CANADA – MEASURES GOVERNING THE SALE OF WINE

(DS537)

THIRD PARTY EXECUTIVE SUMMARY OF THE UNITED STATES OF AMERICA

August 19, 2019

EXECUTIVE SUMMARY OF THE U.S. THIRD PARTY WRITTEN SUBMISSION

I. INTERPRETATION AND APPLICATION OF THE FIRST SENTENCE OF ARTICLE III:2 OF THE GATT 1994

1. Canada contends that "the Appellate Body's conclusion [in *Japan – Alcoholic Beverages II*] that a tax on an imported product that is 'in excess' of the tax on the like domestic product must be 'deemed' to afford protection to domestic production should not be interpreted as a mechanical calculation automatically resulting in a violation, but a conclusion to be drawn unless it could be demonstrated otherwise." Canada emphasizes that, "[s]imilar to the question in Article III:4 whether differential treatment results in less favourable treatment, the critical issue is whether the difference in taxation levels affects the conditions of competition." Canada is incorrect, and Canada's arguments are beside the point.

2. Canada fails to focus on the text of the first sentence of Article III:2 of the GATT 1994 – the provision under which Australia has brought its claims against the federal and Ontario tax measures, as well as the Nova Scotia reduced product mark-up measure. Instead, Canada appears to argue that analytical frameworks elaborated in prior dispute settlement reports to assess claims under Article III:4 of the GATT 1994 should also be used when assessing Australia's claims under the first sentence of Article III:2 of the GATT 1994. However, while Article III:4 of the GATT 1994 requires that imports be accorded "treatment no less favourable" than that accorded to like domestic products, the term "treatment no less favourable" – which is the textual basis for conducting a conditions of competition analysis under Article III:4 – is absent from the first sentence of Article III:2 of the GATT 1994. Because the term "treatment no less favourable" is absent from the first sentence of Article III:2, it is unnecessary to establish that differential taxation modifies the conditions of competition to find that a measure is inconsistent with the first sentence of Article III:2.

3. If an internal tax or charge applied to imported products is found to be "in excess" of that which is applied to like domestic products, and the respondent cannot rebut the evidence demonstrating that such an internal tax or charge is applied "in excess," then the inquiry ends for purposes of the first sentence of Article III:2. Canada disputes this straightforward interpretation of the plain text of the first sentence of Article III:2 of the GATT 1994. Canada "submits that preserving the link between Article III:2, first sentence and Article III:1 requires that a responding party be given an opportunity to rebut the presumption that taxing an imported product 'in excess' of the like domestic product results in protection being afforded to domestic production."

4. The weakness of Canada's argument is revealed by the terminology Canada uses in mounting its defense. Canada asserts that the interpretation of Article III:2 is "coloured by Article III:1", that the terminology of Article III:1 "implies that for a measure to 'afford protection' it must actually affect the competitive relationship between products", and that "the overall purpose of Article III is to ensure that measures are not applied to imported or domestic products so as to afford protection to domestic production and that this general principle informs the rest of Article III". None of Canada's general observations relate to – nor do they alter – the particular terms that actually are present in the first sentence of Article III:2 of the GATT 1994.

5. Rather than impose an additional *condition* for a claim under Article III:2, the context of Article III:1 ("should not be applied … so as to afford protection") suggests that the straightforward obligation of Article III:2 ("shall not be subject … in excess of") is a situation in which protection is afforded. All of Canada's discussion of whether the alleged internal taxes or charges "afford protection" as a separate inquiry is irrelevant to the Panel's disposition of Australia's claims under the first sentence of Article III:2 of the GATT 1994. If Canada has direct evidence that its measures do not impose internal taxes or charges on imports "in excess of" like domestic products, Canada should rebut Australia's case by presenting that evidence.

II. INTERPRETATION AND APPLICATION OF ARTICLE III:4 OF THE GATT 1994

6. The final element of the analysis under Article III:4 of the GATT 1994 concerns whether the measures at issue accord less favorable treatment to imported products than to domestic like products. Prior reports have explained that this is determined "by examining whether a measure modifies the conditions of competition in the relevant market to the detriment of imported products." The Appellate Body has emphasized the "implications" of the measure on the conditions of competition, which underscores that Article III:4 of the GATT 1994 does not require a demonstration of the current, "actual effects of the measure at issue in the internal market of the Member concerned."

7. Because a demonstration of "actual effects" is not required, then establishing the "potential effects," discernible from the "design, structure, and expected operation of the measure," could satisfy the requirements for a successful *de facto* claim under Article III:4. Canada attempts to set an unduly high bar for proving a *de facto* claim under Article III:4 by arguing that a complainant must show "actual effects" of discrimination. Canada's position is not supported by the terms of Article III:4 nor by prior reports.

8. Canada relies on the Appellate Body report in *Korea – Various Measures on Beef* for the proposition that "formal separation [of distribution channels], *in and of itself*, does not necessarily compel the conclusion that the treatment accorded to imported beef is less favorable than the treatment accorded to domestic beef." Canada reasons from this that it is "axiomatic that, in each case, the complainant must adduce evidence to demonstrate that the measure at issue has in fact resulted in a change in competitive conditions to the detriment of the imported product." Canada's reasoning is correct, as far as it goes. However, the Appellate Body went on in *Korea – Various Measures on Beef* to find that "[t]he central consequence of the dual retail system can only be reasonably construed … as the imposition of a drastic reduction of commercial opportunity to reach, and hence to generate sales to, the same consumers served by the traditional retail channels for domestic beef." The Appellate Body emphasized that "the reduction of competitive opportunity through the restriction of access to consumers results from the imposition of the dual retail system." Thus, while a formal difference in treatment may not, in and of itself, be sufficient to establish less favorable treatment, the conclusion that treatment is less favorable can be reached through the application of logic and reasoning, without necessarily, in all cases, having recourse to trade data or economic analysis.

9. Canada also relies on the Appellate Body report in *Thailand – Cigarettes (Philippines)* for the proposition that the Article III:4 analysis "may well involve —but does not require—an assessment of the contested measure in the light of evidence regarding the actual effects of that

measure in the market." Then Canada appears to mischaracterize the same language, in the next paragraph of Canada's first written submission, arguing that Australia's approach in this dispute "does not accord with the advice of the Appellate Body on the need for evidence of 'actual effects'." But the passage of the Appellate Body report Canada quotes plainly says that an assessment of evidence of actual effects is not required. Canada repeats the error later in its submission when it contends that "Australia is required to demonstrate to the Panel that the EWRP, in its actual effect, accords less favourable treatment to imported wine than to domestic like products." Such a demonstration simply is not required to demonstrate a breach of Article III:4.

10. A correct reading of Article III:4 of the GATT 1994, along with prior reports and logic, indicates that a nearly infinite variety of scenarios could result in unequal and less favorable treatment of imports. Accordingly, claims under Article III:4 must be examined case by case, taking into account all relevant facts and circumstances.

III. RELATIONSHIP BETWEEN THE FIRST SENTENCE OF ARTICLE III:2 OF THE GATT 1994 AND ARTICLE III:4 OF THE GATT 1994

11. Australia argues that the federal tax measure and the Nova Scotia reduced product mark-up measure are inconsistent with the first sentence of Article III:2 of the GATT 1994, and Australia further argues, in the alternative, that these measures are inconsistent with Article III:4 of the GATT 1994. Canada argues that "different aspects of the same 'measure' – which could also be characterized as distinct, though related measures, may be subject to Article III:2 or Article III:4, but the same aspect of that measure cannot be subject to both obligations at the same time. Fiscal measures are subject to Article III:2…. regulatory measures are subject to Article III:4." Canada misconstrues the relationship between the first sentence of Article III:2 of the GATT 1994 and Article III:4 of the GATT 1994.

12. The first sentence of Article III:2 of the GATT 1994 refers to "internal taxes or other internal charges of any kind." Whether a challenged measure constitutes an internal tax or other internal charge of any kind is a question that a panel must resolve based on the facts, taking into account the nature and the characteristics of the challenged measure. The characterization of the measure by the complainant does not dictate the status of the measure.

13. Article III:4 of the GATT 1994 applies "in respect of all laws, regulations and requirements affecting [the] internal sale, offering for sale, purchase, transportation, distribution or use" of like products. As with the first sentence of Article III:2 of the GATT 1994, to ascertain whether a challenged measure constitutes a law, regulation, or requirement affecting the internal sale, offering for sale, purchase, transportation, distribution or use of like products, a panel should make an objective assessment taking into account all relevant facts and characteristics of the challenged measure. Again, the characterization of the measure by the complainant – or the responding Member – does not dictate the status of the measure.

14. Nothing in the terms of the first sentence of Article III:2 of the GATT 1994 or Article III:4 of the GATT 1994 expressly provides that a particular measure – or a particular aspect of a particular measure – cannot be subject to the requirements of both provisions simultaneously. Given the broad coverage of Article III:4 of the GATT 1994, a measure imposing an internal tax

or charge, which unquestionably is subject to Article III:2 of the GATT 1994, might also be subject to Article III:4 of the GATT 1994.

15. On the other hand, a measure that is subject to Article III:4 of the GATT 1994 because it is a law, regulation, or requirement affecting the internal sale, offering for sale, purchase, transportation, distribution or use of like products might not necessarily also be subject to Article III:2 of the GATT 1994 because it might not also be an internal tax or charge. But that is because the scope of coverage of Article III:4 of the GATT 1994 is broader than the scope of coverage of Article III:2 of the GATT 1994, and the outcome of the analysis would depend on the facts and characteristics of the challenged measure, rather than as the result of any strict distinction established by the terms of the first sentence of Article III:2 and Article III:4. No such strict distinction is present in the text of those provisions.

EXECUTIVE SUMMARY OF THE U.S. THIRD PARTY ORAL STATEMENT

I. THE PROPER INTERPRETATION OF THE FIRST SENTENCE OF ARTICLE III:2 OF THE GATT 1994

16. In its first written submission, Canada argued at length that Article III:2 "requires consideration of a measure's economic impact on competitive opportunities." Canada reiterated in its opening statement during this meeting that "preserving the link between Article III:1 and Article III:2, first sentence requires, at a minimum, that a responding party be given the opportunity to rebut the presumption that taxing an imported product in excess of the like domestic product in fact results in protection being afforded to domestic production." Canada is incorrect.

17. Canada calls into question the Appellate Body's findings in *Japan – Alcoholic Beverages II*, contending that "the conclusion drawn by the Appellate Body is not persuasive, and merits reconsideration". Canada has every right to make such an argument. The DSU does not assign precedential value to panel or Appellate Body reports adopted by the DSB, or interpretations contained in those reports, in the sense of an interpretation that must be followed in a subsequent dispute.

18. Instead, the DSU and the WTO Agreement reserve such weight to authoritative interpretations adopted by WTO Members in a different body – the Ministerial Conference or General Council – acting not by negative consensus but under different procedures. The DSU explicitly provides in Article 3.9 that the dispute settlement system operates without prejudice to this interpretative authority. The DSU states that it exists to resolve disputes arising under the covered agreements – not disputes concerning panel or Appellate Body interpretations of those agreements. The DSU also provides that a panel or the Appellate Body is to apply customary rules of interpretation of public international law in assisting the DSB to determine whether a measure is inconsistent with a Member's commitments under the covered agreements. Those customary rules of interpretation likewise do not assign a precedential value to interpretations given as part of dispute settlement for purposes of discerning the meaning of agreement text.

19. Canada suggests that, "[w]here Canada parts ways with the Appellate Body, it does so for cogent reasons." Canada goes on to provide its reasons, which, ultimately, amount to Canada

disagreeing with the Appellate Body's interpretation. The United States welcomes Canada's acknowledgement that disagreement, on the basis of a different interpretation resulting from application of customary rules of interpretation to the text of the WTO agreements, is a valid reason to reach an interpretive conclusion that differs from that reached in an earlier Appellate Body report.

20. One would expect that Canada would take the position it is espousing in this dispute consistently in all disputes and in the context of all discussions concerning the DSU. The United States is quite concerned, however, that Canada has very recently expressed the opposite view in another ongoing dispute, even going so far as to argue that a panel acted inconsistently with Article 11 of the DSU by disagreeing with prior Appellate Body findings because the panel considered those findings to be incorrect. It is troubling that a Member would simultaneously take such inconsistent and self-serving positions in different disputes, particularly without disclosing to the adjudicators that it is doing so. This can only serve to undermine the credibility of the WTO dispute settlement system.

II. THE INTERPRETATION AND APPLICATION OF ARTICLE III:4 OF THE GATT 1994

21. In its opening statement, Canada indicated that it "agrees" that "it is not necessary, as a matter of making out a *prima facie* case, for the complaining party to show actual trade effects." Canada contends, though, that this "does not mean that actual effects, or the absence thereof, are irrelevant considerations." Canada suggests that "evidence of actual effects may be taken into account as part of the overall analysis", and the "analysis under Article III:4 goes beyond looking at the design, structure and expected operation of the measure, and should include consideration of market conditions and other extrinsic circumstances."

22. But Canada's proposed approach raises questions like: how are data on trade flows to be taken into account as purported "evidence of actual effects"? and what are the implications of any changes – or the absence of any changes – in trade flows? As Australia astutely observed in its opening statement, "if imports have increased in a market, this does not preclude a finding that the conditions of competition have been affected because imports could have increased more absent the measure."

23. Canada's approach would appear to necessitate a kind of rather complicated counterfactual analysis, in which one would assess what the trade flows would have been but for the challenged measure. Under such an analysis, if it were even possible to do, one might conclude that the trade flows would have been X <u>for reasons</u>. That "<u>for reasons</u>" part is actually the critical part of the analysis in terms of understanding whether the measure changed the conditions of competition – and perhaps whether the measure did or did not have (*i.e.*, cause) actual effects. But, if one knows the reasons, one does not need to actually look at the trade flows, and if one has data on trade flows but does not know the reasons, then one cannot make any conclusions about any so-called "actual effects" of the measure. In that case, application of logic and reason when scrutinizing the structure, design, and expected operation of the measure, while, of course, taking into account all other information and evidence, including trade data, is what is needed to reach a conclusion about whether a measure has changed the conditions of competition to the detriment of imports.

III. OBSERVATIONS REGARDING ARTICLE XVII OF THE GATT 1994

24. Finally, the United States recalls that Australia has made claims under Article III of the GATT 1994 concerning the Emerging Wine Regions Policy ("EWRP") promulgated and put into effect by the Nova Scotia Liquor Corporation ("NSLC"). Canada has invoked Article XVII of the GATT 1994 and contends that Australia's claim against the EWRP must be made under Article XVII because the NSLC is a state trading enterprise ("STE") and "retail mark-ups [are] a commercial practice of an STE related to buying and selling wine rather than a governmental measure." Article XVII, though, does not refer so broadly to actions "related to buying and selling". Rather, Article XVII more narrowly prescribes that an STE "shall, in its purchases or sales involving either imports or exports, act in a manner consistent with the general principles of non-discriminatory treatment prescribed in this Agreement for governmental measures affecting imports or exports by private traders", and, further, STEs "shall, having due regard to the other provisions of this Agreement, make any such purchases or sales solely in accordance with commercial considerations…." The reference to "import mark-up[s]" in Article XVII:4(b) likewise is rather narrow and relates to an obligation to provide information about such mark-ups.

25. Furthermore, Canada has agreed that STEs may be subject to Article III of the GATT 1994, or to any other disciplines of the GATT 1994 or other covered agreements. This may be the case when an STE is doing something other than engaging in "its purchases or sales involving either imports or exports", and Canada suggests that it will be the case "when an STE acts to perform a government function, or exercise governmental authority".

26. Canada proposes a test under which "when an STE acts in fulfilment of a private market commercial function, such as marking up a product on resale, sufficient to cover acquisition costs, selling, general and administrative costs, and an amount for profit, those actions are subject only to Article XVII of the GATT 1994." It is not clear, though, that the EWRP even passes Canada's own test. First, the NSLC evidently is not merely a liquor store. Australia has put before the panel evidence that the NSLC is the provincial regulator of beverage alcohol. The NSLC has a legal mandate to make and implement governmental policy, including a policy of supporting local producers. So, rather than just being a liquor store, the NSLC is a kind of chimera that serves different purposes at different times. Second, in promulgating the EWRP, the NSLC did something aside from, or more than, or perhaps even disconnected from simply "marking up a product on resale, sufficient to cover [costs and profit]". A stated purpose of the policy is to support Nova Scotia wine producers. The Panel should take that into account. The Panel may also want to inquire why the sufficiency of a mark-up for covering costs and profit would vary depending on whether or not the wine comes from an emerging wine region. The reason is not immediately clear.

27. Finally, Canada's suggestion that such actions "are subject only to Article XVII of the GATT 1994" raises some concern. Canada points to nothing in the text of Articles III or XVII that would necessitate such a compartmentalization of measures and claims. Given the link in Article XVII to the principles of Article III, Article XVII reads more like an additional attempt by Members to capture certain specified activity that might not ordinarily be captured already by Article III, rather than broadly removing activity from coverage under Article III.