applied only to imports but that there was an equivalent document required for products of national origin except for a relatively short period at the beginning of the application of the EEC measures. The Panel concluded that the various administrative requirements, including the protein certificate, were not inconsistent with the EEC obligations under Article III:4."[144]

The 1981 Panel Report on "EEC - United Kingdom Application of EEC Directives to Imports of Poultry from the United States" notes that this panel was established in 1980 to examine the US complaint that the UK had prevented the importation of US poultry not in compliance with legislation implementing an EEC Directive, which required that slaughtered poultry be cooled by the "spin-chill" method. As poultry produced in the United Kingdom was by derogation exempted from the requirements of the legislation (permitting it to be chilled by other methods) the US considered the UK action to be a violation of Article III. After formation of the panel, the complaint was withdrawn.[145]

In a 1982 request for consultations under Article XXII:1, the United States cited the differential postal rates applicable to second class printed matter in Canada:

"We consider that such differentiated rates which distinguish between Canadian newspapers and periodicals, non-Canadian printed-in-Canada publications, and non-Canadian mailed-in-Canada publications constitute regulations which accord treatment to imported products less favourable than that accorded to like products of national origin, and that these regulations are therefore contrary to Canada's obligations under Article III of the GATT".[146]

The 1983 Panel Report on "United States - Imports of Certain Automotive Spring Assemblies" examined the consistency with Articles III and XX of Section 337 of the Tariff Act of 1930, a US statutory provision providing (*inter alia*) for enforcement of patent infringement claims when imported goods are alleged to infringe a US patent. The Panel Report notes the Canadian view that the use of Section 337 "in cases of alleged patent infringement granted to holders of United States patents a remedy in addition to that provided by the United States patent laws, which was available only in the context of import trade. This constituted a denial of national treatment under Article III:1 and 4 of the General Agreement. Foreign producers were treated less favourably because, instead of being subject only to the procedures under United States patent law, they had to face separate proceedings in separate bodies. This was not the case for domestic producers unless they engaged in import trade. In the Canadian view this dual system was of a discriminatory nature".[147] The Panel found that "Since Article XX(d) had been found to apply, the Panel considered that an examination of the United States action in the light of the other GATT provisions ... was not required".[148] This Panel Report was adopted

[144]L/4599, adopted 14 March 1978, 25S/49, 65-66, paras. 4.10-4.12.
[145]L/5155, adopted 11 June 1981, 28S/90.
[146]L/5359.
[147]L/5333, adopted on 26 May 1983 subject to an understanding (C/M/168), 30S/107, 119, para. 34.
[148]*Ibid.*, 30S/126-127, para. 61.

subject to an understanding that its adoption "shall not foreclose future examination of the use of Section 337 to deal with patent infringement cases from the point of view of consistency with Articles III and XX of the General Agreement".[149] The same statute was again examined in the 1989 panel decision on "United States - Section 337 of the Tariff Act of 1930".[150]

The 1991 Panel Report on "United States - Restrictions on Imports of Tuna," which has not been adopted, examined a prohibition on imports of tuna and tuna products from Mexico imposed under the US Marine Mammal Protection Act (MMPA), and found that

> "... even if the provisions of the MMPA enforcing the tuna harvesting regulations (in particular those providing for the seizure of cargo as a penalty for violation of the Act) were regarded as regulating the sale of tuna as a product, the United States import prohibition would not meet the requirements of Article III. As pointed out in paragraph 5.12 above, 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 corresponds to that of United States vessels.
>
> "The Panel noted that Mexico had argued that the MMPA requirements with respect to production of yellowfin tuna in the ETP, and the method of calculating compliance with these requirements, provided treatment to tuna and tuna products from Mexico that was less favourable than the treatment accorded to like United States tuna and tuna products. It appeared to the Panel that certain aspects of the requirements could give rise to legitimate concern, in particular the MMPA provisions which set a prospective absolute yearly ceiling for the number of dolphins taken by domestic tuna producers in the ETP, but required that foreign tuna producers meet a retroactive and varying ceiling for each period based on actual dolphin taking by the domestic tuna fleet in the same time period. However, in view of its finding in the previous paragraph, the Panel considered that a finding on this point was not required."[151]

See also the material from this report at pages 137 and 175. See also the unadopted Panel Reports of 1994 on "United States - Restrictions on Imports of Tuna"[152] and "United States - Taxation of Automobiles".[153]

(a) Equality of competitive opportunities

The Panel Report on "Italian Discrimination against Imported Agricultural Machinery" examined an Italian law providing special credit terms to farmers for the purchase of agricultural machinery, conditional on the purchase of machinery produced in Italy. The Panel Report found, *inter alia*, that

> "... the intention of the drafters of the Agreement was clearly to treat the imported products in the same way as the like domestic products once they had been cleared through customs. Otherwise indirect protection could be given.
>
> "In addition, the text of paragraph 4 referred ... to laws and regulations and requirements *affecting* internal sale, purchase, etc., and not to laws, regulations and requirements governing the conditions of sale or purchase. The selection of the word 'affecting' would imply, in the opinion of the Panel, that the drafters of the Article intended to cover in paragraph 4 not only the laws and regulations which directly governed the conditions of sale or purchase but also any laws or regulations which might adversely modify the conditions of competition between the domestic and imported products on the internal market.

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[149] C/M/168.
[150] L/6439, adopted on 7 November 1989, 36S/345.
[151] DS21/R (unadopted), 39S/155, 195-196, paras. 5.15-5.16.
[152] DS29/R, dated 16 June 1994, paras. 5.8-5.9.
[153] DS31/R, dated 11 October 1994, paras. 5.51-5.55.

"… The fact that the drafters of Article III thought it necessary to include [the Article III:8(b)] exemption for production subsidies would indicate that the intent of the drafters was to provide equal conditions of competition once goods had been cleared through the customs".[154]

The 1984 Panel Report on "Canada - Administration of the Foreign Investment Review Act" examined written purchase and export undertakings under the Foreign Investment Review Act of Canada, submitted by investors regarding the conduct of the business they were proposing to acquire or establish, conditional on approval by the Canadian government of the proposed acquisition or establishment. Written undertakings are legally binding on the investor if the investment is allowed. The Panel first determined that the undertakings were to be considered "laws, regulations or requirements" within the meaning of Article III:4 (see page 173 below).

"The Panel then examined the question whether less favourable treatment was accorded to imported products than that accorded to like products of Canadian origin in respect of requirements affecting their purchase. For this purpose the Panel distinguished between undertakings to purchase goods of Canadian origin and undertakings to use Canadian sources or suppliers (irrespective of the origin of the goods), and for both types of undertakings took into account the qualifications 'available', 'reasonably available', or 'competitively available'.

"The Panel found that undertakings to purchase *goods of Canadian origin* without any qualification exclude the possibility of purchasing available imported products so that the latter are clearly treated less favourably than domestic products and that such requirements are therefore not consistent with Article III:4. This finding is not modified in cases where undertakings to purchase goods of Canadian origin are subject to the qualification that such goods be 'available'. It is obvious that if Canadian goods are not available, the question of less favourable treatment of imported goods does not arise.

"When these undertakings are conditional on goods being 'competitively available' (as in the majority of cases) the choice between Canadian or imported products may frequently coincide with normal commercial considerations and the latter will not be adversely affected whenever one or the other offer is more competitive. However, it is the Panel's understanding that the qualification 'competitively available' is intended to deal with situations where there are Canadian goods available on competitive terms. The Panel considered that in those cases where the imported and domestic product are offered on equivalent terms, adherence to the undertaking would entail giving preference to the domestic product. Whether or not the foreign investor chooses to buy Canadian goods in given practical situations, is not at issue. The purpose of Article III:4 is not to protect the interests of the foreign investor but to ensure that goods originating in any other contracting party benefit from treatment no less favourable than domestic (Canadian) goods, in respect of the requirements that affect their purchase (in Canada). On the basis of these considerations, the Panel found that a requirement to purchase goods of Canadian origin, also when subject to 'competitive availability', is contrary to Article III:4. The Panel considered that the alternative qualification 'reasonably available' which is used in some cases, is *a fortiori* inconsistent with Article III:4, since the undertaking in these cases implies that preference has to be given to Canadian goods also when these are not available on entirely competitive terms.

"The Panel then turned to the undertakings to buy from *Canadian suppliers*. The Panel did not consider the situation where domestic products are not available, since such a situation is not covered by Article III:4. The Panel understood the choice under this type of requirement to apply on the one hand to imported goods if bought through a Canadian agent or importer and on the other hand to Canadian goods which can be purchased either from a Canadian 'middleman' or directly from the Canadian producer. The Panel recognized that these requirements might in a number of cases have little or no effect on the choice between imported or domestic products. However, the possibility of purchasing imported products *directly* from the foreign producer would be excluded and as the conditions of purchasing imported products through a Canadian agent or importer would normally be less advantageous, the imported product would therefore have more difficulty in competing with Canadian products (which are not subject

[154]L/833, adopted 23 October 1958, 7S/60, 64, paras. 11-13.

to similar requirements affecting their sale) and be treated less favourably. For this reason, the Panel found that the requirements to buy from Canadian suppliers are inconsistent with Article III:4.

"In case undertakings to purchase from Canadian suppliers are subject to a 'competitive availability' qualification, as is frequent, the handicap for the imported product is alleviated as it can be obtained directly from the foreign producer if offered under more competitive conditions than via Canadian sources. In those cases in which Canadian sources and a foreign manufacturer offer a product on equivalent terms, adherence to the undertaking would entail giving preference to Canadian sources, which in practice would tend to result in the purchase being made directly from the Canadian producer, thereby excluding the foreign product. The Panel therefore found that requirements to purchase from Canadian suppliers, also when subject to competitive availability, are contrary to Article III:4. As before (paragraph 5.9), the Panel considered that the qualification 'reasonably available' is *a fortiori* inconsistent with Article III:4."[155]

The Panel noted in its conclusions that

"The Panel sympathizes with the desire of the Canadian authorities to ensure that Canadian goods and suppliers would be given a fair chance to compete with imported products. However, the Panel holds the view that the purchase requirements under examination do not stop short of this objective but tend to tip the balance in favour of Canadian products, thus coming into conflict with Article III:4. ...

"As to the extent to which the purchase undertakings reflect plans of the investors, the Panel does not consider it relevant nor does it feel competent to judge how the foreign investors are affected by the purchase requirements, as the national treatment obligations of Article III of the General Agreement do not apply to foreign persons or firms but to imported products and serve to protect the interests of producers and exporters established on the territory of any contracting party. Purchase requirements applied to foreign investors in Canada which are inconsistent with Article III:4 can affect the trade interests of all contracting parties, and impinge upon their rights".[156]

The 1989 Panel Report on "United States - Section 337 of the Tariff Act of 1930" again examined the consistency with Articles III and XX of Section 337, a US statute providing procedures for enforcing patent infringement claims which only applies to imported goods alleged to infringe a US patent. The Panel examined in particular the application of Article III:4. Having found that the procedures of Section 337 fell within the scope of "laws, regulations and requirements" (see page 175), the Panel turned to the "no less favourable treatment" standard, examining the United States argument that in certain instances Section 337 proceedings were more favourable to imported products than the alternative of enforcement of a patent in federal district court.

"The Panel noted that, as far as the issues before it are concerned, the 'no less favourable' treatment requirement set out in Article III:4, is unqualified. These words are to be found throughout the General Agreement and later agreements negotiated in the GATT framework as an expression of the underlying principle of equality of treatment of imported products as compared to the treatment given either to other foreign products, under the most favoured nation standard, or to domestic products, under the national treatment standard of Article III. The words 'treatment no less favourable' in paragraph 4 call for effective equality of opportunities for imported products in respect of the application of laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products. This clearly sets a minimum permissible standard as a basis. ...

"The Panel noted the differing views of the parties on how an assessment should be made as to whether the differences between Section 337 and federal district court procedures do or do not accord imported products less favourable treatment than that accorded to products of United States origin. ... In brief, the United States believed that this determination could only be made on the basis of an examination of the *actual results* of past Section 337 cases. It would follow from this reasoning that any unfavourable elements of treatment of imported products could be offset by more favourable elements of treatment,

[155]L/5504, adopted 7 February 1984, 30S/140, 159-161, paras. 5.7-5.11.
[156]*Ibid.*, 30S/166-167, paras. 6.3, 6.5.

provided that the results, as shown in past cases, have not been less favourable. The Community's interpretation of Article III:4 would require that Section 337 not be *capable* of according imported products less favourable treatment; elements of less and more favourable treatment could thus only be offset against each other to the extent that they always would arise in the same cases and necessarily would have an offsetting influence on each other.

"The Panel examined these arguments carefully. It noted that a previous Panel had found that the purpose of the first sentence of Article III:2, dealing with internal taxes and other internal charges, is to protect 'expectations on the competitive relationship between imported and domestic products'.[157] Article III:4, which is the parallel provision of Article III dealing with the 'non-charge' elements of internal legislation, has to be construed as serving the same purpose. Article III:4 would not serve this purpose if the United States interpretation were adopted, since a law, regulation or requirement could then only be challenged in GATT after the event as a means of rectifying less favourable treatment of imported products rather than as a means of forestalling it. In any event, the Panel doubted the feasibility of an approach that would require it to be demonstrated that differences between procedures under Section 337 and those in federal district courts had actually caused, in a given case or cases, less favourable treatment. The Panel therefore considered that, in order to establish whether the 'no less favourable' treatment standard of Article III:4 is met, it had to assess whether or not Section 337 in itself may lead to the application to imported products of treatment less favourable than that accorded to products of United States origin. It noted that this approach is in accordance with previous practice of the CONTRACTING PARTIES in applying Article III, which has been to base their decisions on the distinctions made by the laws, regulations or requirements themselves and on their potential impact, rather than on the actual consequences for specific imported products."[158]

In the 1992 Panel Report on "Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies," the Panel examined restrictions imposed by provincial liquor authorities on access for imported beer to points of sale (with respect to which Canada invoked the Protocol of Provisional Application):

"… The Panel recalled that the CONTRACTING PARTIES had decided in a number of previous cases that the requirement of Article III:4 to accord imported products treatment no less favourable than that accorded to domestic products was a requirement to accord imported products competitive opportunities no less favourable than those accorded to domestic products. The Panel found that, by allowing the access of domestic beer to points of sale not available to imported beer, Canada accorded domestic beer competitive opportunities denied to imported beer. For these reasons the present Panel saw great force in the argument that the restrictions on access to points of sale were covered by Article III:4. However, the Panel considered that it was not necessary to decide whether the restrictions fell under Article XI:1 or Article III:4 because Canada was not invoking an exception to the General Agreement applicable only to measures taken under Article XI:1 (such as the exceptions in Articles XI:2 and XII) and the question of whether the restrictions violated Article III:4 or Article XI:1 of the General Agreement was therefore of no practical consequence in the present case".[159]

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" examined the requirement, imposed by certain states in the US, that imported beer and wine be sold only through in-state wholesalers or other middlemen, while some in-state like products were permitted to be sold directly to retailers, and in some cases at retail on producers' premises.

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[157]Note 1 to this paragraph refers to the Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances", L/6175, paragraph 5.1.9), adopted on 17 June 1987, 34S/136.

[158]36S/386-387, paras. 5.11-5.13. Note 2 to this paragraph provides: "For example: Working Party on Brazilian Internal Taxes (BISD II/184-5, paragraph 13-16); Panel on Italian Discrimination against Imported Agricultural Machinery (BISD 7S/63-64, paragraphs 11-12); Panel on EEC - Measures on Animal Feed Proteins (BISD 25S/65, paragraph 4.10); Panel on Canada - Administration of the Foreign Investment Review Act (BISD 30S/167, paragraph 6.6); Panel on United States - Taxes on Petroleum and Certain Imported Substances (L/6175, paragraphs 5.1.1-5.1.9)".

[159]DS21/R, adopted on 18 February 1992, 39S/27, 75-76, para. 5.5.

"… The Panel recalled that the CONTRACTING PARTIES have consistently interpreted the requirement of Article III:4 to accord imported products treatment no less favourable than that accorded to domestic products as a requirement to accord imported products competitive opportunities no less favourable than those accorded to domestic products.[160]

"The Panel considered as irrelevant to the examination under Article III:4 the fact that many – or even most – in-state beer and wine producers 'preferred' to use wholesalers rather than to market their products directly to retailers. The Article III:4 requirement is one addressed to relative competitive opportunities created by the government in the market, not to the actual choices made by enterprises in that market. Producers located in the states in question have the opportunity to choose their preferred method of marketing. The Panel considered that it is the very denial of this opportunity in the case of imported products which constitutes less favourable treatment. The Panel then recalled the finding of a previous panel[161] that a requirement to buy from domestic suppliers rather than from the foreign producer was inconsistent with Article III:4:

"Similarly, in the present case the Panel considered that the choice available to some United States producers to ship their beer and wine directly to in-state retailers may provide such domestic beer and wine with competitive opportunities denied to the like imported products. Even if in some cases the in-state exemption from the wholesaler requirement is available only to small wineries and small breweries, this fact does not in any way negate the denial of competitive opportunities to the like imported products. In so finding, the Panel recalled its earlier finding, in paragraph 5.19, that beer from large breweries is not unlike beer from small breweries.

"In the view of the Panel, therefore, the requirement that imported beer and wine be distributed through in-state wholesalers or other middlemen, when no such obligation to distribute through wholesalers exists with respect to in-state like domestic products, results in 'treatment … less favourable than that accorded to like products' from domestic producers, inconsistent with Article III:4. The Panel considered that even where Canadian producers have the right to establish in-state wholesalers, as is the case in some states, subject to varying conditions, the fact remains that the wholesale level represents another level of distribution which in-state product is not required to use.

"The Panel … recalled the argument of the United States that the wholesaling requirement was consistent with Article III:4 because in-state breweries and wineries not subject to the wholesaling requirement bore the same costs as did wholesalers in respect of record keeping, audit, inspection and tax collection. The Panel noted that this factual contention – that imported products are not in fact disadvantaged vis-à-vis domestic like products in spite of different requirements – was disputed by Canada and was similar to the position taken by the United States with respect to imported products being subject to the 'preferred' wholesaling method of distribution. As previously noted, the Panel considered that the inconsistency with Article III:4 stems from the denial to the imported products of competitive opportunities accorded to the domestic like products. Whereas domestic beer and wine may be shipped directly from the in-state producer to the retailer, or sold directly at retail, this competitive advantage is denied to imported beer and wine."[162]

(b) Formally identical legal requirements versus formally different legal requirements

The 1989 Panel Report on "United States - Section 337 of the Tariff Act of 1930" further provided:

"… The words 'treatment no less favourable' in paragraph 4 call for effective equality of opportunities for imported products in respect of the application of laws, regulations and requirements affecting the

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[160]Note 8 to the Panel Report provides: "See, for example, the Report of the Panel on 'United States - Section 337 of the Tariff Act of 1930', adopted on 7 November 1989, BISD 36S/345, 386; and the Report of the Panel on 'Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies', [not yet considered by the Council,] DS17/R, page 55".

[161]Note 9 to the Panel Report provides: "Report of the Panel on 'Canada - Administration of the Foreign Investment Review Act', adopted on 7 February 1984, BISD 30S/140, 160-61".

[162]DS23/R, adopted 19 June 1992, 39S/206, 279-280, paras. 5.30-5.33.

internal sale, offering for sale, purchase, transportation, distribution or use of products. This clearly sets a minimum permissible standard as a basis. On the one hand, contracting parties may apply to imported products different formal legal requirements if doing so would accord imported products more favourable treatment. On the other hand, it also has to be recognised that there may be cases where application of formally identical legal provisions would in practice accord less favourable treatment to imported products and a contracting party might thus have to apply different legal provisions to imported products to ensure that the treatment accorded them is in fact no less favourable. For these reasons, the mere fact that imported products are subject under Section 337 to legal provisions that are different from those applying to products of national origin is in itself not conclusive in establishing inconsistency with Article III:4. In such cases, it has to be assessed whether or not such differences in the legal provisions applicable do or do not accord to imported products less favourable treatment. Given that the underlying objective is to guarantee equality of treatment, it is incumbent on the contracting party applying differential treatment to show that, in spite of such differences, the no less favourable treatment standard of Article III is met".[163]

The 1992 Panel Report on "Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies" also examined the application of Article III:4 with respect to formally identical requirements (in the case of minimum prices applied to all beer: see page 177) and formally different requirements (in the case of internal transportation of beer: see page 181).

(c) *Application of legal requirements to individual cases and "balancing"*

The 1989 Panel Report on "United States - Section 337 of the Tariff Act of 1930" further provides:

"The Panel further found that the 'no less favourable' treatment requirement of Article III:4 has to be understood as applicable to each individual case of imported products. The Panel rejected any notion of balancing more favourable treatment of some imported products against less favourable treatment of other imported products. If this notion were accepted, it would entitle a contracting party to derogate from the no less favourable treatment obligation in one case, or indeed in respect of one contracting party, on the ground that it accords more favourable treatment in some other case, or to another contracting party. Such an interpretation would lead to great uncertainty about the conditions of competition between imported and domestic products and thus defeat the purposes of Article III".[164]

After a detailed comparison between Section 337 procedures and those in federal district court,

"The Panel *found* that Section 337, inconsistently with Article III:4 of the General Agreement, accords to imported products alleged to infringe United States patents treatment less favourable than that accorded under federal district court procedures to like products of United States origin as a result of the following factors:

(i) the availability to complainants of a choice of forum in which to challenge imported products, whereas no corresponding choice is available to challenge products of United States origin;

(ii) the potential disadvantage to producers or importers of challenged products of foreign origin resulting from the tight and fixed time-limits in proceedings under Section 337, when no comparable time-limits apply to producers of challenged products of United States origin;

(iii) the non-availability of opportunities in Section 337 proceedings to raise counterclaims, as is possible in proceedings in federal district court;

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[163]L/6439, adopted 7 November 1989, 36S/345, 386, para. 5.11.

[164]L/6439, adopted on 7 November 1989, 36S/345, 387, para. 5.14. See also similar finding with respect to Article I in the Panel Report on "United States - Denial of Most-favoured-nation Treatment as to Non-Rubber Footwear from Brazil", DS18/R, adopted on 19 June 1992, 39S/128, 151, para. 6.10.

(iv) the possibility that general exclusion orders may result from proceedings brought before the USITC under Section 337, given that no comparable remedy is available against infringing products of United States origin;

(v) the automatic enforcement of exclusion orders by the United States Customs Service, when injunctive relief obtainable in federal court in respect of infringing products of United States origin requires for its enforcement individual proceedings brought by the successful plaintiff;

(vi) the possibility that producers or importers of challenged products of foreign origin may have to defend their products both before the USITC and in Federal district court, whereas no corresponding exposure exists with respect to products of United States origin".[165]

In the 1990 Panel Report on "EEC - Payments and Subsidies Paid to Processors and Producers of Oilseeds and Related Animal-Feed Proteins" the Panel examined EEC legislation providing for payment of subsidies to processors of oilseeds whenever they established by documentary evidence that they had transformed oilseeds of Community origin. Discussing as well the relationship between paragraphs 4 and 8(b) of Article III (see page 194 below),

"... The Panel noted that ... if the economic benefits generated by the payments granted by the Community can at least partly be retained by the processors of Community oilseeds, the payments generate a benefit conditional upon the purchase of oilseeds of domestic origin inconsistently with Article III:4. ...

"... The Panel concluded that the Community Regulations do not ensure that the payments to processors are based on prices processors actually have to pay when purchasing Community oilseeds ... [nor that] the subsidy payments are based on prices that the subsidy recipients would actually have paid had they chosen to buy imported rather than domestic products.

"For the reasons indicated in the preceding paragraphs, the Panel found that subsidy payments made to processors can be greater than the difference between the price processors actually pay to producers and the price that processors would have to pay for imported oilseeds. Whether such over-compensation creating an incentive to purchase domestic rather than imported products takes place depends on the circumstances of the individual purchase. The Community Regulations are thus capable of giving rise to discrimination against imported products though they may not necessarily do so in the case of each individual purchase.

"Having made this finding the Panel examined whether a purchase regulation which does not necessarily discriminate against imported products but is capable of doing so is consistent with Article III:4. The Panel noted that the exposure of a particular imported product to a risk of discrimination constitutes, by itself, a form of discrimination. The Panel therefore concluded that purchase regulations creating such a risk must be considered to be according less favourable treatment within the meaning of Article III:4. The Panel found for these reasons that the payments to processors of Community oilseeds are inconsistent with Article III:4".[166]

In the 1992 Follow-up on this Panel Report, the members of the Reconvened Oilseeds Panel noted that "The facts before the Panel, which were not challenged by the United States, indicated that ... the payments to processors conditional on the purchase of domestic oilseeds that had given rise to the inconsistency found by the original Panel had been superseded, there being no provision for such payments under the new support system other than in the transitional arrangements"[167] and concluded that "... the Panel suggests that the CONTRACTING PARTIES take note of the Community's statement that the new support system for oilseeds under

[165] *Ibid.,* 36S/391, para. 5.20.
[166] L/6627, adopted on 25 January 1990, 37S/86, 124-125, paras. 137-141.
[167] DS28/R, dated 31 March 1992, 39S/91, 113, para. 74.

Regulation Nº 3766/91 was intended to eliminate any inconsistency with Article III:4 by the discontinuation of payments to processors conditional on the purchase of domestic oilseeds".[168]

In this connection, see also the unadopted Panel Report of 1994 on "United States - Taxes on Automobiles".[169]

(2) "than that accorded to like products of national origin"

See also the discussion of "like product" above in this chapter and under Article I.

The 1978 Panel Report on "EEC - Measures on Animal Feed Proteins" examined an EEC Regulation requiring domestic producers or importers of oilseeds, cakes and meals, dehydrated fodder and compound feeds and importers of corn gluten feed to purchase a certain quantity of surplus skimmed milk powder held by intervention agencies and to have it denatured for use as feed for animals other than calves. The Panel examined the consistency of the EEC measures with, *inter alia*, Article III:1, III:4 and III:5.

> "The Panel began by examining whether all products used for the same purpose of adding protein to animal feeds should be considered as 'like products' within the meaning of Articles I and III. Having noted that the General Agreement gave no definition of the concept of 'like product' the Panel reviewed how it had been applied by the CONTRACTING PARTIES in previous cases.[170]
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> "The Panel noted, in this case, such factors as the number of products and tariff items carrying different duty rates and tariff bindings, the varying protein contents and the different vegetable, animal and synthetic origins of the protein products before the Panel –not all of which were subject to the EEC measures. Therefore, the Panel concluded that these various protein products could not be considered as 'like products' within the meaning of Articles I and III."[171]

During the discussion in the Council of the Panel Report on "Spain - Measures concerning Domestic Sale of Soyabean Oil"[172] which was noted by the Council and not adopted, representatives of several contracting parties criticized the Panel's conclusion in respect of Article III:4, that the term "like products" meant "more or less the same product", on the basis that this general definition in the Panel Report was too narrow and that past decisions on this term had been made on a case-by-case basis after examining a number of relevant factors.[173]

In the 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages"

> "The Panel began its examination of these beer alcohol content distinctions in the named states by considering whether, in the context of Article III:4, low alcohol beer and high alcohol beer should be considered 'like products'. The Panel recalled in this regard its earlier statement on like product determinations and considered that, in the context of Article III, it is essential that such determinations be made not only in the light of such criteria as the products' physical characteristics, but also in the light of the purpose of Article III, which is to ensure that internal taxes and regulations 'not be applied to imported or domestic products so as to afford protection to domestic production'. The purpose of Article III is not to harmonize the internal taxes and regulations of contracting parties, which differ from country to country. In light of these considerations, the Panel was of the view that the particular level at which the distinction between high alcohol and low alcohol beer is made in the various states does not affect its reasonings and findings.

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[168] *Ibid.*, 39S/118, para. 89.
[169] DS31/R, dated 11 October 1994, paras. 5.47-5.49.
[170] Note 1 at 25S/63 provides: "See for instance BISD II/188, BISD 1S/53, BISD II/181, 183."
[171] L/4599, adopted on 14 March 1978, 25S/49, 63, paras. 4.1-4.2. See also material on this report at pages 162, 199 and 160 in this chapter.
[172] L/5142.
[173] C/M/152.

"The Panel recognized that the treatment of imported and domestic products as like products under Article III may have significant implications for the scope of obligations under the General Agreement and for the regulatory autonomy of contracting parties with respect to their internal tax laws and regulations: once products are designated as like products, a regulatory product differentiation, e.g. for standardization or environmental purposes, becomes inconsistent with Article III even if the regulation is not 'applied ... so as afford protection to domestic production'. In the view of the Panel, therefore, it is imperative that the like product determination in the context of Article III be made in such a way that it not unnecessarily infringe upon the regulatory authority and domestic policy options of contracting parties. The Panel recalled its earlier statement that a like product determination under Article III does not prejudge like product determinations made under other Articles of the General Agreement or in other legislative contexts.

"The Panel recognized that on the basis of their physical characteristics, low alcohol beer and high alcohol beer are similar. It then proceeded to examine whether, in the context of Article III, this differentiation in treatment of low alcohol beer and high alcohol beer is such 'as to afford protection to domestic production'. The Panel first noted that both Canadian and United States beer manufacturers produce both high and low alcohol content beer. It then noted that the laws and regulations in question in the various states do not differentiate between imported and domestic beer as such, so that where a state law limits the points of sale of high alcohol content beer or maintains different labelling requirements for such beer, that law applies to all high alcohol content beer, regardless of its origin. The burdens resulting from these regulations thus do not fall more heavily on Canadian than on United States producers. The Panel also noted that although the market for the two types of beer overlaps, there is at the same time evidence of a certain degree of market differentiation and specialization: consumers who purchase low alcohol content beer may be unlikely to purchase beer with a higher alcohol content and vice-versa, and manufacturers target these different market segments in their advertising and marketing.

"The Panel then turned to a consideration of the policy goals and legislative background of the laws regulating the alcohol content of beer. In this regard, the Panel recalled the United States argument that states encouraged the consumption of low alcohol beer over beer with a higher alcohol content specifically for the purposes of protecting human life and health and upholding public morals. The Panel also recalled the Canadian position that the legislative background of laws regulating the alcohol content of beer showed that the federal and state legislatures were more concerned with raising tax revenue than with protecting human health and public morals. On the basis of the evidence submitted, the Panel noted that the relevant laws were passed against the background of the Temperance movement in the United States. It noted further that prior to the repeal of the Eighteenth Amendment of the United States Constitution authorizing Prohibition, amendments to the federal Volstead Act – the Act which implemented the Eighteenth Amendment – authorized the sale of low alcohol beer, and that the primary focus of the drafters of these amendments may have been the establishment of a brewing industry which could serve as a new source of tax revenue. However, irrespective of whether the policy background to the laws distinguishing alcohol content of beer was the protection of human health and public morals or the promotion of a new source of government revenue, both the statements of the parties and the legislative history suggest that the alcohol content of beer has not been singled out as a means of favouring domestic producers over foreign producers. The Panel recognized that the level at which the state measures distinguished between low and high alcohol content could arguably have been other than 3.2 per cent by weight. Indeed, as the Panel previously noted, Alabama and Oregon make the distinction at slightly different levels. However, there was no evidence submitted to the Panel that the choice of the particular level has the purpose or effect of affording protection to domestic production".[174]

See also the similar treatment of "like product" in the same Report with regard to an Article III:2 claim concerning the Mississippi excise tax exemption for wine made from scuppernong grapes (page 157).

[174]DS23/R, adopted 19 June 1992, 39S/206, 293-294, para. 5.71-5.74.

(3) "in respect of all laws, regulations and requirements"

(a) Requirements applied in individual cases

The 1984 Panel Report on "Canada - Administration of the Foreign Investment Review Act" notes as follows.

> "The Panel could not subscribe to the Canadian view that the word 'requirements' in Article III:4 should be interpreted as 'mandatory rules applying across-the-board' because this latter concept was already more aptly covered by the term 'regulations' and the authors of this provision must have had something different in mind when adding the word 'requirements'. The mere fact that the few disputes that have so far been brought before the CONTRACTING PARTIES regarding the application of Article III:4 have only concerned laws and regulations does not in the view of the Panel justify an assimilation of 'requirements' with 'regulations'. The Panel also considered that, in judging whether a measure is contrary to obligations under Article III:4, it is not relevant whether it applies across-the-board or only in isolated cases. Any interpretation which would exclude case-by-case action would, in the view of the Panel, defeat the purposes of Article III:4.
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> "The Panel carefully examined the Canadian view that the purchase undertakings should be considered as private contractual obligations of particular foreign investors vis-à-vis the Canadian government ... The Panel felt ... that ... private contractual obligations entered into by investors should not adversely affect the rights which contracting parties, including contracting parties not involved in the dispute, possess under Article III:4 of the General Agreement and which they can exercise on behalf of their exporters. This applies in particular to the rights deriving from the national treatment principle, which –as stated in Article III:1 –is aimed at preventing the use of internal measures 'so as to afford protection to domestic production'."[175]

(b) Subsidies and other benefits as "requirements"

The 1958 Panel Report on "Italian Discrimination against Imported Agricultural Machinery" examined an Italian law providing special credit terms to farmers for the purchase of agricultural machinery, conditional on the purchase of machinery produced in Italy.[176] The United Kingdom also complained in October 1957 concerning a subsidy granted by the French government to purchasers of agricultural machinery, conditional on the purchase of domestically-produced machinery.[177]

The Panel Report on "Canada - Administration of the Foreign Investment Review Act" provides as follows.

> "... As both parties had agreed that the Foreign Investment Review Act and the Foreign Investment Review Regulations –whilst providing for the possibility of written undertakings –did not make their submission obligatory, the question remained whether the undertakings given in individual cases are to be considered 'requirements' within the meaning of Article III:4. In this respect the Panel noted that Section 9(c) of the Act refers to 'any written undertakings relating to the proposed or actual investment given by any party thereto conditional upon the allowance of the investment' and that Section 21 of the Act states that 'where a person who has given a written undertaking... fails or refuses to comply with such undertaking' a court order may be made 'directing that person to comply with the undertaking'. The Panel noted that written purchase undertakings –leaving aside the manner in which they may have been arrived at (voluntary submission, encouragement, negotiation, etc.) –once they were accepted, became part of the conditions under which the investment proposals were approved, in which case compliance could be legally enforced. The Panel therefore found that the word 'requirements' as used in Article III:4 could be considered a proper description of existing undertakings."[178]

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[175] L/5504, adopted on 7 February 1984, 30S/140, 159, paras. 5.5-5.6.
[176] L/833, adopted on 23 October 1958, 7S/60.
[177] L/695, SR.12/5.
[178] L/5504, adopted on 7 February 1984, 30S/140, 158, para. 5.4.

In the Panel Report on "EEC - Regulation on Imports of Parts and Components" the Panel examined, *inter alia*, the EEC's acceptance of undertakings under anti-circumvention rules in its anti-dumping legislation, examining whether acceptance of such undertakings to limit the use of imported parts and materials constituted a "requirement" according treatment to imported products less favourable than that accorded to domestic products contrary to Article III:4.

> "The Panel recalled that, during the period June 1987 to October 1988, eleven undertakings by parties related to or associated with Japanese manufactures had been accepted by the EEC in investigations under the anti-circumvention provision and that, according to the relevant Commission decisions published in the Official Journal of the European Communities, these undertakings related, *inter alia*, to changes in the sourcing of parts and materials used in assembly or production operations in the Community. The Panel noted that there is no obligation under the EEC's anti-dumping Regulation to offer parts undertakings, to accept suggestions by the EEC Commission to offer such undertakings and to maintain the parts undertakings given. However, the consequence of not offering an undertaking, or of withdrawing an existing undertaking, can be the continuation of procedures that may lead to the imposition of the anti-circumvention duties. Article 10 of Regulation N° 2324/88 states that 'where an undertaking has been withdrawn or where the Commission has reason to believe that it has been violated ... it may ... apply ... antidumping ... duties forthwith on the basis of the facts established before the acceptance of the undertaking'.
>
> "The Panel noted that Article III:4 refers to 'all laws, regulations or requirements affecting (the) internal sale, offering for sale, purchase, transportation, distribution or use'. The Panel considered that the comprehensive coverage of '*all* laws, regulations or requirements *affecting*' (emphasis added) the internal sale, etc. of imported products suggests that not only requirements which an enterprise is legally bound to carry out, such as those examined by the 'FIRA Panel' (BISD 30S/140, 158), but also those which an enterprise voluntarily accepts in order to obtain an advantage from the government constitute 'requirements' within the meaning of that provision. The Panel noted that the EEC made the grant of an advantage, namely the suspension of proceedings under the anti-circumvention provision, dependent on undertakings to limit the use of parts or materials of Japanese origin without imposing similar limitations on the use of like products of EEC or other origin, hence dependent on undertakings to accord treatment to imported products less favourable than that accorded to like products of national origin in respect of their internal use. The Panel therefore concluded that the decisions of the EEC to suspend proceedings under Article 13:10 conditional on undertakings by enterprises in the EEC to limit the use of parts or materials originating in Japan in their assembly or production operations are inconsistent with Article III:4."[179]

In this connection see also the unadopted 1994 Panel Report on "EEC - Import Régime for Bananas".[180]

(c) Requirements associated with the regulation of international investment

The 1984 Panel Report on "Canada - Administration of the Foreign Investment Review Act" examined, *inter alia*, the argument of Canada that in accordance with Article XXIX:1 of the General Agreement, the word "requirements" in Article III:4 of the General Agreement should be interpreted in the light of Article 12 of the Havana Charter concerning the right to regulate foreign investment.

> "... the Panel could not subscribe to the assumption that the drafters of Article III had intended the term 'requirements' to exclude requirements connected with the regulation of international investments and did not find anything in the negotiating history, the wording, the objectives and the subsequent application of Article III which would support such an interpretation."[181]

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[179] L/6657, adopted on 16 May 1990, 37S/132, 197, para. 5.20-5.21.
[180] DS38/R, dated 11 February 1994, paras. 143-148.
[181] L/5504, adopted on 7 February 1984, 30S/140, 162, para. 5.12.

(4) "affecting"

The 1958 Panel Report on "Italian Discrimination Against Imported Agricultural Machinery," which examined the consistency with Article III:4 of an Italian law providing special credit facilities to farmers for the purchase of agricultural machinery produced in Italy, noted that

> "... the text of paragraph 4 referred both in English and French to laws and regulations and requirements *affecting* internal sale, purchase, etc., and not to laws, regulations and requirements governing the conditions of sale or purchase. The selection of the word 'affecting' would imply, in the opinion of the Panel, that the drafters of the Article intended to cover in paragraph 4 not only the laws and regulations which directly governed the conditions of sale or purchase but also any laws or regulations which might adversely modify the conditions of competition between the domestic and imported products on the internal market".[182]

The 1989 Panel Report on "United States - Section 337 of the Tariff Act of 1930" also addressed the meaning of "affecting" in Article III:4.

> "... The Panel first addressed the issue of whether only substantive laws, regulations and requirements or also procedural laws, regulations and requirements can be regarded as 'affecting' the internal sale of imported products. The positions of the United States and the Community on this were different. The Panel noted that the text of Article III:4 makes no distinction between substantive and procedural laws, regulations or requirements and it was not aware of anything in the drafting history that suggests that such a distinction should be made. A previous Panel had found that 'the selection of the word 'affecting' would imply ... that the drafters of the Article intended to cover in paragraph 4 not only the laws and regulations which directly governed the conditions of sale or purchase but also any laws or regulations which might adversely modify the conditions of competition between the domestic and imported products on the internal market.'[183] In the Panel's view, enforcement procedures cannot be separated from the substantive provisions they serve to enforce. If the procedural provisions of internal law were not covered by Article III:4, contracting parties could escape the national treatment standard by enforcing substantive law, itself meeting the national treatment standard, through procedures less favourable to imported products than to like products of national origin. The interpretation suggested by the United States would therefore defeat the purpose of Article III, which is to ensure that internal measures 'not be applied to imported or domestic products so as to afford protection to domestic production' (Article III:1). The fact that Section 337 is used as a means for the enforcement of United States patent law at the border does not provide an escape from the applicability of Article III:4; the interpretative note to Article III states that any law, regulation or requirement affecting the internal sale of products that is enforced in the case of the imported product at the time or point of importation is nevertheless subject to the provisions of Article III. Nor could the applicability of Article III:4 be denied on the ground that most of the procedures in the case before the Panel are applied to persons rather than products, since the factor determining whether persons might be susceptible to Section 337 proceedings or federal district court procedures is the source of the challenged products, that is whether they are of United States origin or imported. For these reasons, the Panel found that the procedures under Section 337 come within the concept of 'laws, regulations and requirements' affecting the internal sale of imported products, as set out in Article III of the General Agreement."[184]

In this connection see also the unadopted Panel Report of 1994 on "United States - Taxes on Automobiles".[185]

The 1991 Panel Report on "United States - Restrictions on Imports of Tuna," which has not been adopted, examined a US prohibition on the imports of tuna and tuna products from Mexico imposed under the

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[182]L/833, adopted on 23 October 1958, 7S/60, 64, para. 12.

[183]The note to this sentence refers to the Panel Report on "Italian Discrimination Against Imported Agricultural Machinery," adopted on 23 October 1958, 7S/60, para. 12.

[184]L/6439, adopted on 7 November 1989, 36S/345, 385-386, para. 5.10.

[185]DS31/R, dated 11 October 1994, paras. 5.45-5.46.

US Marine Mammal Protection Act because of the incidental taking of dolphins during tuna fishing by the Mexican tuna fleet. The Panel found that

> "... The text of Article III:1 refers to the application to imported or domestic *products* of 'laws, regulations and requirements affecting the internal sale ... of *products'* and 'internal quantitative regulations requiring the mixture, processing or use of *products*'; it sets forth the principle that such regulations on *products* not be applied so as to afford protection to domestic production. Article III:4 refers solely to laws, regulations and requirements affecting the internal sale, etc. of *products*. This suggests that Article III covers only measures affecting products as such. ...
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> "A previous panel had found that Article III:2, first sentence, 'obliges contracting parties to establish certain competitive conditions for imported *products* in relation to domestic *products*'.[186] Another panel had found that the words 'treatment no less favourable' in Article III:4 call for effective equality of opportunities for imported *products* in respect of the application of laws, regulations or requirements affecting the sale, offering for sale, purchase, transportation, distribution or use of *products*, and that this standard has to be understood as applicable to each individual case of imported *products*.[187] It was apparent to the Panel that the comparison implied was necessarily one between the measures applied to imported products and the measures applied to like domestic products.
>
> "The Panel considered that, as Article III applied the national treatment principle to both regulations and internal taxes, the provisions of Article III:4 applicable to regulations should be interpreted taking into account interpretations by the CONTRACTING PARTIES of the provisions of Article III:2 applicable to taxes. The Panel noted in this context that the Working Party Report on Border Tax Adjustments, adopted by the CONTRACTING PARTIES in 1970, had concluded that
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> > '... there was convergence of views to the effect that *taxes directly levied on products were eligible for tax adjustment* ... Furthermore, the Working Party concluded that there was convergence of views to the effect that certain taxes that were not directly levied on products were not eligible for adjustment, [such as] social security charges whether on employers or employees and payroll taxes.'[188]
>
> "Thus, under the national treatment principle of Article III, contracting parties may apply border tax adjustments with regard to those taxes that are borne by products, but not for domestic taxes not directly levied on products (such as corporate income taxes). Consequently, the Note Ad Article III covers only internal taxes that are borne by products. The Panel considered that it would be inconsistent to limit the application of this Note to taxes that are borne by products while permitting its application to regulations not applied to the product as such.
>
> "The Panel further concluded that, even if the provisions of the MMPA enforcing the tuna harvesting regulations (in particular those providing for the seizure of cargo as a penalty for violation of the Act) were regarded as regulating the sale of tuna as a product, the United States import prohibition would not meet the requirements of Article III. As pointed out ... above, 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 corresponds to that of United States vessels."[189]

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[186] A note to this paragraph refers to the Panel report on "United States - Taxes on Petroleum and Certain Imported Substances", adopted 17 June 1987, BISD 34S/136, 158, para. 5.1.9.

[187] A note to this paragraph refers to the Panel Report on "United States - Section 337 of the Tariff Act of 1930", adopted 7 November 1989, BISD 36S/345, 386-7, paras. 5.11, 5.14.

[188] A note to this paragraph refers to 18S/97, 100-101, para. 14.

[189] DS21/R (unadopted), dated 3 September 1991, 39S/155, 194-195, paras. 5.11-5.13, 5.15.

In this connection see also the unadopted Panel Report of 1994 on "United States - Taxes on Automobiles".[190]

(5) "internal sale, offering for sale, purchase, transportation, distribution or use"

(a) Standardization of products

The Report of Sub-Committee A of the Third Committee at the Havana Conference, which considered Article 18 of the Charter (on national treatment), notes as follows:

> "The Norwegian delegation had proposed to insert a new paragraph in Article 18 to make sure that the provisions of this Article would not apply to laws, regulations and requirements which have the purpose of standardizing domestic products in order to improve the quality or to reduce costs of production, or have the purpose of facilitating an improved organization of internal industry, provided they have no harmful effect on the expansion of international trade. The Sub-Committee was of the opinion that this amendment would not be necessary because the Article as drafted would permit the use of internal regulations required to enforce standards".[191]

(b) Minimum and maximum price regulations

The 1992 Panel Report on "Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies" examined minimum prices maintained in certain provinces of Canada. The Panel found that the minimum price requirement fell under Article III, not Article XI (see page 203 below).

> "The Panel noted that minimum prices applied equally to imported and domestic beer did not necessarily accord equal conditions of competition to imported and domestic beer. Whenever they prevented imported beer from being supplied at a price below that of domestic beer, they accorded in fact treatment to imported beer less favourable than that accorded to domestic beer: when they were set at the level at which domestic brewers supplied beer - as was presently the case in New Brunswick and Newfoundland - they did not change the competitive opportunities accorded to domestic beer but did affect the competitive opportunities of imported beer which could otherwise be supplied below the minimum price. The Panel noted, moreover, that one of the basic purposes of Article III was to ensure that the contracting parties' internal charges and regulations were not such as to frustrate the effect of tariff concessions granted under Article II ...
>
> "The Panel considered that the case before it did not require a general finding on the consistency of minimum prices with Article III:4. However, it did consider that the above considerations justified the conclusion that the maintenance by an import and sales monopoly of a minimum price for an imported product at a level at which a directly competing, higher-priced domestic product was supplied was inconsistent with Article III:4."[192]

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" examined "price affirmation requirements" (maximum price levels) in the states of Massachusetts and Rhode Island.

> "The Panel noted that the price affirmation measures apply with respect to sales of alcoholic beverages to wholesalers, and that in-state producers are not required to sell through wholesalers whereas out-of-state and foreign producers are required to do so. ... The Panel considered that the price affirmation measures of Massachusetts and Rhode Island prevent the imported alcoholic beverages from being priced in accordance with commercial considerations in that imported products may not be offered below the price of these products in neighbouring states. In the view of the Panel, these measures thus

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[190]DS31/R, dated 11 October 1994, paras. 5.52-5.55.

[191]Havana Reports, p. 64, para. 49, reflecting E/CONF.2/C.3/A/W.35, p. 1-2 (withdrawal of Norwegian amendment relating to mixing requirements used to enforce standards (see page 183) on the understanding that this statement would be inserted in the Sub-Committee's Report).

[192]DS17/R, adopted 18 February 1992, 39S/27, 84-85, paras. 5.30-5.31.

accord less favourable treatment to imported products than to the like domestic products with respect to their internal sale and offering for sale, inconsistent with Article III:4."[193]

(c) Requirements affecting internal offering for sale

The 1988 Panel Report on "Canada - Import, Distribution and Sale of Alcoholic Drinks by Canadian Provincial Marketing Agencies" examined, *inter alia*, the application by provincial liquor boards of practices concerning listing and delisting of alcoholic beverages for sale, and availability of points of sale, which discriminated against imported alcoholic beverages. The Panel treated these measures as restrictions made effective through state-trading operations contrary to Article XI:1 and considered that it was therefore not necessary to decide whether the practices were contrary to Article III:4. "However, the Panel saw great force in the argument that Article III:4 was also applicable to state-trading enterprises at least when the monopoly of the importation and monopoly of the distribution in the domestic markets were combined, as was the case of the provincial liquor boards in Canada. This interpretation was confirmed *e contrario* by the wording of Article III:8(a)".[194]

The 1992 Panel Report on "Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies" notes as follows.

> "The Panel ... turned to the United States claim that the practice of the liquor boards of Ontario to limit listing of imported beer to the six-pack size while according listings in different package sizes to domestic beer was inconsistent with the General Agreement. The Panel noted that this package-size requirement, though implemented as a listing requirement, was in fact a requirement that did not affect the importation of beer as such but rather its offering for sale in certain liquor board outlets. The Panel therefore considered that this requirement fell under Article III:4. ... The Panel *found* that the imposition of the six-pack configuration requirement on imported beer but not on domestic beer was inconsistent with that provision."[195]

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" examined the requirement, imposed by certain states in the US, that imported beer and wine be sold only through in-state wholesalers or other middlemen, while some in-state like products were permitted to be sold directly to retailers, and in some cases at retail on producers' premises.

> "In the view of the Panel, therefore, the requirement that imported beer and wine be distributed through in-state wholesalers or other middlemen, when no such obligation to distribute through wholesalers exists with respect to in-state like domestic products, results in 'treatment ... less favourable than that accorded to like products' from domestic producers, inconsistent with Article III:4. The Panel considered that even where Canadian producers have the right to establish in-state wholesalers, as is the case in some states, subject to varying conditions, the fact remains that the wholesale level represents another level of distribution which in-state product is not required to use."[196]

See also at page 167 above. The same Panel also examined the exemption of Mississippi-produced wine from "local option" rules prohibiting sale of alcoholic beverages in "dry" subdivisions of the state of Mississippi.

> " ... The Panel noted that the local option law in Mississippi permits wines produced in the state to continue to be sold in those political subdivisions of the state that choose to reinstate prohibition laws, while prohibiting out-of-state and imported wines from being sold in those same subdivisions. The Panel considered that the Mississippi local option law, on its face, accords less favourable treatment to imported wine than to wine of domestic origin, because domestic wine produced in-state may continue to be sold

[193]DS23/R, adopted 19 June 1992, 39S/206, 290, para. 5.59.
[194]L/6304, adopted 22 March 1988, 35S/37, 90, para. 4.26.
[195]DS17/R, adopted 18 February 1992, 39S/27, 75, para. 5.4.
[196]DS23/R, adopted 19 June 1992, 39S/206, 280, para. 5.32.

even where a local political subdivision prohibits the sale of imported wine. The Mississippi law would therefore appear to be inconsistent with Article III:4."[197]

The same Panel also examined the listing requirements of state-operated liquor stores in certain US states.

"Having regard to the past panel decisions and the record in the instant case, the present Panel was of the view that the listing and delisting practices here at issue do not affect importation as such into the United States and should be examined under Article III:4. The Panel further noted that the issue is not whether the practices in the various states affect the right of importation as such, in that they clearly apply to both domestic (out-of-state) and imported wines; rather, the issue is whether the listing and delisting practices accord less favourable treatment – in terms of competitive opportunities – to imported wine than that accorded to the like domestic product. Consequently, the Panel decided to analyze the state listing and delisting practices as internal measures under Article III:4."[198]

(d) Regulations on quality or quantity of products consumed

The 1990 Panel Report on "Thailand - Restrictions on importation of and internal taxes on cigarettes" examined the argument of the United States that Thailand could achieve its public health objectives through internal measures consistent with Article III:4 and that the inconsistency with Article XI:1 could therefore not be considered to be 'necessary' within the meaning of Article XX(b).

"The Panel noted that the principal health objectives advanced by Thailand to justify its import restrictions were to protect the public from harmful ingredients in imported cigarettes, and to reduce the consumption of cigarettes in Thailand. The measures could thus be seen as intended to ensure the quality and reduce the quantity of cigarettes sold in Thailand.

"The Panel then examined whether the Thai concerns about the *quality* of cigarettes consumed in Thailand could be met with measures consistent, or less inconsistent, with the General Agreement. It noted that other countries had introduced strict, non-discriminatory labelling and ingredient disclosure regulations which allowed governments to control, and the public to be informed of, the content of cigarettes. A non-discriminatory regulation implemented on a national treatment basis in accordance with Article III:4 requiring complete disclosure of ingredients, coupled with a ban on unhealthy substances, would be an alternative consistent with the General Agreement. The Panel considered that Thailand could reasonably be expected to take such measures to address the quality-related policy objectives it now pursues through an import ban on all cigarettes whatever their ingredients.

"The Panel then considered whether Thai concerns about the *quantity* of cigarettes consumed in Thailand could be met by measures reasonably available to it and consistent, or less inconsistent, with the General Agreement. The Panel first examined how Thailand might reduce the *demand* for cigarettes in a manner consistent with the General Agreement. The Panel noted the view expressed by the WHO that the demand for cigarettes, in particular the initial demand for cigarettes by the young, was influenced by cigarette advertisements and that bans on advertisement could therefore curb such demand. At the Forty-third World Health Assembly a resolution was approved stating that the WHO is:

'Encouraged by … recent information demonstrating the effectiveness of tobacco control strategies, and in particular … comprehensive legislative bans and other restrictive measures to effectively control the direct and the indirect advertising, promotion and sponsorship of tobacco'.[199]

[197] *Ibid.*, 39S/289, para. 5.56.

[198] DS23/R, adopted 19 June 1992, 39S/206, 292, para. 5.63.

[199] Note 3 to this paragraph provides: "Forty-third World Health Assembly, Fourteenth plenary meeting, Agenda Item 10, 17 May 1990 (A43/VR/14; WHA43.16)."

"The resolution goes on to urge all member states of the WHO

> 'to consider including in their tobacco control strategies plans for legislation or other effective measures at the appropriate government level providing for: ...
>
> > '(c) progressive restrictions and concerted actions to eliminate eventually all direct and indirect advertising, promotion and sponsorship concerning tobacco'

"A ban on the advertisement of cigarettes of both domestic and foreign origin would normally meet the requirements of Article III:4. It might be argued that such a general ban on all cigarette advertising would create unequal competitive opportunities between the existing Thai supplier of cigarettes and new, foreign suppliers and was therefore contrary to Article III:4.[200] Even if this argument were accepted, such an inconsistency would have to be regarded as unavoidable and therefore necessary within the meaning of Article XX(b) because additional advertising rights would risk stimulating demand for cigarettes. The Panel noted that Thailand had already implemented some non-discriminatory controls on demand, including information programmes, bans on direct and indirect advertising, warnings on cigarette packs, and bans on smoking in certain public places.

"The Panel then examined how Thailand might restrict the *supply* of cigarettes in a manner consistent with the General Agreement. The Panel noted that contracting parties may maintain governmental monopolies, such as the Thai Tobacco Monopoly, on the importation and domestic sale of products.[201] The Thai Government may use this monopoly to regulate the overall supply of cigarettes, their prices and their retail availability provided it thereby does not accord imported cigarettes less favourable treatment than domestic cigarettes or act inconsistently with any commitments assumed under its Schedule of Concessions.[202] As to the pricing of cigarettes, the Panel noted that the Forty-third World Health Assembly, in its resolution cited above, stated that it was:

> 'Encouraged by ... recent information demonstrating the effectiveness of tobacco control strategies, and in particular ... policies to achieve progressive increases in the real price of tobacco'.

"It accordingly urged all member states

> 'to consider including in their tobacco control strategies plans for ... progressive financial measures aimed at discouraging the use of tobacco'[203]

"For these reasons the Panel could not accept the argument of Thailand that competition between imported and domestic cigarettes would necessarily lead to an increase in the total sales of cigarettes and that Thailand therefore had no option but to prohibit cigarette imports.

"The Panel then examined further the resolutions of the WHO on smoking which the WHO made available. It noted that the health measures recommended by the WHO in these resolutions were non-discriminatory and concerned all, not just imported, cigarettes. The Panel also examined the Report of the WHO Expert Committee on Smoking Control Strategies in Developing Countries. The Panel observed that a common consequence of import restrictions was the promotion of domestic production and the fostering of interests in the maintenance of that production and that the WHO Expert Committee had made the following recommendation relevant in this respect:

> 'Where tobacco is already a commercial crop every effort should be made to reduce its role in the national economy, and to investigate alternative uses of land and labour. The existence of a tobacco

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[200]Note 2 to this sentence provides: "On the requirement of equal competitive opportunities, see the Report of the panel on 'United States - Section 337 of the Tariff Act of 1930' (L/6439, paragraph 5.26, adopted on 7 November 1989)."

[201]Note 1 on page 37S/225 provides: "Cf. Articles III:4, XVII and XX(d)."

[202]Note 2 on page 37S/225 provides: "Cf. Articles III:2 and 4 and II:4."

[203]Note 3 on page 37S/225 provides: "Forty-third World Health Assembly, Fourteenth plenary meeting, Agenda Item 10, 17 May 1990 (A43/VR/14; WHA43.16)."

industry of any kind should not be permitted to interfere with the implementation of educational and other measures to control smoking'.[204]

"In sum, the Panel considered that there were various measures consistent with the General Agreement which were reasonably available to Thailand to control the quality and quantity of cigarettes smoked and which, taken together, could achieve the health policy goals that the Thai government pursues by restricting the importation of cigarettes inconsistently with Article XI:1. The Panel found therefore that Thailand's practice of permitting the sale of domestic cigarettes while not permitting the importation of foreign cigarettes was an inconsistency with the General Agreement not 'necessary' within the meaning of Article XX(b)."[205]

In the November 1990 Council discussion on adoption of this Panel Report, the representative of Thailand stated that "Thailand took heart from the report that a set of GATT-consistent measures could be taken to control both the supply of and demand for cigarettes, as long as they were applied to both domestic and imported cigarettes on a national-treatment basis".[206]

(e) Marking requirements

The 1956 Working Party Report on "Certificates of Origin, Marks of Origin, Consular Formalities" notes "that the question of additional marking requirements, such as an obligation to add the name of the producer or the place of origin or the formula of the product, should not be brought within the scope of any recommendation dealing with the problem of marks of origin. The point was stressed that requirements going beyond the obligation to indicate origin would not be consistent with the provisions of Article III, if the same requirements did not apply to domestic producers of like products".[207] See also the 1955 complaint referred to above at page 162 regarding a requirement to display a placard stating "We sell foreign eggs".

See also Article IX.

(f) Measures affecting internal transportation

During discussions on this provision at Geneva in 1947 it was stated that "transportation" referred to "all kinds of transportation, from a man's back to jet-propelled rockets".[208] At the Havana Conference, a proposal to delete the references to transportation in Article III received no support, "on the grounds that these provisions were necessary to prevent indirect protection to domestic products by means of differential transportation charges".[209]

The 1992 Panel Report on "Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies" also examined practices concerning the internal transportation of beer in Canada. The delivery of beer in Canada is controlled or conducted by the provincial liquor boards, which require or permit the delivery of domestic beer by the brewer to the point of sale. Except for two provinces, imported beer must be sold to the provincial liquor board which either require or arrange delivery of the beer to their own distribution centres; the cost of delivery to the point of sale was included in the mark-up charged on imported beer.

"The Panel first examined the question of whether Article III:4 of the General Agreement permitted contracting parties to apply regulations to imported products that were different from those applied to domestic products. ... The Panel ... considered that the mere fact that imported and domestic beer were subject to different delivery systems was not, in itself, conclusive in establishing inconsistency with

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[204]Note 4 on page 37S/225 provides: "1982 Expert Committee on 'Smoking Control Strategies in Developing Countries', page 69; cited at page 16 in the WHO Submission to the Panel of 19 July 1990."
[205]DS10/R, adopted 7 November 1990, 37S/200, 223-226, paras. 76-81.
[206]C/M/246, 23 November 1990.
[207]L/595, adopted on 17 November 1956, 5S/102, 105-106, para. 13.
[208]EPCT/A/PV/9, p. 43.
[209]E/CONF.2/C.3/A/W.34, p. 4.

Article III:4 of the General Agreement. The Panel then examined whether the application by Canada of the different delivery systems accorded imported beer treatment no less favourable than that accorded to domestic beer. The Panel ... considered that Article III:4 required Canada to ensure that its regulations affecting the internal transportation of imported beer to points of sale accorded imported beer competitive opportunities at least equal to those accorded to domestic beer and that it was up to Canada to demonstrate that, in spite of the application of different transportation regulations to imported and domestic beer, imported beer was accorded no less favourable treatment in this respect.

"The Panel noted that Canada claimed that it met the requirements of Article III:4 by levying charges for the delivery of imported beer to the points of sale which were no higher than the costs actually incurred by the liquor boards. The Panel, therefore, examined whether Canada, by subjecting imported beer to a levy that corresponded to the actual cost of delivery by the liquor board, offered competitive opportunities to imported beer that were equivalent to the opportunities which would result from the application of the same delivery system to both imported and domestic beer. The Panel noted that such a levy did not necessarily correspond to the cost that the liquor board would incur for the delivery of imported beer if it delivered not only imported but also domestic beer. It could reasonably be assumed that it would, in that case, make economies of scale from which also imported beer could benefit. Nor did such a levy necessarily correspond to the cost of private delivery of imported beer. It could reasonably be assumed that the structure and efficiency of private delivery systems would be different from the systems operated by the liquor boards.

"The Panel further noted that, in order to prove that the levies charged by the liquor boards for delivering imported beer to the points of sale did not exceed the cost of private delivery of such beer, Canada could not base itself on the transportation costs actually incurred by the liquor boards or the domestic breweries; it would have to determine the costs of transporting beer under delivery systems not presently in existence. The Panel felt that, given the inherent difficulties in making such a determination, its result would always be open to challenge. The Panel also noted that, in order to meet its national treatment obligations, Canada did not have to abandon the delivery of imported beer by the liquor boards; it merely had to provide competitive opportunities to imported beer that were at least equal to those accorded to domestic beer, in other words allow for the possibility of private delivery of imported beer. This would enable foreign brewers to choose between liquor-board services and private delivery on purely commercial grounds. If, as claimed by Canada, imported beer did enjoy national treatment, there was no need to prohibit the private delivery of imported beer because the services of the liquor boards would be available at a price at which they could compete successfully with private delivery systems. ..."[210]

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" examined the requirement imposed by certain states that alcoholic beverages imported into the state be transported by common carriers authorized to operate as such within the state whereas in-state producers of alcoholic beverages could deliver their product to customers in their own vehicles.

"The Panel noted that Article III:4 requires that imported products be granted treatment no less favourable than that afforded to like domestic products with respect to laws and regulations affecting their transportation. In the view of the Panel, the requirement for imported beer and wine to be transported by common carrier, whereas domestic in-state beer and wine is not so required, may result in additional charges to transport these imported products and therefore prevent imported products from competing on an equal footing with domestic like products. Accordingly, the Panel found the requirement that imported beer and wine be transported by common carrier into the states of Arizona, California, Maine, Mississippi and South Carolina, which requirement does not exist in such states for in-state beer and wine, is inconsistent with Article III:4."[211]

[210]DS17/R, adopted 18 February 1992, 39S/27, 78-79, paras. 5.12-5.14.
[211]DS23/R, adopted 19 June 1992, 39S/206, 287, para. 5.50.

(6) "differential internal transportation charges": second sentence of paragraph 4

The second sentence of paragraph 4 was drafted during the discussions of the Preparatory Committee at Geneva by a sub-committee which reviewed (*inter alia*) the Charter article on national treatment. The Report of this sub-committee states:

> "The South African Delegation had objected to the inclusion of the word 'transportation' [in the first sentence of this paragraph] but agreed to its retention subject to the addition of a new sentence clarifying the intention that this paragraph should not be construed to prevent differential transport charges which are based on economic operation of the means of transport and not on the nationality of the product concerned. ... Since the present paragraph 2 [4] relates solely to the question of differential treatment between imported and domestic goods, the inclusion of the last sentence in that paragraph should not be understood to give sanction to the use of artificial measures in the form of differential transport charges designed to divert traffic from one port to another".[212]

The same statement regarding differential transport charges designed to divert traffic from one port to another is repeated in the report of Sub-Committee A of the Third Committee, which considered the national treatment article of the Charter at the Havana Conference.[213] The report also notes: "The Sub-Committee inserted the word 'internal' to make it clear that the phrase 'differential transportation charges' does not refer to international shipping".[214] The Sub-Committee also rejected a proposal to delete the word 'transportation' in the first sentence and delete the second sentence.[215]

Concerning discriminatory internal transportation charges constituting a subsidy, see Article XVI.

7. Paragraphs 5, 6 and 7: internal quantitative regulations (mixing regulations)

(1) Scope of paragraph 5

During discussions at the Geneva session of the Preparatory Committee for the Havana Conference, the representative of Norway stated in connection with one of the proposals to amend this paragraph, "In Norway we would normally have a regulation to define that margarine would include a certain amount of butter. ... For practical purposes [margarine] is produced in Norway ... With regard to butter ... if we decided that, for example, margarine should include 20 per cent butter, we would not lay down that that should be totally Norwegian butter, to the exclusion of foreign butter, but, whether or Norwegian or foreign origin, it would be on an equal footing ...".[216] It was stated in reply that

> "The mixing regulation described ... could not be classed as protective in purpose. ... The case presented ... is that of a mixing regulation which may be described as follows:
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> > "A regulation requiring a product be composed of two or more materials in specified proportions, where all the materials in question are produced domestically in substantial quantities, and where there is no requirement that any specified quantity of any of the materials be of domestic origin.
>
> "Stated in this way, it seems obvious that this case is not intended to be covered by Article [III].
>
> "The opposite case of mixing regulations ... is where the regulation requires that a certain percentage of a product of domestic origin be used in the production of another product (e.g. that 25 per cent domestic wheat be used in making flour). Such a regulation would limit the use of the like foreign product and, hence, would under any interpretation be contrary to [Article III:5].

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[212]Report to Commission A by the Sub-Committee on Articles 14, 15 and 24, EPCT/174, pp. 6-7.

[213]Havana Reports, p. 64, para. 51; see E/CONF.2/C.3/SR.11 p. 2 (proposal to pick up this statement, citing prewar *Seehafen-Ausnahmstarife* of Germany).

[214]*Ibid.*, para. 50.

[215]*Ibid.*, para. 52.

[216]EPCT/A/PV/9, p. 52-53.

> "A third and more difficult case of mixing regulations are regulations which require that in producing an article a certain percentage of a specified material produced domestically be used when there is a competitive imported material which is not produced domestically in substantial quantities. It corresponds in the field of mixing regulations to the type of excise tax sought to be prohibited ... [by Article III:2, second sentence]".[217]

This and other questions were referred to an ad-hoc Sub-committee, the report of which noted:

> "The Sub-committee was ... in agreement that under the provisions of Article 18 [III] regulations and taxes would be permitted which, while perhaps having the effect of assisting the production of a particular domestic product (say, butter), are directed as much against the domestic production of another product (say, domestic oleomargarine), of which there was a substantial domestic production, as they are against imports (say, imported oleomargarine)".[218]

This statement was reiterated in the reports adopted at the Havana Conference.

Later, in discussions in the Third Committee at Havana, it was clarified in a statement that:

> "... requiring flour mills, for instance, to use twenty-five per cent wheat of domestic origin would be considered an internal quantitative regulation relating to 'use' under paragraph 5. The paragraph was also intended to relate to mixing regulations such as the mixture of alcohol and gasoline in the manufacture of motor fuel. ... paragraph 5 would not preclude regulations designed to eke out supplies of short materials or to enforce objective standards".[219]

It was also stated that "If a Member required that fifty per cent of the timber used in building should come from domestic sources, the regulation was not related to the mixture nor to the processing of the timber, but to its use".[220]

During the Review Session in 1954-55, "the delegate for Sweden proposed an interpretative note for paragraph 5, on the lines of the statement adopted at the Havana Conference [including the example on butter and oleomargarine] ... After discussion the representative of Sweden expressed his willingness to withdraw his proposal but desired that the Working Party's report should record his statement that the system of levying internal fees on home-produced and imported raw materials for oleomargarine manufacture, as well as on imports of oleomargarine, in order to help in the stabilization of the marketing of butter - which was mentioned in the report of Sub-Committee A of Committee III at Havana and found by that Sub-Committee to be consistent with the terms of Article 18 (Article III of GATT) was still in force. The Working Party took note of the Swedish statement".[221]

In the 1994 panel report on "United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco", the panel examined a claim that the US' Domestic Marketing Assessment ("DMA") was inconsistent with Article III:5. The DMA legislation required each "domestic manufacturer of cigarettes", as defined in the legislation, to certify to the Secretary of the U.S. Department of Agriculture ("USDA") for each calendar year, the percentage of domestically produced tobacco used by such manufacturer to produce cigarettes during the year. A domestic manufacturer that failed to make such a certification or to use at least 75 per cent domestic tobacco was subject to penalties in the form of a nonrefundable marketing assessment (i.e. the DMA) and was required to purchase additional quantities of domestic burley and flue-cured tobacco.

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[217]EPCT/A/SR/10 p. 2-3, EPCT/W/181, p. 10.
[218]EPCT/174, p. 8-9; statement repeated verbatim in Havana Reports, p. 64, para. 54.
[219]E/CONF.2/C.3/SR.40, p. 6.
[220]*Ibid.*, p. 7.
[221]L/329, Report of the Review Working Party on "Schedules and Customs Administration", adopted 26 February 1955, 3S/205, 210, para. 9.

"As to the applicability of Article III:5, first sentence, to the DMA, the Panel considered that it first had to determine whether the United States had established an 'internal quantitative regulation relating to the mixture, processing or use of products in specified amounts or proportions ...'. The Panel noted the following in this respect:

"(a) First, the DMA was established by an Act of the U.S. Congress, Section 1106(a) of the 1993 Budget Act, and was implemented through regulations of USDA. The effective date for the DMA was 1 January 1994. It thus constituted a *regulation* within the meaning of Article III:5.

"(b) Second, the Panel noted that the opening sentence of the DMA legislative provision, Section 1106(a) of the 1993 Budget Act, stated:

> 'CERTIFICATION. A *domestic manufacturer* of cigarettes *shall certify* to the Secretary, for each calendar year, the percentage of the quantity of tobacco used by the manufacturer to produce cigarettes during the year that is produced in the United States'. (*emphasis added*)

"The DMA was thus an internal regulation imposed on domestic manufacturers of cigarettes.

"(c) Third, the Panel noted that the second sub-paragraph of the DMA legislative provision stated:

> 'PENALTIES. In General. Subject to subsection (f) [exception for crop losses due to natural disasters], a *domestic manufacturer of cigarettes that has failed*, as determined by the Secretary after notice and opportunity for a hearing, to *use in the manufacture of cigarettes* during a calendar year a *quantity of tobacco grown in the United States that is at least 75 percent of the total quantity of tobacco used* by the manufacturer or to comply with subsection (a) [certification requirement], *shall be subject to* the requirements of subsections (c), (d) and (e) [*penalties* in the form of a nonrefundable marketing assessment and a required purchase of additional quantities of domestic burley and flue-cured tobacco]'. (*emphasis added*)

"The DMA was thus a *quantitative* regulation in that it set a minimum *specified proportion* of 75 per cent for the use of U.S. tobacco in manufacturing cigarettes.

"(d) Fourth, the DMA was an internal quantitative regulation relating to the *use* of a product, in that it *required the use* of U.S. domestically grown tobacco.

"The Panel thus found that the DMA was an 'internal quantitative regulation relating to the ... use of products in specified amounts or proportions ...', within the meaning of the first part of the first sentence of Article III:5.

"The Panel then turned to a consideration of whether the DMA 'requires, directly or indirectly, that any specified amount or proportion of any product which is the subject of the regulation must be supplied from domestic sources', as provided in the second part of the first sentence of Article III:5. The Panel noted the following in this respect:

"(a) The DMA required each domestic manufacturer of cigarettes to certify to the Secretary of USDA, for each calendar year, the percentage of the quantity of tobacco used by the manufacturer to produce cigarettes during the year that was produced in the United States.

"(b) Subject to an exception dealing with crop losses due to disasters, a domestic manufacturer that failed to make the required certification or to use at least 75 per cent domestic tobacco was subject to penalties including the required purchase of additional domestic tobacco.

> "The Panel thus concluded that the DMA was an internal quantitative regulation relating to the use of tobacco in specified amounts or proportions which required, directly or indirectly, that a minimum specified proportion of tobacco be supplied from domestic sources, inconsistently with Article III:5, first sentence."[222]

(2) "otherwise apply internal quantitative regulations in a manner contrary to the principles set forth in paragraph 1"

See Interpretative Note *ad* Article III, paragraph 5.

The 1978 Panel Report on "EEC - Measures on Animal Feed Proteins" examined the measures in question in relation to this paragraph.

> "Given the reference in Article III:5, second sentence, to Article III:1, the Panel then examined the consistency of the EEC Regulation as an 'internal quantitative regulation' with the provisions of Article III:1, particularly as to whether the Regulation afforded protection to domestic production. The Panel noted that the EEC Regulation considered, in its own terms, that denatured skimmed milk powder was an important source of protein which could be used in feedingstuffs. The Panel also noted that surplus stocks could originate either from domestic production or imports, but that the intervention agencies from which the buyers of vegetable proteins had to purchase a certain quantity of denatured skimmed milk powder only held domestically produced products. The Panel further noted that, although globally about 15 per cent of the EEC apparent consumption of vegetable protein was supplied from domestic sources, not all the individual products subject to the EEC measures were produced domestically in substantial quantities.
>
> "The Panel concluded that the measures provided for by the Regulation with a view to ensuring the sale of a given quantity of skimmed milk powder protected this product in a manner contrary to the principles of Article III:1 and to the provisions of Article III:5, second sentence."[223]

The interpretation of the second sentence of Article III:5 was the subject of the Panel Report on "Spain - Measures concerning Domestic Sale of Soyabean Oil",[224] which was not adopted, and of subsequent discussions in the Council. Several contracting parties expressed reservations with regard to the Panel's interpretation of Article III. The Council took note of the Report as well as of the statements made in the discussion.[225]

In Council discussions in 1982, the European Communities expressed the view that Finland's decision to make exports of leather footwear to the Soviet Union subject, *inter alia*, to the condition that the soles incorporated in such footwear should be of domestic origin, was a violation of certain provisions of the General Agreement, particularly Article III.[226] Finland considered the claim to be without legal justification and stated, inter alia, that "the economic rationale of restricting third country participation in bilateral clearing trade in non-convertible currencies with a non-contracting party ought to be evident".[227]

In the 1994 Panel Report on "United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco"

> "... the Panel noted that the second sentence of Article III:5 is subsidiary to the first sentence thereof, as the second sentence only becomes relevant where a contracting party is '*otherwise* apply[ing] internal quantitative regulations in a manner contrary to the principles set forth in paragraph 1", *i.e.* 'so as to afford protection to domestic production'. The Panel was therefore of the view that, in light of the

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[222]DS44/R, adopted on 4 October 1994, paras. 67-68.
[223]L/4599, adopted on 14 March 1978, 25S/49, 65, paras. 4.7-4.8.
[224]L/5142.
[225]C/M/152, L/5142, L/5161, L/5188.
[226]C/M/161, L/5369.
[227]C/M/161, L/5394.

finding of inconsistency of the DMA with Article III:5, first sentence, it would not be necessary to examine the consistency of the DMA with Article III:5, second sentence.[228]

(3) Special customs treatment granted conditional on mixing or use of the imported product with domestic products

The Report of Sub-Committee A of the Third Committee at the Havana Conference, which considered Article 18 of the Charter (on national treatment), notes as follows:

> "The Sub-Committee is of the opinion that paragraph 5 … would not prohibit the continuance of a tariff system which permits the entry of the product at a rate of duty lower than the normal tariff rate, provided the product is mixed or used with a certain proportion of a similar product of national origin. The Sub-Committee considered that such a provision would not be regarded as an internal quantitative regulation in terms of this paragraph for the reason that the use of a percentage of the local product is not made compulsory, nor is the import of the product in any way restricted".[229]

(4) Application of mixing regulations in time of shortages

The question of the application of mixing regulations in time of shortages was fully discussed at Havana.[230] The main points made in the course of the discussion were as follows.

- "… provided the regulation did not require that the product to be mixed had to be of domestic origin, or provided that the regulation was not imposed for protective purposes, then such a regulation would not contravene the Article."[231]

- In the event that regulations imposed in respect of shortages of raw materials had protective effects, "they would be covered by Article 43" [XX].[232]

Further, a clarification was given in the following statement:

> "… under paragraph 5 a Member could not establish a mixing regulation which protected a domestic product as against an imported product during periods when there was no shortage in order that the industry in question would be in existence in the event of a future shortage".[233]

(5) Paragraph 6: existing mixing regulations and their alteration

The report of the ad-hoc Geneva Sub-committee which examined the national treatment provisions of the Charter notes:

> "The [New York Draft provision] is aimed at preventing only those internal quantitative regulations which are clearly directed against imported products for the purposes of protecting domestic products. The new text removes the requirement that existing internal quantitative regulations not expressly approved by the Organization should be terminated at the expiration of one year after the entry into force of the Charter. The revised draft would permit the continuation of regulations in force on 1 July 1939 or 10 April 1947, whichever date the Member selects, subject to the requirement that such requirements as are retained shall be negotiable and shall not be altered to the detriment of imports. The alternative dates

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[228]DS44/R, adopted on 4 October 1994, para. 69. The footnote to this paragraph provides: "Cf. Report of the panel on United States - Measures Affecting Alcoholic and Malt Beverages, adopted on 19 June 1992, BISD 39S/206, 270, where that panel found that it would not be appropriate to consider Canada's Article III:1 allegations to the extent that it found the U.S. measures to be inconsistent with the more specific provisions of Articles III:2 and III:4."

[229]EPCT/174, p. 8.

[230]E/CONF.2/C.3/SR.40, pp. 5-8; also earlier discussion at E/CONF.2/C.3/A/W.38, p. 1-2 (discussing regulation requiring mixing of imported gasoline with domestic alcohol).

[231]E/CONF.2/C.3/SR.40, p. 6.

[232]E/CONF.2/C.3/SR.40, p. 5.

[233]E/CONF.2/C.3/SR.40, p. 7.

> were thought desirable by the Sub-Committee in order particularly to take account of the departures from normal pre-war practices rendered necessary by war-time or post-war emergencies".[234]

10 April 1947 was the opening date of the Second Session of the Preparatory Committee at Geneva. During the Havana Conference, it was decided to add a third alternative date for existing mixing regulations, the date of the signing of the Havana Conference Final Act (24 March 1948).[235] This date was chosen rather than the date of entry into force of the Charter "to avoid giving Members an opportunity to impose new regulations which would be contrary to paragraph [5]".[236]

The Report of Sub-Committee A of the Third Committee at the Havana Conference, which considered Article 18 of the Charter (on national treatment), notes that "a Member would be free to alter the details of an existing regulation provided that such alterations do not result in changing the overall effect of the regulation to the detriment of imports".[237] During the Review Session of 1954-55, it was proposed that an interpretative note to Article III:6 be added on the lines of this statement; however,

> "The Working Party considered that it was not necessary to insert a note in the Agreement as paragraph 6 is to be interpreted in this sense, with the understanding that such changes would be of a minor character and would not apply to a concession provided for in a schedule to the General Agreement".[238]

Sub-Committee A at Havana also noted in its report that:

> "The delegate from Ireland inquired whether the phrase 'shall not be modified to the detriment of imports' would permit changes in the amounts or proportions of a product required to be mixed under an existing regulation in Ireland, which changes are the result of changes in crops from year to year. The Sub-Committee decided that since the regulation in question clearly contemplates such changes, the changes would not be precluded by paragraph 6 ...".[239]

The Working Party on "The Haitian Tobacco Monopoly" in 1955 examined whether the licensing of tobacco imports by the Tobacco Régie required a release under the provisions of Article XVIII:12 (prior to the Review Session amendments to Article XVIII). "The representative of Haiti declared that the licensing system served solely to enforce the internal quantitative regulations of the Régie and did not impose any additional limitation of the quantity that may be imported. The Working Party therefore took the view that in these circumstances Article XI would not apply, that the import control should be considered under the terms of the exception in Article [XX:(d)] and that the internal regulation to which it relates should be considered under paragraphs 5 and 6 of Article III." The mixing regulation on tobacco was found to have been in effect on one of the dates specified in Article III:6. "The representative of Haiti also informed the Working Party that the provisions of paragraph 6 were fully complied with in that the regulation in force on the base date had not been altered to the detriment of imports. In these circumstances the Working Party did not see anything in paragraphs 5 or 6 of Article III which required a release under Article XVIII for these measures."[240]

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[234]EPCT/174, p. 7-8.

[235]Havana Reports, p. 65, para. 60.

[236]E/CONF.2/C.3/SR.40, p. 9.

[237]Havana Reports, p. 65, para. 58.

[238]Report of the Review Working Party on "Schedules and Customs Administration", L/329, adopted on 26 February 1955, 3S/205, 211, para. 11.

[239]Havana Reports, p. 65, para. 59; see also E/CONF.2/C.3/W.35 p. 4 (regulation in question required mixing of imported petroleum with industrial alcohol made from domestic potatoes).

[240]L/454, adopted on 22 November 1955, 4S/38, 39-40, paras. 9-10. Before the revision of Article XVIII in the Review Session, Article XVIII:12 provided for notification and concurrence with regard to certain measures affecting imports which were not otherwise permitted by the General Agreement.

(6) Paragraph 7

Article 22 of the Geneva Draft Charter (corresponding to GATT Article XIII) provided in its paragraph 5 that internal quantitative restrictions would be included within its scope. The chairman of the working party of Sub-Committee A which redrafted Article 18 at Havana explained that "in the Working Party's view it would not be feasible or desirable to allocate between sources of supply by internal quantitative restrictions, as implied by paragraph 5 of Article 22. Article 18 was concerned with allocation between domestic and foreign sources of supply and the word 'external' had been inserted before 'sources of supply' in order to ensure most-favoured-nation treatment. For this reason the Working Party had recommended new paragraph 7 and the deletion of the reference to Article 18 in paragraph 5 of Article 22".[241]

In later discussions at Havana, it was stated that "the objectives of the Geneva draft and paragraph 7 were the same, i.e., to secure non-discrimination as between foreign suppliers with respect to products subject to internal mixing regulations. The Sub-Committee had thought that the best way to assure non-discrimination was to permit free competition. In the case of import quotas this was not always possible, so Article 22 [XIII] permitted allocation in accordance with certain rules. The same reasons of practicality did not apply, however, in the case of internal quantitative regulations, and therefore paragraph 7 had been inserted as the best method of securing most-favoured-nation treatment".[242]

(7) Relationship between provisions on mixing regulations and other provisions of Article III

During discussions in Sub-Committee A at Havana, it was stated that "there was some inconsistency between the language of paragraphs 2 [III:4] and 3 [III:5], in that paragraph 2 refers only to 'like' products whereas it was not the intention of the drafters that paragraph 3 should be restricted to 'like' products".[243]

The 1978 Panel Report on "EEC - Measures on Animal Feed Proteins" examined an EEC Regulation requiring domestic producers or importers of oilseeds, cakes and meals, dehydrated fodder and compound feeds and importers of corn gluten feed to purchase a certain quantity of surplus skimmed milk powder held by intervention agencies and to have it denatured for use as feed for animals other than calves.

> "The Panel examined the obligation under the EEC Regulation, to purchase a certain quantity of denatured skimmed milk powder from intervention agencies, in terms of the provisions of Article III:5, that is whether the EEC measures constituted an 'internal quantitative regulation relating to the mixture, processing or use' within the meaning of Article III:5.
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> "The Panel noted that the Council Regulation (EEC) No. 563/76 referred, in its stated considerations, to the considerable stocks of skimmed milk powder held by intervention agencies and to the objective of increasing the utilization of skimmed milk powder as a protein in feedingstuffs for animals other than calves. In other words, the Regulation was intended to dispose on the internal market ('utilization') of a given quantity ('stocks') of skimmed milk powder in a particular form ('denatured' i.e. utilizable only for the intended purposes). The Panel therefore considered that the EEC Regulation was an 'internal quantitative regulation' in the sense of Article III:5. However, the Panel found that this 'internal quantitative regulation' as such was not related to the 'mixture, processing and use ... in specified amounts or proportions' within the meaning of Article III:5 because, at the level of its application, the EEC Regulation introduced basically an obligation to purchase a certain quantity of skimmed milk powder and the purchase obligation falls under Article III:1."[244]

The 1984 Panel Report on "Canada - Administration of the Foreign Investment Review Act" examined also a claim by the United States that purchase undertakings (see pages 165 above) which obliged the investor to purchase in Canada a specified amount or proportion of his requirements were contrary to Article III:5.

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[241] E/CONF.2/C.3/A/W.49, p. 2.
[242] E/CONF.2/C.3/SR.41, p. 2.
[243] E/CONF.2/C.3/A/W.38, p. 2.
[244] L/4599, adopted on 14 March 1978, 25S/49, 64-65, paras. 4.5-4.6.

"… The Panel noted that these cases had been characterized by both parties as *purchase* undertakings … and had also been presented as such by the United States. … In this regard the Panel noted that in paragraph 5 of Article III the conditions of purchase are not at issue but rather the existence of internal quantitative regulations relating to the mixture, processing or use of products (irrespective of whether these are purchased or obtained by other means). On the basis of the presentations made, the Panel (which was unable to go into a detailed examination of individual cases where purchase undertakings referred to percentages or specific amounts) therefore did not find sufficient grounds to consider the undertakings in question in the light of Article III:5, but came to the conclusion that they fell under the purchase requirements that had been found inconsistent with Article III:4."[245]

In the 1994 Panel Report on "United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco",

"The Panel noted that both Article III:5 and Article III:4 deal with internal regulations, but that Article III:5 is the more specific of the two provisions. In view of the Panel's finding of inconsistency of the DMA with Article III:5, and following the reasoning enunciated in paragraph 69, the Panel considered that it would not be necessary to examine the consistency of the DMA with Article III:4.[246]

8. Paragraph 8

(1) Paragraph 8(a): "procurement by governmental agencies"

The ITO Charter, as proposed in the original United States draft, would have provided for national and most-favoured-nation treatment in respect of governmental purchases of supplies for governmental use. However, this provision was deleted from the London Draft Charter "as it appears to the Preparatory Committee that an attempt to reach agreement on such a commitment would lead to exceptions almost as broad as the commitment itself".[247] See also the material on the drafting history of Article XVII:2 under that provision.

During discussions in Sub-Committee A at Havana, it was agreed that "paragraph 5 [III:8] was an exception to the whole of Article 18 [III]".[248] It was noted later that "the Sub-Committee had considered that the language of paragraph 8 would except from the scope of Article 18 [III] and hence from Article 16 [I], laws, regulations and requirements governing purchases effected for governmental use where resale was only incidental".[249]

During discussions at Havana, in response to a question regarding the case of a government which received tied loans and purchased equipment from the countries granting the loans, and which might resell such equipment later to private enterprises, it was stated that paragraph 8 "had been redrafted by the Sub-Committee specifically to cover purchases made originally for governmental purposes and not with a view to commercial resale, which might nevertheless later be sold; nor … [could] Article 18 [III] be construed as applying to contracts for purchases in foreign countries, since paragraph 8 refers only to laws, regulations or requirements relating to mixture, processing or use, which might grant protection or give more favourable treatment to domestic as opposed to foreign products".[250]

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[245]L/5504, adopted on 7 February 1984, 30S/140, 162, para. 5.13.

[246]DS44/R, adopted on 4 October 1994, para. 72. The footnote to this paragraph provides as follows: "Cf. Report of the panel on United States - Measures Affecting Alcoholic and Malt Beverages, adopted on 19 June 1992, BISD 39S/206, 270, where that panel found that it would not be appropriate to consider Canada's Article III:1 allegations to the extent that it found the U.S. measures to be inconsistent with the more specific provisions of Articles III:2 and III:4."

[247]London Report, p. 9, para. (d)(iv).

[248]E/CONF.2/C.3/A/W.39, p. 1.

[249]E/CONF.2/C.3/SR.41, p. 3.

[250]E/CONF.2/C.3/SR.41.

The 1979 Agreement on Government Procurement negotiated in the Tokyo Round of Trade Negotiations, as amended in 1988, provides in Article II:

> "1. With respect to all laws, regulations, procedures and practices regarding government procurement covered by this Agreement, the Parties shall provide immediately and unconditionally to the products and suppliers of other Parties offering products originating within the customs territories (including free zones) of the Parties, treatment no less favourable than:
>
> (a) that accorded to domestic products and suppliers; and
>
> (b) that accorded to products and suppliers of any other Party.
>
> "2. With respect to all laws, regulations, procedures and practices regarding government procurement covered by this Agreement, the Parties shall ensure:
>
> (a) that their entities shall not treat a locally-established supplier less favourably than another locally-established supplier on the basis of degree of foreign affiliation or ownership;
>
> (b) that their entities shall not discriminate against locally-established suppliers on the basis of the country of production of the good being supplied, provided that the country of production is a Party to the Agreement in accordance with the provisions of paragraph 4 of this Article.
>
> "3. The provisions of paragraph 1 shall not apply to customs duties and charges of any kind imposed on or in connexion with importation, the method of levying such duties and charges, and other import regulations and formalities."[251]

(a) "governmental"

The report of the Sub-committee which examined the national treatment articles of the Charter at Geneva provides that this "word was intended to include all governmental bodies, including local authorities".[252]

The 1952 Panel Report on "Belgian Family Allowances" examined a Belgian law imposing a 7.5 per cent levy on foreign goods purchased by public bodies when these goods originated in countries whose system of family allowances did not meet specific requirements. Having found that this levy was an internal charge under Article III:2, and further that the m.f.n. requirements of Article I:1 applied to the exemptions from the levy, the Panel further observed that:

> "[the] undertaking to extend an exemption of an internal charge unconditionally is not qualified by any other provision of the Agreement. The Panel did not feel that the provisions of paragraph 8(a) of Article III were applicable in this case as the text of the paragraph referred only to laws, regulations and requirements and not to internal taxes or charges. As regards the exception contained in paragraph 2 of Article XVII, it would appear that it referred only to the principle set forth in paragraph 1 of that Article, i.e. the obligation to make purchases in accordance with commercial considerations, and did not extend to matters dealt with in Article III".[253]

See also Article I:1(c) and 2 of the Agreement on Government Procurement of 1979.[254]

The Panel Report on "United States - Procurement of a Sonar Mapping System", which has not been adopted, examined as a threshold issue whether the acquisition of a sonar mapping system by a private company, Antarctic Support Associates (ASA), in connection with a contract between ASA and the US

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[251] 26S/33, 35 and 34S/12, 13.
[252] EPCT/174, p. 9.
[253] G/32, adopted on 7 November 1952, 1S/59, 60, para. 4.
[254] 26S/34.

National Science Foundation (NSF), was a government procurement subject to the obligations of the Agreement on Government Procurement or a private procurement subject to the disciplines of the GATT.

"The Panel noted that there was no definition of government procurement in the Agreement. The scope of the Agreement was instead determined by the wording of Article I which spoke of 'any procurement of products ... by' covered entities. It specified further that procurement could be 'through such methods as purchase or as lease, rental or hire-purchase, with or without an option to buy'. The Panel considered that, since these methods were all means of obtaining the use or benefit of a product, the word 'procurement' could be understood to refer to the obtaining of such use or benefit. At the same time, the wording of Article I:1(a) made it clear that such use was to be obtained through procurement 'by' an entity, which suggests that the entity has some form of controlling influence over the obtaining of the product.

"Some guidance as to the meaning of government procurement can be obtained from examination of those provisions of the General Agreement in which reference is made to it. The Panel noted that the General Agreement, in referring to government procurement, spoke in terms of 'products for immediate or ultimate consumption in governmental use' (Article XVII:2), and 'procurement by governmental agencies of products purchased for governmental purposes' (Article III:8(a)). The Panel noted that the emphasis in these provisions on the concepts of governmental use, governmental purposes and procurement by government agencies supported its own understanding of the concept of government procurement as explained in paragraph 4.7 below.

"While not intending to offer a definition of government procurement within the meaning of Article I:1(a), the Panel felt that in considering the facts of any particular case the following characteristics, none of which alone could be decisive, provide guidance as to whether a transaction should be regarded as government procurement within the meaning of Article I:1(a): payment by government, governmental use of or benefit from the product, government possession and government control over the obtaining of the product.

"In the present case the European Community suggested that the fact that the procurement of the sonar mapping system would take place by means of a contract between two private companies could lead to the conclusion that it is a private transaction outside the scope of the Agreement. The Panel concurred with the Community's view that this would normally be the case; the purchase by service contractors of products they need in order to be able to render the services contracted for would not normally be government procurement. The fact that government money was used would not necessarily overturn such a view. Nor would the fact that a number of conditions and guarantees relating to the procurement were required by the government necessarily lead to the conclusion that it was procurement by the government; they could simply reflect normal concern for the proper use of government funds.

"However, there were a number of factors in this case which, when taken together, led the Panel to conclude that it was indeed a case of government procurement. The Panel noted first that payment for the system would be made with government money; due to the contractually-prescribed reimbursement of ASA's costs by the NSF, the purchase money for the system remained government money. The amount of the purchase was also specifically determined by the government, with the maximum permissible price legislatively prescribed (Section 307 of P.L. 101-302).

"Secondly, the NSF would take title to the sonar mapping system as of the time of its delivery; at no stage would it become the property of ASA. Having obtained title at the moment of the purchase the NSF, at the expiry of the contract with ASA, would be able to choose whether to continue to use, or to dispose of, the system. Whereas ownership is not a necessary element of government procurement, as is clear from the various methods of procurement mentioned in Article I:1(a), transfer of title to the Government is a strong indication that government procurement is involved. The NSF would also enjoy the benefits of the system's purchase - Antarctic research and the preparation of seabed maps - which were clearly for government purposes, and the Government can thus be regarded as the ultimate beneficiary of the system.

"Thirdly, the Panel noted that the selection of the system was subject to the final approval of the NSF, which also retained the right to cancel the contract between ASA and the supplier of the sonar mapping system, with compensation, at its convenience. Other indicators of the extent of the Government's control of the procurement, perhaps less significant, include the fact that the NSF attached to the procurement many non-technical requirements, some of which could influence the final selection of the system. These requirements include the application of numerous Federal Acquisition Regulations (FARs), including the 'Buy American' domestic sourcing rules, implementing various social and political objectives of the United States Government.

"Fourthly, the Panel noted that the nature of the contract between the NSF and ASA meant that ASA would have no commercial interest in the transaction in the sense of a profit motive or a commercial risk, since it would not directly profit from the selection of the lowest-cost bid among competing manufacturers of sonar mapping systems. In making its selection therefore ASA would be functioning less like a private buyer than like a procurement agency acting on behalf of a third party.

"The Panel concluded that, in the light of the Government's payment for, ownership and use of the sonar mapping system and given the extent of its control over the obtaining of the system, the acquisition of the sonar mapping system was government procurement within the meaning of Article I:1(a), first sentence, and not 'private' procurement outside the Agreement as proposed in the alternative by the European Community."[255]

(b) "not with a view to commercial resale or with a view to use in the production of goods for commercial sale"

At Havana, paragraph 8(a) of Charter Article 18 on national treatment was revised by adding the word "commercial" before "resale" and "sale". This change was brought into the General Agreement in 1948 when the original text of Article III was replaced by the text of Article 18 of the Charter; however, the parallel changes which were made at Havana to paragraph 2 of Article 29 (on government procurement) were not brought over into the text of paragraph 2 of Article XVII.[256]

See also the Interpretative Note to paragraph 2 of Article XVII (non-application of state trading obligations to government procurement) where it is stated in respect of the terms "production of goods" that "The term 'goods' is limited to products as understood in commercial practice, and is not intended to include the purchase or sale of services".

The Report of the Working Party on "Accession of Venezuela" notes that

"Referring to the purchases by state enterprises, some members questioned whether the buy national provisions of Decree 1182 were consistent with the provisions of Articles XVII and III of the General Agreement. A member added that in order to conform to Article III obligations the preference provided by Decree 1182 should only be applied to imports by the State for its own consumption and not to imports by enterprises engaged in normal commerce. ... The representative of Venezuela ... confirming that Decree 1182 provided a buy-Venezuela preference ... noted that its provisions did not distinguish between Government purchases for governmental use and purchases by State enterprises for commercial purposes.

"The representative of Venezuela ... stated that by 30 June 1994, his Government would ensure that Decree 1182 will be brought into conformity with Article III of the General Agreement, and that its application to purchases other than those for ultimate consumption in governmental use would not deny the benefits of Article III to imports from other contracting parties. The representative of Venezuela also stated that if Decree 1182 was still in effect at that time without the above-mentioned actions having been taken, the matter will be reviewed by the CONTRACTING PARTIES. The representative of Venezuela further

[255]GPR.DS1/R, dated 23 April 1992 (unadopted), paras. 4.5-4.13.
[256]Working Party Report on "Modifications to the General Agreement", GATT/CP.2/22/Rev.1, adopted 1-2 September 1948, II/39.

confirmed that his Government would, if requested, consult with interested contracting parties concerning the effect of Decree 1182 on their trade".[257]

(c) Tied loans

See the reference to tied loans above at page 190. A Brazilian proposal in the Review Session that the General Agreement be amended to prohibit tied loans so that funds could be spent in the cheapest markets was not adopted.[258]

See also Interpretative Note ad Article XVII, paragraph 1(b).

A Note relating to Article I:1 of the Agreement on Government Procurement states:

"Having regard to general policy considerations relating to tied aid, including the objective of developing countries with respect to the untying of such aid, this Agreement does not apply to procurement made in furtherance of tied aid to developing countries so long as it is practised by Parties".[259]

(2) Paragraph 8(b): "payment of subsidies exclusively to domestic producers"

The chairman of the working party of Sub-Committee A which redrafted Article 18 at Havana explained that "the Working Party had tried to clarify the wording of sub-paragraph (b). This provision had been added to the Geneva draft because it was felt that if subsidies were paid on domestic and not on imported products, it might be construed that Members were not applying the 'national treatment' rule".[260]

The Report of the Sub-Committee at the Havana Conference which examined Article 18 of the Charter (the text of which constitutes Article III of the General Agreement) notes with respect to paragraph 8(b) that

"This sub-paragraph was redrafted in order to make it clear that nothing in Article 18 could be construed to sanction the exemption of domestic products from internal taxes imposed on like imported products or the remission of such taxes. At the same time the Sub-Committee recorded its view that nothing in this sub-paragraph or elsewhere in Article 18 would override the provisions of Section C of Chapter IV [on Subsidies]".[261]

The 1958 Panel Report on "Italian Discrimination against Agricultural Machinery," which examined the consistency with Article III:4 of an Italian law providing special credit facilities to farmers for the purchase of agricultural machinery produced in Italy, notes that the "Panel agreed with the contention of the United Kingdom delegation that in any case the provisions of paragraph 8(b) would not be applicable to this particular case since the credit facilities provided under the Law were granted to the purchasers of agricultural machinery and could not be considered as subsidies accorded to the producers of agricultural machinery".[262]

The 1990 Panel Report on "European Economic Community - Payments and Subsidies paid to Processors and Producers of Oilseeds and related Animal-Feed Proteins" examined EEC legislation providing for payment of subsidies to processors of oilseeds whenever they established by documentary evidence that they had transformed oilseeds of Community origin.

"The Panel first examined the United States' claim that the payments to processors generate an incentive to purchase domestic rather than imported oilseeds inconsistently with Article III:4. The Panel noted that the Community considers the payments made to processors to be covered by Article III:8(b) which provides that Article III '... shall not prevent the payment of subsidies exclusively to domestic

[257] L/6696, adopted on 11 July 1990, 37S/43, 65-66, paras. 70-71.
[258] SR.9/18, p. 1; see also 3S/243, para. 37.
[259] 26S/55.
[260] E/CONF.2/C.3/A/W.49, p. 2.
[261] Havana Reports, p. 66, para. 69; see also E/CONF.2/C.3/SR.13 p. 1-2.
[262] L/833, adopted on 23 October 1958, 7S/60, 64, para. 14.

producers ...' The Community argues that the payments to processors are made conditional upon the transformation or purchase of domestic oilseeds sold at prices determined by the Community Regulations, are therefore passed on to the producers of domestic oilseeds and consequently constitute producer subsidies within the meaning of that provision.

"The Panel noted that Article III:8(b) applies only to payments made *exclusively* to domestic producers and considered that it can reasonably be assumed that a payment not made directly to producers is not made 'exclusively' to them. It noted moreover that, if the economic benefits generated by the payments granted by the Community can at least partly be retained by the processors of Community oilseeds, the payments generate a benefit conditional upon the purchase of oilseeds of domestic origin inconsistently with Article III:4. Under these circumstances Article III:8(b) would not be applicable because in that case the payments would not be made exclusively to domestic producers but to processors as well."[263]

The 1992 Panel Report on "United States - Measures Affecting Alcoholic and Malt Beverages" examined a United States tax measure providing a credit against excise taxes for small United States producers of beer and wine, which was not available for imported beer and wine. The Panel found that this tax law operated to create lower tax rates on domestic beer and wine than on like imported products.

"The Panel then considered the additional argument of the United States that the lower federal excise tax rate was allowable as a subsidy to domestic producers under Article III:8(b). The United States maintained that the clear intent of the lower tax was to subsidize small producers and that reduction in the rate of the excise tax was a GATT-consistent means of providing such a subsidy....

"The Panel noted that in contrast to Article III:8(a), where it is stated that 'this Article *shall not apply to* ... [government procurement]', the underlined words are not repeated in Article III:8(b). The ordinary meaning of the text of Article III:8(b), especially the use of the words 'shall not prevent', therefore suggests that Article III does apply to subsidies, and that Article III:8(b) only clarifies that the *product-related* rules in paragraphs 1 through 7 of Article III 'shall not prevent the payment of subsidies exclusively to domestic *producers*' (emphasis added). The words 'payment of subsidies' refer only to direct subsidies involving a payment, not to other subsidies such as tax credits or tax reductions. The specific reference to 'payments .... derived from the proceeds of internal taxes ... applied consistently with the provisions of this Article' relates to after-tax-collection payments and also suggests that tax credits and reduced tax rates inconsistent with Article III:2, which neither involve a 'payment' not result in 'proceeds of internal taxes applied consistently with ... this Article', are not covered by Article III:8(b).

"This textual interpretation is confirmed by the context, declared purpose and drafting history of Article III. The context of Article III shows its close interrelationship with the fundamental GATT provisions in Articles I and II and the deliberate separation of the comprehensive national treatment requirements in Article III from the subsidy rules in Article XVI. The most-favoured-nation requirement in Article I, and also tariff bindings under Article II, would become ineffective without the complementary prohibition in Article III on the use of internal taxation and regulation as a discriminatory non-tariff trade barrier. The additional function of the national treatment requirements in Article III to enhance non-discriminatory conditions of competition between imported and domestic products could likewise not be achieved. As any fiscal burden imposed by discriminatory internal taxes on imported goods is likely to entail a trade-distorting advantage for import-competing domestic producers, the prohibition of discriminatory internal taxes in Article III:2 would be ineffective if discriminatory internal taxes on imported products could be generally justified as subsidies for competing domestic producers in terms of Article III:8(b).

"Article III:8(b) limits, therefore, the permissible producer subsidies to 'payments' after taxes have been collected or payments otherwise consistent with Article III. This separation of tax rules, e.g. on tax

[263]L/6627, adopted on 25 January 1990, 37S/86, 124, paras. 136-137.

exemptions or reductions, and subsidy rules makes sense economically and politically. Even if the proceeds from non-discriminatory product taxes may be used for subsequent subsidies, the domestic producer, like his foreign competitors, must pay the product taxes due. The separation of tax and subsidy rules contributes to greater transparency. It also may render abuses of tax policies for protectionist purposes more difficult, as in the case where producer aids require additional legislative or governmental decisions in which the different interests involved can be balanced.

"The Panel considered that the drafting history of Article III confirms the above interpretation. The Havana Reports recall in respect of the provision corresponding to Article III:8(b):

'This sub-paragraph was redrafted in order to make it clear that nothing in Article [III] could be construed to sanction the exemption of domestic products from internal taxes imposed on like imported products or the remission of such taxes. At the same time the Sub-Committee recorded its view that nothing in this sub-paragraph or elsewhere in Article [III] would override the provisions [of Article XVI]'.[264]

"The drafters of Article III explicitly rejected a proposal by Cuba at the Havana Conference to amend the Article to read:

'The provisions of this Article shall not preclude the exemption of domestic products from internal taxes as a means of indirect subsidization in the cases covered under Article [XVI]'.[265]

"The Panel found, therefore, that the expansive interpretation of Article III:8(b) suggested by the United States is not supported by the text, context, declared purpose and drafting history of Article III and, if carried to its logical conclusion, such an interpretation would virtually eliminate the prohibition in Article III:2 of discriminatory internal taxation by enabling contracting parties to exempt all domestic products from indirect taxes. The Panel accordingly found that the reduced federal excise tax rates on beer are not covered by Article III:8(b)."[266]

In the 1994 Panel Report on "United States - Measures Affecting the Importation, Internal Sale and Use of Tobacco", the panel examined a claim regarding the No Net Cost Assessment ("NNCA") levied on domestic and imported tobacco, the proceeds of which were deposited in an account used to reimburse the U.S. Government for any losses resulting from the domestic tobacco price-support programme.

"The Panel was cognizant of the fact that a remission of a tax on a product and the payment of a producer subsidy out of the proceeds of such a tax could have the same economic effects. However, the Panel noted that the distinction in Article III:8(b) is a formal one, not one related to the economic impact of a measure. Thus, in view of the explicit language of Article III:8(b), which recognizes that the product-related rules of Article III 'shall not prevent the payment of subsidies exclusively to domestic producers', the Panel did not consider, as argued by the complainants, that the payment of a subsidy to tobacco producers out of the proceeds of the NNCA resulted in a form of tax remission inconsistent with Article III:2.[267]

...

"The Panel then considered the complainants' claim that the NNCA was inconsistent with Article III:2, second sentence, because the NNCAs charged on imported tobacco reduced the cost of the price support programme to the domestic tobacco producer, without providing any benefit to imported tobacco. The Panel did not consider that it needed to examine this claim in view of the fact that

[264]The footnote to this paragraph refers to Havana Reports, page 66.

[265]The footnote to this paragraph refers to E/CONF.2/C.3/6, page 17; E/CONF.2/C.3/A/W.32, page 2.

[266]DS23/R, adopted 19 June 1992, 39S/206, 271-273, paras. 5.7-5.12.

[267]The footnote to this paragraph notes: "See report of the panel on United States - Measures Affecting Alcoholic and Malt Beverages, adopted on 19 June 1992, BISD 39S/206, 271-273 for a discussion of the reasons for the distinction in GATT between tax exemptions and remissions on the one hand and producer subsidies on the other."

Article III:8(b), which explicitly recognizes that subsidies to domestic producers are not subject to the national treatment rules of Article III, applies to all provisions of Article III, including that of Article III:2, second sentence."[268]

See also material on this panel report above.

9. Paragraph 9

During discussions on this paragraph at Havana it was agreed to retain it in Article 18 [III] "on the grounds that 'internal maximum price control measures' were internal regulations within the terms of paragraphs 1 and 4 of Article 18".[269] At Havana it was also stated that "this provision would apply in the case of a country establishing a maximum control price for a commodity of which that country was such an important consumer that its price was likely to become the effective world price. If such a price were too low, it would be prejudicial to the interests of exporting countries".[270]

The Report of the Working Party on "Accession of El Salvador" contains, *inter alia*, the statement of the representative of El Salvador that "from the date of accession, price regulations would be applied in conformity with Article III:9 of the General Agreement".[271]

10. Paragraph 10

See the chapter on Article IV regarding the background of paragraph 10 and Article IV. The exception in Paragraph 10 to the general provisions of Article III is defined therein as applying to "internal quantitative regulations relating to exposed cinematograph films and meeting the requirements of Article IV". As for taxes on films, the Report of the Working Party on "Accession of the United Arab Republic" discusses a "film tax" in relation to Article III:2 and the Protocol of Provisional Accession.[272] See also references to the New Zealand film hire tax and renters' film quota in Annex A of the General Agreement.

B. RELATIONSHIP WITH OTHER ARTICLES OF THE GENERAL AGREEMENT

1. Article I

The unconditional most-favoured-nation clause in Article I:1 includes within its scope "all matters referred to in paragraphs 2 and 4 of Article III". In response to a request for an interpretation of paragraph 1 of Article I with respect to rebates of excise duties, the Chairman of the CONTRACTING PARTIES ruled on 24 August 1948 that "the most-favoured-nation treatment principle embodied in that paragraph would be applicable to any advantage, favour, privilege or immunity granted with respect to internal taxes".[273] Under the Protocol Amending Part I and Articles XXIX and XXX of the General Agreement, which was agreed in the Review Session of 1954-55, the words "and with respect to the application of internal taxes to exported goods" would have been included in paragraph 1 to remove any uncertainty as to the application of Article I to discrimination in the exemption of exports from the levy of an excise tax.[274] See further under Article I:1.

The 1952 Panel Report on "Belgian Family Allowances" examined a Belgian law providing for a charge to be levied on foreign goods purchased by public bodies when these goods originated in a country whose system of family allowances did not meet specific requirements. Having found that this charge was an internal charge under Article III:2 (see below), the Panel noted:

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[268]DS44/R, adopted 4 October 1994, para. 109, 111.
[269]E/CONF.2/C.3/A/W.49, p. 3; see also E/CONF.2/C.3/A/W.46 and E/CONF.2/C.3/A/W.48 p. 1-2.
[270]E/CONF.2/C.3/A/W.46 p. 3.
[271]L/6771, adopted on 12 December 1990, 37S/9, 21, para. 36.
[272]L/3362, adopted on 27 February 1970, 17S/33, 37, para. 17.
[273]II/12, CP.2/SR.11, CP.3/SR.19.
[274]3S/206, para. 3. This Protocol was abandoned as of 31 December 1967; see 15S/65.

"Belgium has granted exemption from the levy under consideration to products purchased by public bodies when they originate in Luxemburg and the Netherlands, as well as in France, Italy, Sweden and the United Kingdom. If the General Agreement were definitively in force in accordance with Article XXVI, that exemption would have to be granted unconditionally to all other contracting parties. ... The consistency or not of the system of family allowances in force in the territory of a given contracting party with the requirements of the Belgian law would be irrelevant in this respect, and the Belgian legislation would have to be amended insofar as it introduced a discrimination between countries having a given system of family allowances and those which had a different system or no system at all, and made the granting of an exemption dependent on certain conditions".[275]

See also the Note *Ad* Article I:1, which provides that "The obligations incorporated in paragraph 1 of Article I by reference to paragraphs 2 and 4 of Article III ... shall be considered as falling within Part II for the purposes of the Protocol of Provisional Application". See further on page 204 below.

The 1987 Panel Report on "Japan - Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages" examined, *inter alia*, a claim by the EEC under Article III:1 and 2 with respect to these duties, taxes and labelling practices. In interpreting Article III:2, the Panel examined its context:

"The *context* of Article III:2 shows that Article III:2 supplements, within the system of the General Agreement, the provisions on the liberalization of customs duties and of other charges by prohibiting discriminatory or protective taxation against certain products from other GATT contracting parties. ... For instance, the prohibition under GATT Article I:1 of different tariff treatment for various types of 'like' products (such as unroasted coffee, see BISD 28S/102, 112) could not remain effective unless supplemented by the prohibition of different internal tax treatment for various types of 'like' products. ... Article I:1 was generally construed, in order to protect the competitive benefits accruing from reciprocal tariff bindings, as prohibiting 'tariff specialization' discriminating against 'like' products".[276]

The 1990 Panel Report on "EEC - Regulation on Imports of Parts and Components" examined, *inter alia*, a claim by Japan that since the EEC Regulation at issue provided for imposition of duties on products produced or assembled in the EEC on the basis of the proportion of parts imported from Japan used in production or assembly of such products, imposition of duties or acceptance of undertakings under that Regulation was inconsistent with Articles I and II or III. The Panel "found that the anti-circumvention duties are not levied 'on or in connection with importation' within the meaning of Article II:1(b), and therefore do not constitute customs duties within the meaning of that provision".[277] It then "found that the anti-circumvention duties are inconsistent with Article III:2, first sentence, [and] saw no need for examining whether the anti-circumvention duties are also inconsistent with the obligations of the EEC under Article III:2, second sentence, and Article I:1".[278] The Panel "found the acceptance by the EEC of parts undertakings limiting the use of imported parts and components to be inconsistent with Article III:4, [and therefore] saw no need for examining whether the acceptance of such undertakings is also inconsistent with Article I:1 of the General Agreement".[279]

See also the discussion of the relation between Article I and III in the unadopted 1994 Panel Report on "EEC - Import Régime for Bananas".[280]

2. Article II

A number of panels have examined whether a measure was an internal tax or charge (under Article III) or a duty or charge "imposed on or in connection with importation" (under Article II). In the 1952 Panel

[275] G/32, adopted on 7 November 1952, 1S/59, 60, para. 3.
[276] L/6216, adopted on 10 November 1987, 34S/83, 113-114, para. 5.5(b).
[277] L/6657, adopted on 16 May 1990, 37S/132, 193 para. 5.8.
[278] *Ibid.*, 37S/193-194, para. 5.10.
[279] *Ibid.*, 37S/197-198, para. 5.22.
[280] DS38/R, dated 11 February 1994, paras. 143-148.

Report on "Belgian Family Allowances" the Panel began by examining the nature of the Belgian law in question:

> "After examining the legal provisions regarding the methods of collection of that charge, the Panel came to the conclusion that the 7.5 per cent levy was collected only on products purchased by public bodies for their own use and not on imports as such, and that the levy was charged, not at the time of importation, but when the purchase price was paid by the public body. In those circumstances, it would appear that the levy was to be treated as an 'internal charge' within the meaning of paragraph 2 of Article III of the General Agreement, and not as an import charge within the meaning of paragraph 2 of Article II".[281]

The 1978 Panel Report on "EEC - Measures on Animal Feed Proteins" examined an EEC Regulation requiring domestic producers or importers of oilseeds, cakes and meals, dehydrated fodder and compound feeds and importers of corn gluten feed to purchase a certain quantity of surplus skimmed milk powder held by intervention agencies and to have it denatured for use as feed for animals other than calves. The Panel examined the consistency with Articles II and III of these aspects of the Regulation and of the requirement for producers and importers to present either a protein certificate (certifying the purchase and denaturing of a certain quantity of milk powder) or a security deposit.

> "The Panel ... considered the question of whether the EEC measures should be examined both as internal measures under Article III and border measures under Article II. In this regard, the Panel reviewed the drafting history of Articles II and III and their subsequent application by contracting parties, particularly with a view to ascertaining the relationship between these two Articles...
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> "The Panel also recalled its own findings that (a) the EEC measures applied to both imported and domestically produced vegetable proteins (except in the case of corn gluten); (b) the EEC measures basically instituted an obligation to purchase a certain quantity of skimmed milk powder and, as an 'internal quantitative regulation' fell under Article III:1; (c) the EEC security deposit and protein certificate were enforcement mechanisms for the purchase obligation.
>
> "Having regard to the legal considerations referred to above and taking account of its own findings in relation to Article III:5 and Article III:1 that the EEC measures were an 'internal quantitative regulation', the Panel concluded that the EEC measures should be examined as internal measures under Article III and not as border measures under Article II".[282]

In the 1985 Panel Report on "Canada - Measures Affecting the Sale of Gold Coins," which has not been adopted,

> "The Panel noted that Articles III and II of the General Agreement distinguish between charges applied to products 'imported into the territory of any other contracting party' (Article III:2) and charges 'imposed on or in connection with importation' (Article II:1(b) ... The Panel noted that the Ontario retail sales tax is levied at the time of retail sale of goods within the province, not at the time of importation into Canadian territory (see para. 5 above). The Ontario measure thus affects the internal retail sale of gold coins rather than the importation of Krugerrands as such. The Panel therefore considered that the tax was an 'internal tax' to be considered under Article III and not an 'import charge' to be considered under Article II".[283]

The 1988 Panel Report on "Canada - Import, Distribution and Sale of Alcoholic Drinks by Canadian Provincial Marketing Agencies"

> "...noted that Article 31:6 of the Havana Charter provided that 'in applying the provisions of this Article, due regard shall be had for the fact that some monopolies are established and operated mainly

[281]G/32, adopted on 7 November 1952, 1S/59, 60, para. 2. See also page 191, 197 above.
[282]L/4599, adopted on 14 March 1978, 25S/49, 66-67, paras. 4.15, 4.17, 4.18.
[283]L/5863, unadopted, dated 17 September 1985, para. 50.

for social, cultural, humanitarian or revenue purposes'. While the drafting history indicated that Article 31 should be applied to the extent that it was relevant to the context of the General Agreement, the Panel considered that Canada had the right to use import monopolies to raise revenue for the provinces, consistently with the provisions of the General Agreement. The Panel also considered that its conclusions on Article II:4 did not affect this right, because Article II:4, applied in the light of Article 31:4 of the Charter, permitted the charging of internal taxes conforming to the provisions of Article III. It noted that federal and provincial sales taxes were levied on alcoholic beverages and asked itself whether the fiscal elements of mark-ups, which produced revenue for the provinces, could also be justified as 'internal taxes conforming to the provisions of Article III', noting that Article III:2 also referred, not only to 'internal taxes', but also to 'other internal charges.' The panel was of the view that to be so considered, the fiscal element of mark-ups must of course meet the requirements of Article III, e.g., they must not be applied to imported or domestic products so as to afford protection to domestic production. The Panel also considered it important that, if fiscal elements were to be considered as internal taxes, mark-ups would also have to be administered in conformity with other provisions of the General Agreement, in particular Article X dealing with the Publication and Administration of Trade Regulations".[284]

In the 1990 Panel Report on "EEC - Regulation on Imports of Parts and Components," the Panel examined the argument of the EEC that the anti-circumvention duties at issue were customs or other duties imposed "on or in connection with importation" under Article II:1(b), or internal taxes or charges falling under Article III:2.

"The Panel noted that the anti-circumvention duties are levied, according to Article 13:10(a), 'on products that are introduced into the commerce of the Community after having been assembled or produced in the Community'. The duties are thus imposed, as the EEC explained before the Panel, not on imported parts or materials but on the finished products assembled or produced in the EEC. They are not imposed conditional upon the importation of a product or at the time or point of importation. The EEC considers that the anti-circumvention duties should, nevertheless, be regarded as customs duties imposed 'in connection with importation' within the meaning of Article II:1(b). The main arguments the EEC advanced in support of this view were: firstly, that the purpose of these duties was to eliminate circumvention of anti-dumping duties on finished products and that their nature was identical to the nature of the anti-dumping duties they were intended to enforce; and secondly, that the duties were collected by the customs authorities under procedures identical to those applied for the collection of customs duties, formed part of the resources of the EEC in the same way as customs duties and related to parts and materials which were not considered to be 'in free circulation' within the EEC.

"In the light of the above facts and arguments, the Panel first examined whether the *policy purpose of a charge* is relevant to determining the issue of whether the charge is imposed 'in connection with importation' within the meaning of Article II:1(b). The text of Articles I, II, III and the Note to Article III refers to charges 'imposed on importation', 'collected ... at the time or point of importation' and applied 'to an imported product and to the like domestic product'. The relevant fact, according to the text of these provisions, is not the policy purpose attributed to the charge but rather whether the charge is due on importation or at the time or point of importation or whether it is collected internally. This reading of Articles II and III is supported by their drafting history and by previous panel reports (e.g. BISD 1S/60; 25S/49, 67). ... The Panel further noted that the policy purpose of charges is frequently difficult to determine objectively. Many charges could be regarded as serving both internal purposes and purposes related to the importation of goods. Only at the expense of creating substantial legal uncertainty could the policy purpose of a charge be considered to be relevant in determining whether the charge falls under Article II:1(b) or Article III:2. The Panel therefore concluded that the policy purpose of the charge is not relevant to determining the issue of whether the charge is imposed in 'connection with importation' within the meaning of Article II:1(b).

[284]L/6304, adopted on 22 March 1988, 35S/37, 88-89, para. 4.20.

"The Panel proceeded to examine whether the mere *description or categorization of a charge under the domestic law* of a contracting party is relevant to determining the issue of whether it is subject to requirements of Article II or those of Article III:2. The Panel noted that if the description or categorization of a charge under the domestic law of a contracting party were to provide the required 'connection with importation', contracting parties could determine themselves which of these provisions would apply to their charges. They could in particular impose charges on products after their importation simply by assigning the collection of these charges to their customs administration and allocating the revenue generated to their customs revenue. With such an interpretation the basic objective underlying Articles II and III, namely that discrimination against products from other contracting parties should only take the form of ordinary customs duties imposed on or in connection with importation and not the form of internal taxes, could not be achieved. The same reasoning applies to the *description or categorization of the product subject to a charge*. The fact that the EEC treats imported parts and materials subject to anti-circumvention duties as not being 'in free circulation' therefore cannot, in the view of the Panel, support the conclusion that the anti-circumvention duties are being levied 'in connection with importation' within the meaning of Article II:1(b).

"In the light of the above, the Panel found that the anti-circumvention duties are not levied 'on or in connection with importation' within the meaning of Article II:1(b), and consequently do not constitute customs duties within the meaning of that provision."[285]

3. Article XI

The Working Party on "The Haitian Tobacco Monopoly" in 1955 examined whether the licensing of tobacco imports by the Tobacco Régie required a release under the provisions of Article XVIII:12 (prior to the Review Session amendments to Article XVIII). "The representative of Haiti declared that the licensing system served solely to enforce the internal quantitative regulations of the Régie and did not impose any additional limitation of the quantity that may be imported. The Working Party therefore took the view that in these circumstances Article XI would not apply, that the import control should be considered under the terms of the exception in Article [XX:(d)] and that the internal regulation to which it relates should be considered under paragraphs 5 and 6 of Article III."[286] See also the references to this case above in the material on mixing regulations; see also the reference to border enforcement of mixing regulations under the Interpretative Note Ad Article III.

The 1984 Panel Report on "Canada - Administration of the Foreign Investment Review Act" notes that

"The Panel shares the view of Canada that the General Agreement distinguishes between measures affecting the 'importation' of products, which are regulated in Article XI:1, and those affecting 'imported products', which are dealt with in Article III. If Article XI:1 were interpreted broadly to cover also internal requirements, Article III would be partly superfluous. Moreover, the exceptions to Article XI:1, in particular those contained in Article XI:2, would also apply to internal requirements restricting imports, which would be contrary to the basic aim of Article III. The Panel did not find, either in the drafting history of the General Agreement or in previous cases examined by the CONTRACTING PARTIES, any evidence justifying such an interpretation of Article XI. For these reasons, the Panel, noting that purchase undertakings do not prevent the importation of goods as such, reached the conclusion that they are not inconsistent with Article XI:1".[287]

The 1987 Panel Report on "United States - Taxes on Petroleum and Certain Imported Substances" provides that "The general prohibition of quantitative restrictions under Article XI .... and the national

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[285]L/6657, adopted on 16 May 1990, 37S/132, 192-93, paras. 5.5-5.8. The "previous panel reports" referred to in para. 5.6 are the Reports on "Belgian Family Allowances", G/32, adopted on 7 November 1952, 1S/59, 60, para. 2, and "EEC - Measures on Animal Feed Proteins", L/4599, adopted on 14 March 1978, 25S/49, 67, paras. 4.16-4.18.

[286]L/454, adopted on 22 November 1955, 4S/38, 39, para. 9. Before the revision of Article XVIII in the Review Session, Article XVIII:12 provided for notification and concurrence with regard to certain measures affecting imports which were not otherwise permitted by the General Agreement.

[287]L/5504, adopted on 7 February 1984, 30S/140, 162-163, para. 5.14.

treatment obligation of Article III ... have essentially the same rationale, namely to protect expectations of the contracting parties as to the competitive relationship between their products and those of other contracting parties. Both articles are not only to protect current trade but also create the predictability needed to plan future trade".[288]

A series of three cases in 1988 and 1992 examined the application of Articles III and XI to regulations affecting imported alcoholic beverages in Canada and the United States. The 1988 Panel Report on "Canada - Import, Distribution and Sale of Alcoholic Drinks by Provincial Marketing Agencies" provides that

> "The Panel ... *concluded* that the practices concerning listing/delisting requirements and the availability of points of sale which discriminate against imported alcoholic beverages were restrictions made effective through state-trading operations contrary to Article XI:1. ...
>
> "The Panel then examined the contention of the European Communities that the practices complained of were contrary to Article III. The Panel noted that Canada did not consider Article III to be relevant to this case, arguing that the Interpretative Note to Articles XI, XII, XIII, XIV and XVIII made it clear that provisions other than Article XVII applied to state-trading enterprises by specific reference only. The Panel considered that it was not necessary to decide in this particular case whether the practices complained of were contrary to Article III:4 because it had already found that they were inconsistent with Article XI. However, the Panel saw great force in the argument that Article III:4 was also applicable to state-trading enterprises at least when the monopoly of the importation and monopoly of the distribution in the domestic markets were combined, as was the case of the provincial liquor boards in Canada. This interpretation was confirmed *e contrario* by the wording of Article III:8(a)".[289]

The 1992 Panel Report on "Canada - Import, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies" examined a United States claim that the practice of the liquor boards of Ontario to limit listing of imported beer to the six-pack size while according listings in different package sizes to domestic beer was inconsistent with the General Agreement.

> "... The Panel noted that this package-size requirement, though implemented as a listing requirement, was in fact a requirement that did not affect the importation of beer as such but rather its offering for sale in certain liquor-board outlets. The Panel therefore considered that this requirement fell under Article III:4 of the General Agreement, which required, *inter alia*, that contracting parties accord to imported products '... treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal ... offering for sale ...'. The Panel *found* that the imposition of the six-pack configuration requirement on imported beer but not on domestic beer was inconsistent with that provision."[290]

With respect to restrictions imposed by provincial liquor authorities on access for imported beer to points of sale (with respect to which Canada invoked the Protocol of Provisional Application):

> "The Panel which had examined in 1988 the practices of the Canadian liquor boards had analysed the restrictions on access to points of sale under Articles III:4 and XI:1 of the General Agreement. While that Panel had found these restrictions to be inconsistent with Canada's obligations under Article XI:1, it had also pointed out that it 'saw great force in the argument that Article III:4 was also applicable to State-trading enterprises at least when the monopoly of the importation and monopoly of the distribution in the domestic markets were combined, as was the case of the provincial liquor boards in Canada'. The present Panel, noting that Canada now considered Article III:4 to be applicable to practices of the liquor boards, examined this issue again. ... The Panel found that, by allowing the access of domestic beer to points of sale not available to imported beer, Canada accorded domestic beer competitive opportunities

[288] L/6175, adopted on 17 June 1987, 34S/136, 160, para. 5.2.2; see also reference to this passage in Panel Report on "European Economic Community - Payments and Subsidies paid to Processors and Producers of Oilseeds and related Animal-Feed Proteins", L/6627, adopted on 25 January 1990, 37S/86, 130, para. 150.

[289] L/6304, adopted 22 March 1988, 35S/37, 89-90, paras. 4.25-4.26.

[290] DS17/R, adopted 18 February 1992, 39S/27, 75, para. 5.4.

denied to imported beer. For these reasons the present Panel saw great force in the argument that the restrictions on access to points of sale were covered by Article III:4. However, the Panel considered that it was not necessary to decide whether the restrictions fell under Article XI:1 or Article III:4 because Canada was not invoking an exception to the General Agreement applicable only to measures taken under Article XI:1 (such as the exceptions in Articles XI:2 and XII) and the question of whether the restrictions violated Article III:4 or Article XI:1 of the General Agreement was therefore of no practical consequence in the present case".[291]

The Panel also examined minimum prices maintained for beer in certain provinces of Canada.

"The Panel first examined whether the minimum prices fell under Article XI:1 or Article III:4. The Panel noted that according to the Note Ad Article III a regulation is subject to the provisions of Article III if it 'applies to an imported product and to the like domestic product' even if it is 'enforced in case of the imported product at the time or point of importation'. The Panel found that, as the minimum prices were applied to both imported and domestic beer, they fell, according to this Note under Article III."[292]

The 1992 Panel on "United States - Measures Affecting Alcoholic and Malt Beverages" examined the listing requirements of state-operated liquor stores in certain US states:

"Having regard to the past panel decisions and the record in the instant case, the present Panel was of the view that the listing and delisting practices here at issue do not affect importation as such into the United States and should be examined under Article III:4. The Panel further noted that the issue is not whether the practices in the various states affect the right of importation as such, in that they clearly apply to both domestic (out-of-state) and imported wines; rather, the issue is whether the listing and delisting practices accord less favourable treatment – in terms of competitive opportunities – to imported wine than that accorded to the like domestic product. Consequently, the Panel decided to analyze the state listing and delisting practices as internal measures under Article III:4".[293]

The 1991 Panel Report on "United States - Restrictions on Imports of Tuna," which has not been adopted, examined the relationship between Articles III and XI, and found that the restrictions at issue were governed not by Article III but by Article XI.

"The Panel noted that Mexico had argued that the measures prohibiting imports of certain yellowfin tuna and yellowfin tuna products from Mexico imposed by the United States were quantitative restrictions on importation under Article XI, while the United States had argued that these measures were internal regulations enforced at the time or point of importation under Article III:4 and the Note *Ad* Article III, namely that the prohibition of imports of tuna and tuna products from Mexico constituted an enforcement of the regulations of the MMPA relating to the harvesting of domestic tuna.

"The Panel examined the distinction between quantitative restrictions on importation and internal measures applied at the time or point of importation, and noted the following. While restrictions on importation are prohibited by Article XI:1, contracting parties are permitted by Article III:4 and the Note *Ad* Article III to impose an internal regulation on products imported from other contracting parties provided that it: does not discriminate between products of other countries in violation of the most-favoured-nation principle of Article I:1; is not applied so as to afford protection to domestic production, in violation of the national treatment principle of Article III:1; and accords to imported products treatment no less favourable than that accorded to like products of national origin, consistent with Article III:4. …

"… The Panel noted that the MMPA regulates the domestic harvesting of yellowfin tuna to reduce the incidental taking of dolphin, but that these regulations could not be regarded as being applied to tuna

[291] *Ibid.*, 39S/75-76, para. 5.6.
[292] *Ibid*, 39S/84, para. 5.28.
[293] DS23/R, adopted 19 June 1992, 39S/206, 292, para. 5.63.

products as such because they would not directly regulate the sale of tuna and could not possibly affect tuna as a product. Therefore, the Panel found that the import prohibition on certain yellowfin tuna and certain yellowfin tuna products of Mexico and the provisions of the MMPA under which it is imposed did not constitute internal regulations covered by the Note *Ad* Article III."[294]

In this connection see also the unadopted panel report of 1994 on "United States - Restrictions on Imports of Tuna".[295]

4. Article XVII

See under Article XVII.

5. Article XX(d)

See under Article XX.

6. **Article XXIV:12**

See under Article XXIV.

7. Part IV

See under Part IV.

C. EXCEPTIONS AND DEROGATIONS

1. Exceptions to the scope of the national treatment requirement

See discussion above of paragraphs 3, 6, 8 and 10 of Article III.

2. Protocol of Provisional Application

The Report of the Working Party on "Brazilian Internal Taxes" notes that the majority of the members of the Working Party took the view

"... that the Protocol of Provisional Application limited the operation of Article III only in the sense that it permitted the retention of an absolute difference in the level of taxes applied to domestic and imported products, required by existing legislation, and that no subsequent change in legislation should have the effect of increasing the absolute margin of difference".[296]

The Interpretative Note to Article I paragraph 1 provides that "The obligations incorporated in paragraph 1 of Article I by reference to paragraphs 2 and 4 of Article III ... shall be considered as falling within Part II for the purposes of the Protocol of Provisional Application". The objective of this provision, which was based on a proposal by the US delegation, was to reserve legislation regarding preferential internal taxes until definitive acceptance of the Agreement.[297] Similar provisions appear in the standard text of protocols of access; see discussion under Article I.

[294]DS21/R (unadopted) dated 3 September 1991, 39S/155, 193, 195, paras. 5.8-5.9, 5.14.
[295]DS29/R, dated 16 June 1994, para. 5.8-5.9.
[296]GATT/CP.3/42, adopted 30 June 1949, II/181, 183, para. 12.
[297]Proposal at EPCT/W/343; discussion at EPCT/TAC/PV/26, p. 9-11 (referring to preferential internal tax on processing of coconut oil from the Philippines, later notified as measure under the Protocol of Provisional Application; see L/309/Add.2).

3. Protocols of accession

Paragraph 3 of the Protocol for the Accession of the Philippines to the General Agreement provides as follows.

> "The Philippines intends to bring into line with Article III of the General Agreement, the sales and specific taxes with respect to the items listed in document L/4724/Add.1 whose rates, in accordance with the relevant sections of Titles IV and V of the Philippines Internal Revenue Code in force on the date of this Protocol, vary according to whether the items are locally manufactured or imported and will endeavour to do so as soon as possible in the light of its development, financial and trade needs. If by 31 December 1984, the above-mentioned taxes are still in effect with differential rates for imported items, the matter will be reviewed by the CONTRACTING PARTIES."[298]

A Decision of the CONTRACTING PARTIES of 27 November 1984[299] extended this time-limit until 31 December 1989; a Decision of 4 December 1989[300] further extended this time-limit until 31 December 1991 at which point it lapsed; consensus was not reached on a further extension.[301]

Paragraph 3 of the Protocol for the Accession of Thailand to the General Agreement provides as follows.

> "Thailand intends to bring into line with Article III of the General Agreement, the business and excise taxes with respect to items on which the incidence of these taxes varies according to whether the items are locally produced or imported, and will endeavour to do so as soon as possible in the light of the provisions of Part IV, and in particular Thailand's development, financial and trade needs. If by 30 June 1987, the incidence of the above-mentioned taxes still varies as between locally produced and imported items, the matter will be reviewed by the CONTRACTING PARTIES."[302]

A Decision of the CONTRACTING PARTIES of 17 June 1987[303] extended this time-limit to 30 June 1990; a Decision of 3 October 1990[304] retroactively extended this time-limit until 31 December 1991 at which point it lapsed.

III. PREPARATORY WORK AND SUBSEQUENT MODIFICATIONS

The US-UK *Proposals* provided in section III.A that "Members should undertake: 1. To accord to products imported from other members treatment no less favorable than that accorded to domestic products with regard to matters affecting the internal taxation and regulation of the trade in goods". This principle was elaborated in Article 9 of the US Draft Charter. These provisions were debated at London in the Technical Sub-Committee of Committee II and were redrafted by an ad-hoc group of rapporteurs; however, no national treatment article appeared in the London Draft Charter, as the drafting of this and most of the other general commercial provisions was deferred until the New York meetings of the Drafting Committee. After further work in the Drafting Committee, provisions on national treatment appeared as Article 15 of the New York Draft Charter. At Geneva, the national treatment article was considered in the plenary sessions of Commission A and in an ad-hoc Sub-Committee on the Charter articles on most-favoured-nation treatment, national treatment and tariff negotiations; this article appeared as Article 18 of the Geneva Charter. It was at this time that the provisions on films were separated into a different article. Article III of the original General Agreement text of 30 October 1947 corresponded almost exactly to Article 18 of the Geneva Draft Charter.

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[298] 26S/193, para. 3.
[299] L/5741, 31S/7; see C/M/183.
[300] L/6619, 36S/44; see C/M/237.
[301] W.47/23, SR.47/3 p. 6, C/W/694, C/M/254, p. 6-7.
[302] 29S/4, para. 3.
[303] L/6190, 34S/28; see C/M/211.
[304] L/6736, 37S/29; see C/M/243, C/M/244, C/M/245 p. 22.

At the Havana Conference, extensive debates on this provision of the Charter took place in the Third Committee, in its Sub-Committee A on Tariff Negotiations, Internal Taxation and Regulation, and Working Party 3 of the Sub-Committee which focused exclusively on national treatment. As the Chairman of Sub-Committee A stated:

> "... the text of Article 18 had been recast, because the Geneva text, in itself the result of many compromises, was somewhat cryptic and obscure. The text recommended by the Sub-Committee differed considerably in form from the original, but there was only one important change of substance. In the Geneva text discriminatory internal taxes which afforded protection to directly competitive or substitutable products in cases in which there was no substantial domestic production of the like product could be maintained subject to negotiations, but the Sub-Committee recommended their outright elimination as a sounder principle. Members would, of course, be free to convert the protective element of such taxes into customs duties".[305]

The Report of Sub-Committee A adds that "The new form of the Article makes clearer than did the Geneva text the intention that internal taxes on goods should not be used as a means of protection".[306]

The CONTRACTING PARTIES at their Second Session in September 1948 decided to replace the original text of Article III with the text of Article 18 of the Charter *mutatis mutandis*. The Working Party on "Modifications to the General Agreement" "noted that administrative difficulties might arise in the case of countries which would have to change their fiscal regulations twice - on acceptance of the Agreement, and again on ratification of the Charter. ... it recognized that the wording adopted at Havana was clearer and more precise than the text as it now stood".[307] These changes were effected through the Protocol Modifying Part II and Article XXVI, which entered into force 14 December 1948. Article III has not been amended since that date.

The Review Session Working Party on "Schedules and Customs Administration" in 1954-55 considered and rejected various proposals for the insertion of interpretative notes to Article III; see above at pages 144, 184 and 188.[308] It was agreed at the Review Session to insert the provisions of Article IV (on cinematographic films) into paragraph 10 of Article III with no substantive change.[309] However, as this amendment was made contingent on the entry into force of the Protocol Amending Part I and Article XXIX, which did not achieve the requisite unanimous approval and was abandoned, this amendment never entered into force.

[305]E/CONF.2/C.3/SR.40 p. 1.
[306]Havana Reports, p. 61, para. 36.
[307]GATT/CP.2/22/Rev.1, adopted 1 and 2 September 1948, II/39, 40-41, para. 11.
[308]See also Report of this Working Party, L/329, adopted 26 February 1955, 3S/205, 210-211, paras. 9-11.
[309]See W.9/236 (changes proposed by the Legal and Drafting Committee).

IV. RELEVANT DOCUMENTS

London

Discussion:	EPCT/C.II/PV/10 (p. 53), 13 (p. 51)
Reports:	EPCT/C.II/64, EPCT/C.II/54/Rev.1, pp. 4-5
Other:	EPCT/C.II/W.2, 5, 14

New York

Discussion:	EPCT/C.6/6, 8, 84
Reports:	EPCT/C.6/55/Rev.1, 97/Rev.1

Geneva

Discussion:	EPCT/EC/SR.2/3, 22 EPCT/A/SR/9+Corr.1, 10+Corr.1-4, 22, 23, 26, 43 EPCT/A/PV/22+Corr.1-5, 23+Corr.1-2, 26+Corr.1-3 EPCT/B/SR.22 EPCT/WP.1/SR/11 EPCT/TAC/SR.10 EPCT/TAC/PV/26 (p.29)
Reports:	EPCT/127, 162, 174, 178, 180, 186
Other:	EPCT/W/23, 25, 26, 28, 29, 30, 48, 56, 62, 79, 92, 99, 106, 112, 147,149, 150, 181, 267, 272, 280, 301, 309, 313

Havana

Discussion:	E/CONF.2/C.3/SR.9, 11, 13, 40, 41, 42
Reports:	E/CONF.2/C.3/59, 71
Other:	E/CONF.2/C.3/A/W.30 to 35, 38, 39, 46 to 50

CONTRACTING PARTIES

Discussion:	GATT/CP.3/SR.9, 10, 30 GATT/CP.5/SR.6/21
Reports:	GATT/CP.3/42 GATT/CP.5/37 G/25

Review Session

Discussion:	SR.9/18, 20
Reports:	W.9/193+Corr.1, 200, 212+Corr.1, 236+Add.1, L/329, 3S/205
Other:	L/189+Add.1, 261/Add.1, 275 W.9/45 Spec/3/55, 85/55, 94/55