

PHILIPPINES – TAXES ON DISTILLED SPIRITS

(AB-2011-6 /DS403)

APPELLEE SUBMISSION OF THE UNITED STATES OF AMERICA

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Short Form	Full Citation
<i>Australia – Apples (AB)</i>	Appellate Body Report, <i>Australia – Measures Affecting the Importation of Apples from New Zealand</i> , WT/DS367/AB/R, adopted 17 December 2010
<i>Canada – Periodicals (AB)</i>	Appellate Body Report, <i>Canada – Certain Measures Concerning Periodicals</i> , WT/DS31/AB/R, adopted 30 July 1997
<i>Canada/U.S. – Continued Suspension (AB)</i>	Appellate Body Report, <i>Canada – Continued Suspension of Obligations in the EC – Hormones Dispute; United States – Continued Suspensions in the EC – Hormones Dispute</i> WT/DS321/AB/R, WT/DS320/AB/R, adopted 14 November 2008
<i>Chile – Alcohol (Panel)</i>	Panel Report, <i>Chile – Taxes on Alcoholic Beverages</i> , WT/DS87/R, WT/DS110/R, adopted 12 January 2000, as modified by the Appellate Body Report, WT/DS87/AB/R, WT/DS110/AB/R
<i>Chile – Alcoholic Beverages (AB)</i>	Appellate Body Report, <i>Chile – Taxes on Alcoholic Beverages</i> , WT/DS87/AB/R, WT/DS110/AB/R, adopted 12 January 2000
<i>EC – Asbestos (Panel)</i>	Panel Report, <i>European Communities – Measures Affecting Asbestos and Products Containing Asbestos</i> , WT/DS135/R, adopted 5 April 2001, as modified by the Appellate Body Report, WT/DS135/AB/R
<i>EC – Asbestos (AB)</i>	Appellate Body Report, <i>European Communities – Measures Affecting Asbestos and Products Containing Asbestos</i> , WT/DS135/AB/R, adopted 5 April 2001
<i>EC – Poultry (AB)</i>	Appellate Body Report, <i>European Communities – Measures Affecting the Importation of Certain Poultry Products</i> , WT/DS69/AB/R, adopted 23 July 1998
<i>Japan – Alcoholic Beverages I</i>	GATT Panel Report, <i>Japan – Customs Duties, Taxes and Labelling Practices on Imported Wines and Alcoholic Beverages</i> , L/6216, adopted 10 November 1987, BISD 34S/83
<i>Japan – Alcoholic Beverages II (Panel)</i>	Panel Report, <i>Japan – Taxes on Alcoholic Beverages</i> , WT/DS8/R, WT/DS10/R, WT/DS11/R, adopted 1 November, 1996, as modified by the Appellate Body Report, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R

<i>Japan – Alcoholic Beverages II (AB)</i>	Appellate Body Report, <i>Japan – Taxes on Alcoholic Beverages</i> , WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November, 1996
<i>Korea – Alcohol (Panel)</i>	Panel Report, <i>Korea – Taxes on Alcoholic Beverages</i> , WT/DS75/R, WT/DS84/R, adopted 17 February 1999, as modified by the Appellate Body Report, WT/DS75/AB/R, WT/DS84/AB/R
<i>Korea – Alcoholic Beverages (AB)</i>	Appellate Body Report, <i>Korea – Taxes on Alcoholic Beverages</i> , WT/DS75/AB/R, WT/DS84/AB/R, adopted 17 February 1999
<i>Mexico – Taxes on Soft Drinks (Panel)</i>	Panel Report, <i>Mexico – Tax Measures on Soft Drinks and Other Beverages</i> , WT/DS308/R, adopted 24 March 2006, as modified by the Appellate Body Report, WT/DS308/AB/R
<i>US – Cotton Yarn (AB)</i>	Appellate Body Report, <i>United States – Transitional Safeguard Measure on Combed Cotton Yarn from Pakistan</i> , WT/DS192/AB/R, adopted 5 November 2001
<i>US – Wool Shirts (AB)</i>	Appellate Body Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/AB/R and Corr.1, adopted 23 May 1997

I. Introduction

1. As it has since the beginning of this dispute, in this appeal, the Philippines attempts to recast the measures at issue as something they are not. In the service of this effort, the Philippines refers to larger fiscal policy objectives and a commitment to progressive taxation, asserting that this dispute raises systemic issues regarding the autonomy of WTO Members.¹ It does not. The United States has taken no position on the fiscal priorities that the Philippine government should have, nor on how it should achieve them. The sole issue in this dispute is whether the Philippines' excise tax system for distilled spirits discriminates against imported products in breach of Article III:2 of the *General Agreement on Tariffs and Trade 1994* ("GATT 1994").

2. Contrary to the Philippines' assertions, the Panel's analysis faithfully adhered to the requirements of GATT Article III:2, first and second sentences, is consistent with the reasoning of earlier panels and the Appellate Body considering similar claims on the same types of products, and was based on an objective assessment of the evidence before it.

3. As we will discuss throughout this submission, the Philippines' presentation of its measures and the issues before the Division is distorted, and leaves out critical facts. In its submission, the Philippines implies that because its tax measures are based on raw material, they are origin neutral.² To the contrary, the specific contours of the distinction ensure that the lowest tax rate is applied to all distilled spirits produced in the Philippines.³ While the Philippines' appellant submission correctly recites the tax rates for spirits that are not made from favored raw materials – from 126 to 504 pesos per proof liter, depending on the price of the spirit – it fails to

¹ Philippines Appellant Submission, para. 2.

² Philippines Appellant Submission, para. 8.

³ Panel Report, para. 2.17.

note the tax rate for the spirits made from typical local raw materials – 11.65 pesos per proof liter, regardless of the price of the spirit.⁴

4. Moreover, the Philippines’ distinction between the “sugar-based”⁵ category of spirits and other spirits provides no practical information about the products for sale in the Philippines. As any layperson can tell, the products at issue are all the familiar types of distilled spirits – whiskey, brandy, gin, vodka, tequila, and rum.⁶ The difference is that the Philippine domestic producers make all of these products from typical local materials and enjoy low taxes, whereas imported products produced from other raw materials face vastly higher taxes.

5. The Philippines also omits from its presentation a great deal of the evidence on which the Panel relied for its findings, including product labels, end uses, marketing, and color.⁷ Indeed, its arguments focus almost entirely on the narrow set of evidence related to physical characteristics that it believes supports its claims, such as congeners in distilled spirits products. In each instance that the Panel declined to interpret a particular fact in the same way as the Philippines, or weigh the evidence in the manner preferred by the Philippines, the Philippines asks the Appellate Body to reverse the Panel’s specific factual findings. Based on these arguments, the Philippines seeks a reversal of the conclusion that the Philippine measures are inconsistent with both the first and second sentences of Article III:2 of the GATT 1994.

⁴ In 2011, all rates were updated. The rate for products made of designated raw materials is now 14.68 pesos/proof liter, and the rates for other spirits are now 158.73, 317.44, or 634.90 pesos/proof liter, depending on price. Panel Report, paras. 2.3-2.4.

⁵ See, e.g., Philippines Appellant Submission, para. 5.

⁶ See, e.g., Exhibits US-22, 34, and 38 and U.S. First Written Submission, para. 46.

⁷ See, e.g., Panel Report, para. 2.25, 2.39, and 2.42; Exhibits US-22, 38, 41.

6. With respect to the Panel’s analysis under Article III:2 of the GATT 1994, the Philippines asks the Appellate Body to reverse the finding that imported and domestic distilled spirits are “like” with respect to the first sentence of Article III:2, and “directly competitive or substitutable” with respect to the second sentence of Article III:2. In addition, the Philippines asks the Panel to reverse the Panel’s finding that the Philippines’ measures are applied “so as to protect domestic production.”

7. The Philippines also makes several claims under Article 11 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (“DSU”), arguing that the Panel failed to make the “objective assessment of the matter before it” which the DSU requires. The specific subjects on which the Philippines challenges the objectivity of the Panel overlap with its other claims. The Philippine claims under Article 11 concern the Panel’s treatment of expert evidence on the physical characteristics of the products at issue; evidence on tariff classification; the studies on substitution presented by the parties; and evidence on the characteristics of the Philippine market (market segmentation, potential competition).

8. The Philippines does not challenge several other findings of the Panel, including the similarity in the end uses of Philippine and imported spirits,⁸ nor the Panel’s finding that the names and designs of Philippine distilled spirits generally “mimic or replicate the names of products and designs of the similar imported spirits made from other raw materials.”⁹ In addition, the Philippines does not challenge the Panel’s findings that under the Philippine

⁸ See Panel Report, para. 7.48.

⁹ Panel Report, para. 7.61.

measures, imported products are taxed “in excess of” domestic products¹⁰ and that imported and domestic products are “not similarly taxed.”¹¹

9. The Philippines’ claims each center on one of two subjects: physical characteristics and extent or likelihood of competition under current market conditions.

10. Regarding physical characteristics, the Philippines advances the idea that if there are any differences between Philippine domestic products and imported products, the two groups cannot be “like products.” This is at odds with the approach adopted by the Appellate Body. “Like products” do not need to be “identical.”¹² For example, in *Japan – Alcoholic Beverages*, distilled spirits were found to be “like” (vodka and shochu) despite differences in physical characteristics.¹³

11. Regarding competition under current market conditions, the Philippines argues that because most Filipino consumers have relatively low incomes, and most imported spirits are relatively more expensive, competition cannot occur between imported and domestic products in the Philippine market. It states, if consumers do not have “the means to make an effective choice between the products . . . then . . . the products must necessarily fall outside the narrow range of products that may be considered under Article III:2, particularly its first sentence.”¹⁴ Under this rationale, infrequent or special occasion purchases are not sufficient to show that

¹⁰ Panel Report, paras. 7.86 and 7.88.

¹¹ Panel Report, para. 7.167. The Philippines states that although it disagrees with this finding, it is not making any claim of legal error. See Philippines Appellant Submission, fn 88.

¹² Panel Report, para. 7.32.

¹³ *Japan – Alcoholic Beverages II (Panel)*, para. 6.23.

¹⁴ Philippines Appellant Submission, para. 62.

products are “like” or “directly competitive or substitutable,” and for potential purchases to be relevant, there must be some evidence of the frequency with which these purchases will occur.¹⁵

12. This, too, is at odds with the correct approach to this dispute. First, the record shows that, although imported products tend to be more expensive, “there are a number of high-priced domestic spirits, as well as less expensive imports.”¹⁶ Second, evidence of a competitive relationship – even a “direct” competitive relationship – is not limited to evidence of existing or likely purchases of products. Indeed, evidence on the products themselves are at the center of the inquiry. As the Appellate Body in *Korea – Alcoholic Beverages* stated, citing the Panel Report in that dispute:

The determination of whether domestic and imported products are directly competitive or substitutable “requires evidence of the direct competitive relationship between the products, including, in this case, comparisons of their physical characteristics, end-uses, channels of distribution and prices.” The Panel reasoned, furthermore, that the “focus should not be exclusively on the quantitative extent of the competitive overlap, but on the methodological basis on which a panel should assess the competitive relationship.”¹⁷

13. In sections II and III, the United States will address the Philippines’ specific claims regarding the Panel’s findings under the first and second sentences of Article III:2 of the GATT 1994. The claims are closely linked and the Panel properly relied on the same set of evidence for both.¹⁸ In its application of the legal standard to the facts before it, the Panel did not err.

¹⁵ See, e.g., Philippines Appellant Submission, paras. 70, 102, 115.

¹⁶ Panel Report, paras. 2.36, 7.51.

¹⁷ *Korea – Alcoholic Beverages (AB)*, para. 109, citing *Korea – Alcoholic Beverages (Panel)*, paras. 10.43 and 10.39.

¹⁸ Panel Report, para. 7.98, citing *Korea – Alcoholic Beverages (AB)*, para. 118.

14. In sections IV, the United States will address the Philippines' claims that the Panel failed to objectively assess the evidence. As noted above, these claims largely cover the same factual ground as the Philippines' other claims and likewise fail.

II. The Panel Correctly Interpreted Article III:2, First Sentence

15. All Parties to this dispute agree that there are two elements necessary to find a measure is inconsistent with the first sentence of Article III:2 of the GATT 1994. First, the domestic and imported products at issue must be "like products." Second, the measure must tax imported products in excess of like domestic products.

16. The Philippines has not contested the Panel's conclusion that the Philippines' measures tax imported products in excess of domestic products.¹⁹ Thus, the only issue before the Division relating to the first sentence of Article III:2 of the GATT 1994 is whether the Panel's conclusion that the imported and domestic products at issue are "like products" should be upheld.

17. Past panels and the Appellate Body have developed a consistent approach to determining whether products are "like products" for purposes of Article III:2. As the Panel correctly stated at paragraph 7.31 of its report, the determination must be made on a case-by-case basis, by examining the relevant factors.²⁰

18. The Panel introduced its analysis for purposes of this dispute as follows:

In order to address the likeness requirement of the first sentence of Article III:2, we will consider the evidence presented by the parties regarding the products' properties, nature and quality; their end uses, with reference to the Philippine market; Philippines consumers' tastes and habits; the tariff classification of the products based on the Harmonized System; and other relevant internal regulations

¹⁹ Panel Report, para. 7.86.

²⁰ See, e.g., *Japan – Alcoholic Beverages II (Panel)*, para. 6.21 and *Mexico – Taxes on Soft Drinks (Panel)*, para. 8.28.

in the Philippines. We will construe the likeness test in a narrow manner in accordance with previous interpretations of the first sentence of Article III:2 of the GATT 1994.²¹

19. The Panel analyzed evidence under each of these factors, before drawing its general conclusions. The Panel’s analysis addressed specific evidence under each of these criteria, such as:

a) *Products’ properties, nature and quality*: Product color, alcohol content, and taste²²

b) *End uses*: Purpose (*e.g.*, socializing) and method (*e.g.*, in cocktails or straight)²³

c) *Consumers’ tastes and habits*: Marketing campaigns, product labels, sales outlets, and studies on substitutability²⁴

d) *Tariff classification*: 6-digit and 4-digit classification information²⁵

e) *Internal regulations*: Philippine sales ordinances and regulations on spirits²⁶

20. The Panel did not find one factor or piece of evidence to be dispositive as to whether products are “like” or not “like.” As the Panel stated, citing *EC – Asbestos*, “[t]he Appellate Body has noted that a panel should examine the evidence relating to each of these four criteria and, then, weigh all of that evidence, along with any other relevant evidence, in making an overall determination of whether the products at issue may be characterized as ‘like.’”²⁷

²¹ Panel Report, para. 7.33.

²² *See, e.g.*, paras. 7.35, 7.88, and 7.42-7.47.

²³ *See, e.g.*, para. 7.48.

²⁴ *See, e.g.*, paras. 7.51 and 7.61.

²⁵ *See, e.g.*, paras 7.63 and 7.65-7.70.

²⁶ *See, e.g.*, paras. 7.72-7.73.

²⁷ Panel Report, para. 7.31, citing *EC – Asbestos (AB)*, para. 109.

21. The Panel followed this approach, summarizing its conclusions on the specific criteria before reaching its general conclusions that Philippine and imported spirits are “like.”²⁸

22. The Philippines largely ignores the overall analysis of the Panel and focuses entirely on two discrete issues: the physical differences between imported and domestic products, and the alleged inability of many Philippine consumers to purchase imported products on a weekly basis. With respect to the first issue, the Philippines refers to evidence of some physical differences between imported and domestic products, the Panel’s use of evidence on tariff classification and U.S. and European Union internal labeling regulations. For the latter, the Philippines challenges the Panel’s use of evidence of competition as it pertains to consumers’ tastes and habits in the Philippine market.

23. Indeed, the Philippines characterizes the “like product” analysis as essentially pertaining to only two factors (physical characteristics and market relationship),²⁹ omitting other factors that the Appellate Body has routinely noted are relevant, and which the Panel reviewed in this dispute.

A. The Panel Correctly Considered and Addressed Evidence Related to the Physical Characteristics of Distilled Spirits in the Philippine Market

1. Differences in Chemical Composition Do Not Prevent Philippine Domestic Spirits from Being “Like” Imported Spirits

24. The Philippines argues that any “significant” physical differences between Philippine domestic products and imported products, even those that may not be perceptible to the consumer, should be sufficient to disqualify products from being considered physically “like.”³⁰

²⁸ Panel Report, para. 7.75-7.77, 7.80-7.85.

²⁹ Philippines Appellant Submission, para. 22.

³⁰ Philippines Appellant Submission, para. 30.

The specific physical differences it points to are the differences in chemical compounds, or congeners, that linger in spirits as a result of the raw material used, and the differences resulting from the use of additives and flavorings in spirits to mimic those congeners where they do not otherwise occur.³¹

25. The Philippines’ arguments regarding the physical characteristics of imported and domestic spirits suffer from two fundamental errors. In each case, the Philippines is essentially reading the term “like” to mean “identical,” but that is not what the agreed text of Article III:2 says. First, the Philippines overstates the importance of physical characteristics in the determination of whether products are “like.” Second, it overstates the importance of certain physical differences and ignores key physical characteristics that consumers actually rely on in choosing brands of spirits.

26. The United States agrees that physical characteristics are important criteria for determining whether products are “like.”³² But physical characteristics are still just part of the list of factors – they are not the whole list nor necessarily dispositive.

27. In examining the physical characteristics of the products at issue, it is important to take into account the specific facts in this case regarding the products at issue. Unlike in *Japan – Alcoholic Beverages II*, *Korea – Alcoholic Beverages*, and *Chile – Alcoholic Beverages*, the Philippines measures do not protect only one type of domestic spirit, such as soju or pisco. Instead, Philippine manufacturers produce brandies, whiskies, gins, and other products that compete with imported products of the same type.³³ Some physical characteristics, such as

³¹ Philippines Appellant Submission, para. 34.

³² U.S. First Written Submission, para. 91.

³³ See, e.g., Exhibit US-38.

physiological effects, are similar across all types of products. For other characteristics, both the imported products and the domestic Philippine products vary from type to type. Thus, while both domestic and imported distilled spirits in the Philippines “range from clear (transparent) to golden or mahogany”³⁴ in color, it is also true to say that regardless of the raw material from which the products are made both Philippine and imported gins are clear and taste of juniper, and both Philippine and imported whiskies are more golden in color.³⁵

28. As the Panel found, Philippine producers take great pains to make their gins, brandies and other products similar to imported products of the same type, so much so that they are virtually indistinguishable on the shelf for a consumer.³⁶ In this context, the Panel was correct to focus on the characteristics of the final products sold to consumers, and less on the raw materials used. This is similar to the approach taken by the panel in *Mexico – Taxes on Soft Drinks*, where the discrimination among products was achieved through different treatment of products sweetened with cane sugar versus other sweeteners.³⁷ As the Panel stated: “Alternative processes involve the use of non-traditional raw materials in creating final products that closely mimic traditional products. In these circumstances a panel should focus its ‘likeness’ analysis on the physical qualities and characteristics of the final product, and not on the different raw materials used.”³⁸

29. The Philippines suggests that any differences between domestic and imported products should “disqualify” the two groups from being “like products,” arguing that the subtle differences

³⁴ Panel Report, para. 7.35.

³⁵ See, e.g., Exhibit US-38.

³⁶ Panel Report, para. 2.25. See also Exhibits US-30 and 42.

³⁷ *Mexico – Taxes on Soft Drinks (Panel)*, paras. 8.30-8.31 and 8.131.

³⁸ Panel Report, para 7.37.

in imported and domestic spirits prevent them from being “like.”³⁹ It states: “the simple fact that sugar-based spirits in the Philippines are physically different from their non-sugar-based counterparts should have been viewed by the Panel as disqualifying these products from being considered physically ‘like’” and that “the relevant standard is whether the products objectively differ in their physical properties.”⁴⁰ The Philippines entirely ignores relevant evidence, cited by the Panel, such as marketing and end uses, that supports the Panel’s finding of likeness.⁴¹

30. The Philippines’ presentation on physical characteristics centers entirely on the physical characteristics that directly result from the use of different raw materials, particularly congeners present in the chemical composition of the product and the inverse, flavors added because the base raw material does not have the congeners or flavor profile that the producer desires. As the Panel noted, these additives are used to ensure that the domestic Philippine product has the color, odor, and taste of the imported products of the same types.⁴² In the Philippines, producers strip alcohol “of its congeners to produce a neutral spirit. Special additives are then incorporated into the cane sugar-based spirit in order to ensure, as much as possible, that it has the colour, odour and taste traditionally associated with brandy, whisky or tequila.”⁴³ The resulting products have different organoleptic properties from type to type, but there is no evidence that these differences indicated two separate and identifiable groups between Philippine brandies, gins, etc., and their imported counterparts.⁴⁴

³⁹ Philippines Appellant Submission, para. 39.

⁴⁰ Philippines Appellant Submission, paras. 39, 42.

⁴¹ Panel Report, paras. 7.48, 7.51. Exhibits US-38, 41, 41, 34, 30, 42.

⁴² Panel Report, paras. 2.25, 7.38.

⁴³ Panel Report, para. 2.25.

⁴⁴ Panel Report, para. 7.40.

31. The Philippines’ emphasis on distinctions in additives and congeners is unduly narrow for a proper assessment of physical characteristics. In fact, this emphasis is at odds with the admonition in its first written submission that the criteria for “likeness” should not be applied mechanistically.⁴⁵

32. All parties, including the Philippines, concur that “like product” must be determined on a case by case basis. In *Japan – Alcoholic Beverages II* the Appellate Body stated that “there can be no one precise and absolute definition of what is ‘like.’”⁴⁶ As the Panel correctly noted (and contrary to what the Philippines appears to be arguing here), “like products” do not need to be “identical.”⁴⁷ For example, in *Japan – Alcoholic Beverages II*, the spirits which were found to be “like” (vodka and shochu) were physically different – the panel stated that the two types of products “shared *most* physical characteristics.”⁴⁸ They were not necessarily made with the same raw materials, and the panel also noted possible differences in alcoholic strength.⁴⁹

33. Accordingly, in its evaluation of the “physical qualities and characteristics” of products, the Panel in this case correctly did not focus just on some physical characteristics, as the Philippines’ suggests. Citing *EC – Asbestos*, the Panel’s analysis of the products addressed their “properties, nature, and quality,”⁵⁰ and “colour, flavor and aroma”.

34. The Panel methodically reviewed the evidence on physical characteristics, taking note of similarities in flavor characteristics (*e.g.*, the juniper berries of gin), color, and alcohol content

⁴⁵ Philippines First Written Submission, para. 83.

⁴⁶ *Japan – Alcoholic Beverages II (AB)*, p. 21.

⁴⁷ Panel Report, para. 7.32.

⁴⁸ *Japan – Alcoholic Beverages II (Panel)*, para. 6.23.

⁴⁹ *Japan – Alcoholic Beverages II (Panel)*, para. 6.23.

⁵⁰ Panel Report, para. 7.34.

for Philippine and imported distilled spirits⁵¹. In addition to the chemical studies that the Philippines relies on, the Panel reviewed pictures of Philippine and imported products, evidence on alcohol content, and marketing regarding the taste of the products.⁵² The Panel correctly examined the physical characteristics of the products at issue, both as a discrete criterion, and as one of the several factors for determining the “likeness” of imported and domestic products.

2. The Panel Did Not Err in its Findings on Regulations Outside the Philippines

35. In furtherance of its claims that the Panel failed to consider properly differences in the “physical characteristics” of imported and domestic products,⁵³ the Philippines challenges the Panel’s treatment of internal regulations from the European Union and the United States.⁵⁴ These regulations require that spirits labeled as whisky and brandy be produced from specific raw materials. The Philippines argues that the Panel erred by not considering these regulations as evidence that distilled spirits made from different raw materials are not “like products.”

36. The Philippines agrees that the “relevant market” for the determination of “likeness” is the Philippines – so it is curious that its claims of error focus on regulations for brandy and whiskey in complainants’ markets and ignores evidence on the record that included *Philippine* regulations on brandy, whiskey, vodka, and rum.

37. The Panel’s treatment of the internal regulations of the European Union and the United States was correct.

⁵¹ Panel Report, para. 7.35, 7.37-7.38, 7.42-7.47.

⁵² Panel Report, paras. 2.42, 7.35, 7.42-7.47. *See*, Exhibits US-22, 30, 34, 36, and 38 and U.S. First Written Submission, para. 51, Figure 3.

⁵³ Philippines Appellant Submission, para. 22 heading.

⁵⁴ Philippines Appellant Submission, para. 52.

38. The Panel did assess internal regulations. Correctly, it reviewed the Philippine counterparts to the U.S. and European Union regulations: the Standard Administrative Orders for rum, vodka, brandy, and whiskey.⁵⁵ These regulations permit the sale of products labelled as brandy, whiskey and vodka even if the specific brand is not made from what would generally be considered the traditional raw material for that type of spirit.⁵⁶ The Panel also took note of other internal regulations of distilled spirits that apply in the Philippines, noting that they did not distinguish among distilled spirits based on raw material.⁵⁷ Even the measures at issue define the category “distilled spirits” without regard to the raw material from which a particular spirit is produced.⁵⁸

B. The Panel Properly Analyzed Competition Among Imported and Domestic Products for the Purposes of Determining If They Are “Like Products”

39. The Philippines challenges several aspects of the Panel’s analysis of the criteria of “consumer tastes and habits” in the Philippine market. It asserts that the majority of Philippine consumers do not have the economic means to purchase imported spirits on a weekly basis and that purchases for “special occasions” are not sufficient evidence of competition. The Philippines also asserts that the Panel erred by applying its analysis of competition for the purposes of the second sentence of Article III:2 to the narrower analysis under the first sentence.

40. As a threshold matter, the Panel drew on a variety of evidence in its discussion of consumer tastes and habits, including (1) the fact that the same outlets in the Philippines that sell

⁵⁵ Exhibits US-22-25 and US-27.

⁵⁶ See Panel Report, paras. 2.56, 2.63, 2.70, 2.76, 2.82.

⁵⁷ Panel Report, para. 7.72.

⁵⁸ Panel Report, para. 7.72.

imported spirits also sell domestic spirits,⁵⁹ (2) the similarity in marketing campaigns for Philippine and imported distilled spirits,⁶⁰ and (3) the overlap in the range in price among imported spirits and among Philippine domestic spirits.⁶¹ To assess the Panel’s application of the legal standard, it is important to consider that it was not relying solely on the specific evidence regarding competition about which the Philippines raises concerns.

41. At the same time, the evidence referenced by the Philippines regarding the purchases and preferences does not indicate that Philippine distilled spirits are not “like” their imported counterparts. The Philippines incorrectly asserts that a certain quantity or volume of current competition or purchases is necessary before products may be considered “like.”

42. The Philippines attempts to use *Japan – Alcoholic Beverages* to insert a threshold for current competition into the test for “likeness.” It bases this on a citation from *Japan – Alcoholic Beverages II* that the “object and purpose”⁶² of Article III:2 of the GATT 1994 is “promoting non-discriminatory competition among imported and like domestic products.”⁶³

43. First, nothing in the statement of the Appellate Body in that dispute suggests that competition must be presently occurring in order for there to be a competitive relationship between two products. In fact, the Appellate Body in *Japan – Alcoholic Beverages II* confirmed

⁵⁹ Panel Report, paras. 2.36, 2.41, and 7.51.

⁶⁰ Panel Report, paras. 2.42 and 7.51.

⁶¹ Panel Report, paras. 7.51 and 7.59.

⁶² As an additional matter, the general rule of interpretation in Article 31 of the Vienna convention refers to interpreting the *treaty*, not an individual provision thereof, in light of the treaty’s object and purpose. Customary rules of interpretation do not provide for attributing an object and purpose to an individual provision – among other things, that would risk circular reasoning and also risk involving paraphrasing the provision and treating the paraphrase as though it were treaty text.

⁶³ Philippines’ Appellant Submission, para. 25.

that the “like product” examination will vary from case to case, and should not be interpreted so inflexibly. It stated that in applying the criteria for likeness “to the facts of any particular case, and in considering other criteria that may also be relevant in certain cases, panels can only apply their best judgment in determining whether in fact products are ‘like.’ . . . [i]t is a discretionary decision that must be made in considering the various characteristics of products in individual cases.”⁶⁴

44. If the Philippines’ argument were correct, imported products could never be “like” domestic products if a measure entirely excluded them from competition in a market. This would have the troubling effect of shielding the most successfully discriminatory measures from Article III:2.

45. The Philippines argues that if the majority of consumers lack the ability to buy a product on a weekly basis, the product cannot be considered in competition with the alternative product.⁶⁵ The very premise of its argument is false: it is based on the idea that the distinguishing feature of the domestic and imported products was their price. The Panel did not accept this false premise. Correctly, throughout the report, the Panel considered the two groups of spirits, imported and domestic, as they are defined by the Philippine measures themselves. According to the measures, there are two groups of spirits: (1) brandies, whiskies, gins, vodkas, tequilas and rums made from the typical local raw materials listed in the Philippines measures (which includes all Philippine brands of distilled spirits); and (2) other brandies, whiskies, gins, vodkas, tequilas and rums. The measures do not distinguish between product categories based on price.

⁶⁴ *Japan – Alcoholic Beverages II (AB)*, p. 20-21.

⁶⁵ *See, e.g.*, Philippines Appellant Submission, para. 62.

46. The Philippines also cites to language in *EC — Asbestos* indicating that “where the evidence relating to properties establishes that the products at issue are physically quite different . . . a higher burden is placed on complaining Members to establish that, despite the pronounced physical differences, there is a competitive relationship between the products, such that *all* of the evidence, taken together, demonstrates that the products are ‘like.’”⁶⁶ As an initial matter, the products at issue here are physically indistinguishable; they are neither “quite different” nor are their physical differences “pronounced.” As a result, the “higher burden” does not apply. In addition, the passage goes on to say that a “heavy burden” is placed on the complainant “to show, under the second and third criteria,” that the products are like.⁶⁷ The Appellate Body thus reiterated that a “competitive relationship” is demonstrated through analysis of end-uses and consumers’ tastes and habits. The Philippines’ effort to create additional criteria under the rubric of “competitive relationship” is therefore unavailing.

47. Finally, the Philippines incorrectly asserts that the Panel committed error because, in the Philippines’ view, a special occasion product cannot be in competition with a routinely purchased product.⁶⁸ The Philippines offers no support for this proposition. Indeed, as the Panel noted, at least one panel considering a similar issue concluded that spirits “are consumer goods which are purchased frequently, and even [a purchaser of lesser means] can afford to purchase a bottle of a more expensive beverage at least occasionally.”⁶⁹ Furthermore, in the case of the Philippines, the evidence did not support the conclusion that there were two separate market

⁶⁶ *EC — Asbestos (AB)*, para. 118.

⁶⁷ *Id.*

⁶⁸ Philippines Appellant Submission, para. 70.

⁶⁹ *Korea — Alcoholic Beverages (Panel)*, para. 10.74.

segments, with distinct consumption patterns. The Panel noted that “the population in the Philippines does not appear to be divided into two separate groups, but is rather distributed along a continuum of income brackets.”⁷⁰ (See Part IV.D for a discussion of the Philippines claim elsewhere in its submission that this factual finding was contrary to Article 11.)

48. The Philippines attempts to distinguish the panel’s analysis in *Korea – Alcohol*, protesting that the Philippine market is not the same as the Korean market, and that the Panel in that dispute was reviewing whether the imported and domestic products were “directly competitive or substitutable” and not whether they were “like.” Regarding the first point, as noted, the Panel in this case found evidence of a variety of income levels, not distinct market segments, much like the panel in *Korea-Alcohol*. Regarding the second, there is nothing to suggest that the panel’s reasoning hinged on the fact that it was proceeding under the “directly competitive or substitutable” provision. Even if “like product” is a relatively narrow category, affordability is not a prerequisite to concluding that consumers prefer one product over another.

C. The Panel Correctly Analyzed Tariff Classification

49. The Philippines asks the Appellate Body to reverse the Panel’s findings concerning tariff classification, arguing that the “range of products under the simple four digit heading is not sufficiently detailed for a panel to draw any particular inferences as to whether the products are “like.”⁷¹

50. The Panel noted that all distilled spirits are classified under HS 2208 and that is an “indication” of similarity.⁷² The Panel also examined the six digit level, noting that some

⁷⁰ Panel Report, para. 7.59.

⁷¹ Philippines Appellant Submission, para. 81.

⁷² Panel Report, para. 7.63.

Philippine products may be classified with imported products of the same type made from different raw materials, but others are not. Accordingly, the Panel found the evidence “inconclusive.”⁷³ The Philippines asks the Appellate Body to reject these modest findings.

51. The Appellate Body in *Japan – Alcoholic Beverages II* stated that tariff classification *can* be relevant in determining whether products are like and can be a “helpful sign” of similarity.⁷⁴ It does not oblige panels to draw conclusions based on tariff classification in all circumstances. Indeed, it is important to recognize that a primary reason that the classification of types of spirits at the six digit level was inconclusive for the Panel is because of the variance from subheading to subheading in the relevance of raw material.

52. The Panel correctly applied the standard for “likeness.” The Panel reviewed evidence on tariff classification, which past panels had indicated *could* indicate similarity. It found some indication of similarity, but overall inconclusive evidence on this specific point. This is an appropriate application of the standard to the specific facts of this dispute.

D. Conclusion on Article III:2, First Sentence

53. In summary, with respect to the Panel’s conclusion that imported and domestic distilled spirits are “like products” within the meaning of the first sentence of Article III:2 of the GATT 1994, the Philippines asks the Appellate Body to apply a rigid view of “like product,” such that almost any physical difference between competing products would mean they are not “like.” “Like products” do not need to be “identical”⁷⁵ – there must be some scope for difference

⁷³ Panel Report, para. 7.71.

⁷⁴ *Japan – Alcoholic Beverages II (AB)*, p. 21.

⁷⁵ Panel Report, para. 7.32. *See, e.g., Japan – Alcoholic Beverages II (Panel)*, para. 6.23.

between the imported product and the domestic product, or there would be no need for the inquiry at all. By following the approach of past panels, and reviewing the evidence under *all* criteria, not just the criteria highlighted by the Philippines, the Panel was able to assess whether the differences were significant enough that the Philippine brandies and gins are not “like” imported brandies and gins. Through this approach, the Panel reached the correct conclusion.

III. The Panel Did Not Err in Finding the Philippines’ Measures Inconsistent with the Second Sentence of Article III:2 of the GATT 1994

54. The parties agree on the three elements necessary to establish the claim that the Philippines’ measures are inconsistent with the second sentence of Article III:2 of the GATT 1994. The Panel recited the three elements, as established in prior disputes, as follows:

- 1) whether the imported and domestic products at issue are “directly competitive or substitutable” with respect to each other;
- 2) whether these directly competitive or substitutable products are “not similarly taxed”; and
- 3) whether the dissimilar taxation of these directly competitive or substitutable products is “applied . . . so as to afford protection to domestic production.”⁷⁶

55. The Philippines has not appealed the Panel’s findings that domestic and imported products are “not similarly taxed,”⁷⁷ but makes several claims with respect to the Panel’s findings that Philippine distilled spirits are “directly competitive or substitutable” with imported distilled spirits. It also challenges the Panel’s finding that the Philippines’ measures are applied so as to afford protection.

⁷⁶ Panel Report at 7.96, citing *Japan – Alcoholic Beverages II (AB)*, p. 116; *Korea – Alcoholic Beverages (AB)*, para. 107; *Chile – Alcoholic Beverages (AB)*, para. 47; *Canada – Periodicals (AB)*, p. 470.

⁷⁷ See Philippines Appellant Submission, fn 88.

A. The Panel Correctly Applied the Term “Directly Competitive or Substitutable”

56. Products are “directly competitive or substitutable” if they offer “alternative ways of satisfying a particular need or taste.”⁷⁸ As the Panel noted,

The term “directly competitive or substitutable” implies a relationship between the imported and domestic products at issue that can essentially be described as “in competition” in the marketplace. This is a “dynamic, evolving process”, which means that “the competitive relationship between products is *not* to be analyzed *exclusively* by reference to *current* consumer preferences.”⁷⁹

57. To determine whether products are “directly competitive or substitutable,” panels have reviewed a similar set of factors to those used to determine whether products are “like,” including consumer tastes and habits; product properties, nature, and quality; end uses, tariff classification; and internal regulations in the market in question.⁸⁰ The difference is simply that the scope of products that are “directly competitive or substitutable” is a broader group than “like products.”⁸¹

58. Similar to the way it examined each factor to determine whether Philippine distilled spirits are “like” imported spirits, the Panel examined each criterion by category, in some cases cross-referencing its treatment of the relevant evidence for the purposes of the first sentence of Article III:2.⁸² The Panel then drew its conclusion from the evidence as a whole, stating,

⁷⁸ *Korea – Alcoholic Beverages (AB)*, para. 114.

⁷⁹ Panel Report, para. 7.100, citing *Korea – Alcoholic Beverages (AB)*, para. 114.

⁸⁰ Panel Report, para. 7.102, citing *Japan – Alcoholic Beverages II (AB)*, *Korea – Alcoholic Beverages (Panel)*, and *Chile – Alcoholic Beverages (Panel)*.

⁸¹ Panel Report, paras. 7.98-7.99, citing *Korea – Alcoholic Beverages (AB)*, para. 118.

⁸² *See, e.g.*, Panel Report, para. 7.127.

“[h]aving considered all of the above factors and elements” the products at issue are “directly competitive or substitutable.”⁸³

59. It reviewed evidence under the following criteria:

*a) Products’ channels of distribution (e.g., sales of imported and domestic spirits in the same store in the Philippines)*⁸⁴

*b) Products’ properties, nature, and quality (e.g., color, organoleptic properties)*⁸⁵

*c) End uses and marketing (e.g., similar marketing strategies)*⁸⁶

*d) Tariff classification (e.g., same tariff classification at 4-digit level)*⁸⁷

*e) Internal regulations (e.g., lack of distinction in local ordinances between domestic and imported distilled spirits)*⁸⁸

60. In addition to these criteria, and notwithstanding that the Panel had already concluded that the domestic spirits at issue were “like” the imported spirits, the Panel also included a discussion of evidence on the competitive relationship between the products at issue.

61. The Philippines’ claims regarding to the Panel’s findings that the products at issue are “directly competitive or substitutable” all concern this section on the competitive relationship.

62. Significantly, the claims all follow from the Philippines’ recurrent theme that some significant quantum of current competition is necessary to support a finding under Article III:2 of the GATT 1994. As discussed below and in Section I.B, there is no such requirement, and each of the Philippines’ specific claims fail.

⁸³ Panel Report, para. 7.138.

⁸⁴ Panel Report, para. 7.123.

⁸⁵ Panel Report, para. 7.127.

⁸⁶ Panel Report, para. 7.129.

⁸⁷ Panel Report, para. 7.134.

⁸⁸ Panel Report, para. 7.135.

1. The Panel’s Examination of the Competitive Relationship Between Imported and Domestic Spirits in the Philippine Market Fully Addressed the “Degree” of Competition

63. The Philippines argues that the Panel erred by not considering the “degree” of competition between domestic and imported products.⁸⁹ In asking the Appellate Body to reverse the Panel’s findings in paragraphs 7.118-7.121 (and the related conclusions), the Philippines asserts that “[i]f the term ‘directly competitive or substitutable’ had been properly interpreted and applied, the findings regarding the very poor quality of the competition in the Philippine market would have [led] to the conclusion that there is insufficient proximity in the degree of competition between the products at issue to permit their characterization as ‘directly competitive or substitutable.’”⁹⁰

64. It makes this point, in part, by highlighting this statement by the Panel, relying on *Korea – Alcoholic Beverages*:

“The question before us under Article III of the GATT 1994 is not so much what the ‘degree of competition’ between the products at issue is, but what is the ‘nature’ or ‘quality’ of their ‘competitive relationship.’”⁹¹

65. Although the Philippines concurs that it is not appropriate to rely *solely* on quantitative information to assess the competitive relationship between products to determine whether they are “directly competitive or substitutable,” it minimizes the significance of other types of evidence.

66. To support its assertion that the quality of the competitive relationship between the products at issue in this dispute is not sufficient, it notes “a great disparity in the accessibility of

⁸⁹ Philippines Appellant Submission, para. 38.

⁹⁰ Philippines Appellant Submission, para. 95.

⁹¹ Panel Report, para. 7.101, citing *Korea – Alcoholic Beverages (AB)*, para. 114.

these products,” as well as perceptions of consumers and treatment by suppliers.⁹² But the Panel based its conclusions on evidence of similarities in each of these areas, including the fact that Philippine consumers may purchase imported spirits on special occasions,⁹³ notwithstanding the higher price; the lack of differentiation between imported and domestic products in labeling and marketing;⁹⁴ and the appearance of imported and domestic spirits side by side in the same stores.⁹⁵

67. In other words, the evidence before the Panel was sufficient to establish that there was a “degree of competition” and, specifically, that the relationship between imported and domestic products is “in competition” such that they offer “alternative ways of satisfying a particular need or taste.”⁹⁶

68. To support its argument that “degree of competition” requires something very narrow or specific, the Philippines cites to the Appellate Body’s statement in *U.S.– Cotton Yarn* that “[l]ike products are necessarily in the highest degree of competitive relationship in the marketplace.”⁹⁷ The Appellate Body made this observation in the context of examining whether products are “directly competitive” in the context of Article 6.2 of the *Agreement on Textiles and Clothing*, which authorized safeguard actions where imports of a product caused “serious damage, or actual threat thereof, to the domestic industry producing like and/or directly competitive products.” The

⁹² Philippines Appellant Submission, para. 94.

⁹³ Panel Report, 7.119. *See also* Exhibit US-41.

⁹⁴ Panel Report, 7.131. *See also*, Exhibit US-38.

⁹⁵ Panel Report, para. 7.123. *See also*, Exhibits US-30 and 42.

⁹⁶ Panel Report, para. 7.100.

⁹⁷ Philippines Appellant Submission, para. 26 and note 21 (citing *U.S. – Cotton Yarn (AB)*, para. 97).

descriptive phrase “highest degree” merely compared the term “like products” to the phrase before the Appellate Body, “directly competitive products;”⁹⁸ it does not shed light on the meaning of “like products” in the context of Article III:2.

69. Finally, the Philippines’ statement that “the Panel never made an inquiry as to the ‘degree of proximity’ of the competition between the products” does not accurately reflect the work of the Panel. For example, the Panel’s conclusion following its review of the studies presented by the parties states that, “the studies support the proposition that there is *a significant degree of competitiveness or substitutability* in the Philippines’ market between the distilled spirits at issue in the present dispute.”⁹⁹

70. In short, the Panel’s analysis of “competitive relationship” more than addressed any notion of “degree” of proximity required by the appropriate legal standard.

2. The Panel’s Examination of the Competitive Relationship Between Imported and Domestic Spirits in the Philippine Market Fully Addressed the “Directness” of Competition

71. After “degree” of competition, the Philippines raises a second claim regarding the Panel’s analysis of the competitive relationship between the products at issue with a claim concerning the “directness” of competition.

72. Specifically, the Philippines objects to the Panel’s finding that the fact that Filipinos who do not ordinarily purchase imported distilled spirits may nonetheless do so on special occasions.¹⁰⁰ The Philippines states that “direct competition” requires “close proximity,”

⁹⁸ See *U.S. – Cotton Yarn (AB)*, footnote 68 (citing *Korea – Alcoholic Beverages (AB)*, para. 118 (explaining that “[l]ike’ products are a subset of directly competitive or substitutable products”).

⁹⁹ Panel Report, para. 7.113 (emphasis added).

¹⁰⁰ Panel Report, para. 7.119.

including “frequency” of purchase.¹⁰¹ It further claims that consumers are likely to have different motivations for special occasion purchases.¹⁰²

73. It is not clear on what basis the Philippines makes these assertions. There is no “frequency” requirement for direct competition. Further, as the Panel noted, the reasons for consumption of distilled spirits, including relaxation and socializing, are similar for all distilled spirits.¹⁰³ In addition, even Philippine producers present their products as appropriate for special occasions:

As noted in the promotional materials prepared by manufacturers and distributors of both domestic and imported spirits sold in the Philippines, these products can be consumed on a number of occasions, such as parties, reunions, celebrations and romantic encounters.¹⁰⁴

74. There is no evidence that the “need or taste” that spirits satisfy on special occasions are different such that “special occasion” products do not directly compete with other products. The Philippines does not contest that when a consumer is making such a purchase, the consumer could compare a higher-quality domestic product, such as Ginebra San Miguel “Premium”¹⁰⁵ and an imported alternative. The tax rate at issue will affect the conditions of competition at that point. There is no evidence that there is a different market for “sugar based” versus other spirits on this basis.

¹⁰¹ Philippines Appellant Submission, para. 97.

¹⁰² Philippines Appellant Submission, para. 98.

¹⁰³ Panel Report, para. 7.128, 2.40.

¹⁰⁴ Panel Report, para. 2.40. *See also*, Panel Report, para. 7.59.

¹⁰⁵ *See*, Exhibit US-45, “From the makers of the finest liquors in the Philippines, revel in the taste of San Miguel Premium Gin.” *See also*, Exhibit US-55 (“Barcelona brandy is a toast to life”).

3. Competition within a Subset of the Market May Be Sufficient to Indicate that Products Are Directly Competitive or Substitutable

75. The Philippines’ next claim relates mainly to the Panel’s findings in paragraphs 7.118 and 7.120, where it cited the fact that at least a subset of the Philippine market (a “narrow segment” in the Philippines’ words) can currently purchase imported spirits as evidence of the competitive relationship between imported and domestic spirits.

76. According to the Philippines, in using evidence of competition within a subset of the Philippine market, the Panel erred. The Philippines argues that the Panel’s conclusions assume that just because consumers may be able to purchase, they will do so, and that the Panel is neglecting other evidence, such as the other reasons consumers may stay with a familiar brand¹⁰⁶ and the scale of the data on substitutability from the Euromonitor International survey.¹⁰⁷ It further states that the “degree” of competition demonstrated by such evidence is insufficient.

77. In this approach, the Philippines overstates the Panel’s conclusions. The Panel’s findings simply acknowledge that, notwithstanding the relatively low income of the average Philippine consumer, a subset of the market may purchase imported spirits currently even though they are generally more expensive. This fact supports the Panel’s general findings that there is a “competitive relationship” between imported and domestic spirits, as one criterion demonstrating the similarity of Philippine and imported spirits.

78. This is only logical – the existence of current competition certainly does not show *less* likelihood of a competitive relationship.

¹⁰⁶ Philippines Appellant Submission, para. 104.

¹⁰⁷ Philippines Appellant Submission, para. 105.

79. The Philippines’ specific concerns with these findings are simply quarrels with the Panel’s weighing of the evidence. The Panel’s analysis noted that there may be reasons such as brand loyalty why a consumer may not actually purchase a competitor product, even if he can afford to.¹⁰⁸ The Panel also included an extensive discussion of the results of the Euromonitor International survey, discussed in Section IV. The Philippines would have these findings outweigh the Panel’s finding of a competitive relationship in the Philippine market.

80. However, keeping in mind that the Panel’s task is to analyze and balance a number of criteria, there is no reason that a contrary – or potentially contrary – piece of evidence should mean that actual evidence of current competition does not support the Panel’s finding that there is a competitive relationship between imported and domestic spirits in the Philippine market.

81. As the Panel states at the end of the section regarding the competitive nature of the products at issue, “the instances of actual competition . . . are a clear indication that the imported and domestic products at issue in this dispute are indeed *capable* of being directly competitive or substitutable in the future.”¹⁰⁹

4. The Panel Correctly Determined that Potential Competition Exists in the Philippine Market

82. The Philippines next challenge concerns the basis for the Panel’s findings on potential competition. In particular, the Philippines asserts that the overlap in prices identified by the Panel is not sufficient to show “direct competition,”¹¹⁰ and also that the Panel did not have specific evidence to show that Philippine and imported products would be directly competitive in

¹⁰⁸ *Chile– Alcoholic Beverages (Panel)*, para 7.72, citing *Korea – Alcoholic Beverages (AB)*, para. 123. Panel Report, paras. 2.45 and 7.50.

¹⁰⁹ Panel Report, para. 7.121.

¹¹⁰ Philippines Appellant Submission, para. 109.

the near future.¹¹¹ The Philippines goes so far as to suggest that the Panel’s conclusions are “fantastical.”¹¹²

83. Such hyperbole is unwarranted. The Philippines’ arguments are based on the premise that “direct competition” requires some minimum threshold amount of actual competition among products in the relevant market, regardless of how similar or different the products are according to the other relevant criteria. As discussed above, “direct” competition has no such requirement.

84. There is no question that products may be “directly competitive or substitutable” even if the “direct competition” is only potential and is not occurring in the market currently or at a defined point in the future.

85. The underlying question concerns the products themselves and whether they “compete” in that they are similar enough to meet the legal standard of Article III:2. Thus, “the requisite relationship *may* exist between products that are not, at a given moment, considered by consumers to be substitutes but which are, nonetheless, *capable* of being substituted for one another.”¹¹³ Recognizing the potential for products to compete even if current market conditions preclude sales of some products is particularly important where the measures themselves, as here, “may have the effect of freezing consumer preferences” by imposing significant costs on the purchase of imported products.¹¹⁴ As the Appellate Body stated in *Korea – Alcoholic Beverages*,

¹¹¹ Philippines Appellant Submission, para. 114.

¹¹² Philippines Appellant Submission, para. 111.

¹¹³ Panel Report, para. 7.100.

¹¹⁴ Panel Report, para. 7.106, citing *Korea – Alcoholic Beverages (AB)*, paras. 119-120 and *Chile – Alcoholic Beverages (Panel)*, para. 7.25.

“Particularly in a market where there are regulatory barriers to trade or to competition, there may well be latent demand.”¹¹⁵

86. In addition, it should be noted that the overlap in prices between imported and domestic products that the Panel observed further undermines the Philippines’ assertions of market segmentation. The Panel noted the overlaps occurred for both low and high priced products, and were not simply exceptions to a general rule.¹¹⁶ Taken together with the fact that the Panel did not identify distinct income-based market segments among Philippine consumers, the price overlap demonstrates that Philippine consumers’ choices are not restricted into two distinct segments.

5. The Panel Correctly Did Not Require Competition in a “Representative” Group of the Market as a Condition for a Finding that the Products at Issue Are Directly Competitive or Substitutable

87. The Philippines’ final argument is that imported and domestic products cannot be “directly competitive or substitutable” if they do not compete throughout the entire Philippine market. The Philippines asserts that, “The assessment of whether sugar-based and non-sugar-based products are competitive in the Philippines must be done in relation to the market that is most representative of the market as a whole.”¹¹⁷ To support its position, the Philippines takes out of context the Panel’s statements that the model for a cross-price elasticity study should be based on a representative sample to be most reliable. The Panel’s remarks were limited to the specific type of cross-price elasticity study that would be best, which is a question of

¹¹⁵ *Korea – Alcoholic Beverages (AB)*, para. 116.

¹¹⁶ Panel Report, para. 7.118.

¹¹⁷ Philippines Appellant Submission, para. 117.

methodology. It was not an invitation to ignore actual competition in the market because it does not necessarily occur throughout the market.

88. The Panel expressly found that the Philippine market was not segmented¹¹⁸ and that many consumers could purchase spirits on special occasions.¹¹⁹ Nonetheless, the Panel correctly stated that, contrary to the Philippines assertion, “Article III of GATT 1994 does not protect just *some* instances or *most* instances, but rather, it protects *all* instances of direct competition.”¹²⁰

6. Conclusions Regarding the Panel’s “Directly Competitive or Substitutable” Findings under Article III:2, Second Sentence

89. In summary, the Philippines’ objections to the Panel’s analysis of the competitive relationship between imported and domestic products are premised on a misreading of the text of Article III:2 that would result in that Article protecting against discrimination in only limited situations.

90. The Philippines approach to “degree” and “directness” suggests that imported and domestic products must be in the same position in the marketplace. Its approach to “potential” competition inserts an additional requirement of showing “actual” competition right now. And its approach to “representativeness” requires competition right now across the market – and ignores competition that occurs or has the potential to occur in a subset of the market.

91. Put another way, a complainant could not successfully show that products are “directly competitive or substitutable” unless the imported products already were competing throughout

¹¹⁸ Panel Report, para. 7.118.

¹¹⁹ Panel Report, para. 7.119.

¹²⁰ Panel Report, para. 7.120.

the relevant market on an equal basis with domestic products. Such a condition would vitiate the protections in Article III:2.

B. The Panel Correctly Analyzed the Magnitude of the Discriminatory Taxation and the Design and Structure of the Philippines' Measures to Show They Afford Protection to Domestic Products

92. The final requirement to show that a measure is inconsistent with the second sentence of Article III:2 of the GATT 1994 is that the measure be applied so as to protect domestic production. As set out by the Appellate Body in *Japan – Alcoholic Beverages II*, whether a measure affords protection to domestic products may be ascertained by the design, architecture, and structure of the measure and by the magnitude of the differential in taxation between imported and local products.¹²¹

93. Past panels have focused on the magnitude of the difference in taxation between domestic and imported goods, and also the design, structure, and application of the measure at issue. The Panel's treatment of this issue followed this model, and was succinct and complete. While the Philippines criticizes the Panel's analysis as "limited", in fact the Panel provided a complete, to-the-point assessment of the issue. As the Panel explained, the design, architecture and structure of the measures are such that the raw materials designated in the measure, from which distilled spirits must be produced to enjoy favorable tax treatment, are all grown in the Philippines. And, conversely, "the vast majority of imported distilled spirits are *not* made from designated raw materials. This means that *de facto* the measure results in all domestic distilled spirits enjoying the favourable low tax, while the vast majority of the imported spirits are subject to

¹²¹ *Japan – Alcoholic Beverages II (AB)*, p. 29.

higher taxes.”¹²² With respect to the size of the differential in tax treatment, the Panel observed that the taxes on the vast majority of imported spirits are, “in nominal terms, approximately 10 to 40 times that applicable to all domestic spirits.”¹²³

94. If the magnitude of the difference in taxation between domestic and imported goods is sufficiently large, that difference in itself may be sufficient to show that the measure is applied so as to protect domestic production.¹²⁴ This is one such case – the taxes applied to imported products are approximately from *ten to forty times higher* than the taxes on other products. Such a differential is “nominally large”¹²⁵ and is sufficient to show that the measures protect Philippine products.

95. The Panel rightly focuses on the measure itself, which differentiates products by raw material. As the Panel explains in paragraph 7.182 of its report, by taxing products from a limited list of typical Philippine raw materials at a low rate, and everything else at a high rate, it has created a situation where *all* Philippine products have very low taxes and avoid the burdens facing imports.¹²⁶ The Panel also discussed the requirement that the designated raw material be “produced commercially” in the country where the spirit is produced. Thus, a spirit would be subject to a high tax rate if it is produced in a country that does not “commercially” produce that raw material, even if the raw material that the distiller uses is from a country that does produce the raw material commercially.¹²⁷

¹²² Panel Report, para. 7.182.

¹²³ Panel Report, para. 7.183.

¹²⁴ Panel Report, para. 7.180, citing *Japan – Alcoholic Beverages II (AB)*, p. 122.

¹²⁵ Panel Report, para. 7.183.

¹²⁶ *See also*, Panel Report, para. 2.37.

¹²⁷ Panel Report, para. 7.182, fn 559 and para. 2.8.

96. The fact that Philippine producers of distilled spirits import ethyl alcohol to produce their products in no way diminishes the Panel’s conclusion that the structure of the measure favors Philippine producers of distilled spirits. The products at issue in this dispute are brandies, whiskies, gins, vodkas and tequilas, imported and domestic, sold in the Philippine market – not the ethyl alcohol inputs used by producers. As noted above in the discussion on physical characteristics, the Panel appropriately followed the approach used by the panel in *Mexico – Taxes on Soft Drinks* and focused on the final products at issue in the dispute and their treatment, not on the raw materials or production processes from which they result.¹²⁸

97. The Philippines argues that the Panel should have relied on evidence the Philippines presented regarding the fiscal goals of the tax system.¹²⁹ The Philippines further suggests that there should be no inference that its measure is protectionist, stating, “What legislature designs a measure to protect its domestic production from ‘special occasion’ or latent competition at some indefinite point in the future?”¹³⁰ None of these arguments hold water: it is not necessary to make any inquiry into the motives of government to determine whether the structure of the Philippine measures protects domestic products – it is sufficient to know that by taxing products from designated raw materials at a very low rate, all Philippine domestic products are taxed at the lowest possible rate. Even the Philippines does not dispute the fact that imported spirits are taxed much more highly than all domestic products.

¹²⁸ Panel Report, para. 7.37, citing *Mexico – Taxes on Soft Drinks*, paras. 8.30-8.31 and 8.131.

¹²⁹ Philippines Appellant Submission, paras. 131-132.

¹³⁰ Philippines Appellant Submission, para. 131.

98. Finally, it is important to consider that if it were appropriate for the Panel to have more closely reviewed evidence on the alleged reasons for the measure, such statements do not exclusively support the Philippines. The Panel had before it statements from Philippine government officials stating that the purpose of the measure is to protect domestic production. It chose not to rely on these statements, instead making an objective judgment based on the measure itself.¹³¹

IV. The Panel Conducted an Objective Assessment of the Matter Before It

99. Each of the Philippines' five claims under Article 11 of the DSU covers a topic that it also raises under one of the claims above. Indeed, as a whole, the Philippines' Article 11 challenge merely highlights the fact that the Philippines' entire appeal is simply an attempt to reargue the facts of the dispute on appeal.

100. The Philippines' objections to the Panel's analysis in part appear premised on a misunderstanding of the role of the Panel in making factual findings. For example, the Philippines asserts that panels generally are limited in their ability to assess the facts because they are not experts in every subject.¹³² Certainly, members of a panel do not arrive as experts in the factual issues of each dispute. Yet they are not required to be, nor are they required to defer automatically to evidence authored by purported experts. Moreover, the "standard of review" invoked by the Philippines in paragraph 137 of its appellant submission does not apply to this dispute. The cited language relates to the review by panels of the risk assessment undertaken by Members when implementing sanitary or phytosanitary measures.¹³³ Because the Panel in this

¹³¹ Panel Report, para. 7.184. *See, e.g.*, Exhibit US-11.

¹³² Philippines Appellant Submission, para. 137.

¹³³ *Canada/U.S. – Continued Suspension (AB)*, paras. 585-616.

case was not assessing a Member’s assessment of scientific evidence in adopting a measure, it was not restricted by a “standard of review” in evaluating evidence.

101. Article 11 calls for a panel to “make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements.” As the Appellate Body has previously found, a panel is not required to address specifically all arguments and facts in its report. As emphasized by the Appellate Body in *EC – Poultry (AB)*:

“A panel need only address those *claims* which must be addressed in order to resolve the matter in issue in the dispute.” Just as a panel has the discretion to address only those claims which must be addressed in order to dispose of the matter at issue in a dispute, so too does a panel have the discretion to address only those *arguments* it deems necessary to resolve a particular claim. So long as it is clear in a panel report that a panel has reasonably considered a claim, the fact that a particular argument relating to that claim is not specifically addressed in the “Findings” section of a panel report will not, in and of itself, lead to the conclusion that that panel has failed to make the “objective assessment of the matter before it” required by Article 11 of the DSU.¹³⁴

102. Likewise, in this instance, the Panel had the discretion to address the arguments it found necessary to the resolution of the claims before it. The fact that it did not decide the facts of the case in the manner the Philippines requested does not mean it failed to meet its obligations or that its findings were in error.

A. The Panel Analyzed Expert Views Provided by the Philippines Along with Other Related Evidence on the Properties of the Distilled Spirits at Issue

103. The Philippines argues that the Panel impermissibly disregarded expert evidence with respect to the organoleptic properties and chemical make-up of distilled spirits and proceeded to

¹³⁴ *EC – Poultry (AB)*, para. 135 (italics in original); see also *United States – Wool Shirts and Blouses*, paras. 18–19.

substitute its own judgment for whether there are significant differences in physical characteristics with respect to these features in the products at issue.¹³⁵ Contrary to the Philippines' assertions, the Panel considered the submitted expert evidence, along with other evidence of the physical characteristics and qualities of the two categories of spirits, in evaluating whether they are "like." The Panel made an objective assessment of all relevant factors in coming to its conclusion, in accordance with Article 11 of the DSU.

104. Although the Panel did not reproduce the entirety of the expert evidence or quote directly the expert testimony, it did summarize and consider the evidence related to the congener content and organoleptic properties of the spirits.¹³⁶ The particular excerpts cited by the Philippines in its Appellant Submission must be examined in the context of the entirety of the expert evidence, which is the lens through which the Panel weighed its relevance. After considering this body of evidence, the Panel concluded that it was not probative of whether the products are "like" under Article III:2.¹³⁷ In coming to this conclusion, the Panel observed that "the differences in chemical composition between spirits made from the same raw materials, as reported in [the Philippines'] gas chromatography studies, are in most cases greater than those between spirits made from different raw materials."¹³⁸ In other words, the chemical make-ups of two "sugar based" spirits are likely to differ at least as much as the chemical make-ups of a "sugar based" spirit and "non-sugar based" spirit.

¹³⁵ Philippines Appellant Submission, paras. 139-157.

¹³⁶ Panel Report, para. 7.40 and notes 397-400.

¹³⁷ Panel Report, para. 7.40.

¹³⁸ Panel Report, para. 7.40 and note 399.

105. The Panel also noted that, although the organoleptic properties vary within and among categories of spirits, the Philippines’ submissions did not support a finding that the differences between spirits produced from designated materials and those made from other materials were distinct “such that they could be divided into two separate and identifiable groups.”¹³⁹ The Panel concluded that “there is no evidence to suggest that a non-expert consumer would be able to distinguish between imported and domestic spirits of the same type based only on the different raw materials used in their respective production,” and that the expert evidence was therefore not pertinent or significant to its reasoning.

106. The Panel’s conclusion was based in part on the premise that a “difference in raw materials would only be relevant to the extent that it results in final products that are not similar.”¹⁴⁰ Even if the expert evidence revealed that the chemical make-up of the spirits made from designated raw materials and other raw materials differed in a consistent and significant manner, that difference would only be relevant if it resulted in an identifiable dissimilarity between the products.

107. The Philippines applies circular reasoning when it argues that differences in the chemical make-up resulting from a particular raw material used renders spirits not “like.” Without some resulting perceptible difference, this reasoning amounts to asserting that “spirits made from different raw materials are not alike because they are made from different raw materials.” The Panel is required to, as it did, probe deeper into the question of what effects, if any, the differences in chemical composition have with respect to the relevant attributes of the distilled

¹³⁹ Panel Report, para. 7.40.

¹⁴⁰ Panel Report, para. 7.37 (citing *Mexico – Taxes on Soft Drinks (Panel)*, paras. 8.30-8.31 and 8.131).

spirits. Thus it turned to the physical characteristics material to the “likeness” inquiry, *i.e.*, those characteristics, such as color, flavor and aroma, that are perceptible to the consumer.¹⁴¹

108. The Panel examined the physical characteristics of each category of distilled spirit at issue in this dispute and observed that variations in the chemical compositions of a particular product may result in differing physical attributes. In general “[d]ifferent brands of spirits of the same type may have differences in taste and aroma, and a consumer may prefer one product over another,” but despite this, the Panel found that the evidence presented did not establish “that a non-expert consumer” would be able to distinguish spirits made from designated raw materials from those made with other raw materials.¹⁴²

109. In coming to this conclusion, the Panel considered each type of distilled spirit and its characteristics individually. The Panel noted, for example, that although Philippine brandies are made from sugar cane molasses (as opposed to grapes or other fruit), the process of stripping the ethyl alcohol made from sugar cane molasses of its naturally occurring congeners and adding flavoring and other ingredients results in a “final product that has the taste normally associated with brandy.”¹⁴³ In other words, Philippine brandy is purposefully produced to have the general organoleptic properties of brandy, and this result is achieved.

110. The Panel objectively assessed the expert evidence in accordance with Article 11 of the DSU. In particular, the statements cited by the Philippines, taken in the context of the entirety of the submissions, are indeterminate as to whether the spirits at issue are “like.” Although the Panel did not cite particular excerpts of the testimony, it considered this body of evidence before

¹⁴¹ Panel Report, paras. 7.41-7.47.

¹⁴² Panel Report, para. 2.26.

¹⁴³ Panel Report, para. 7.43.

concluding that it was not relevant to its inquiry. Moreover, the statements were not “pertinent” or “significant” to the Panel’s reasoning, which properly focused on whether physical characteristics, discernible to the consumer, differ between the spirits produced with the designated raw materials and spirits produced with other raw materials. In its overall treatment of the expert evidence, the Panel therefore made an objective assessment of the facts under Article 11.

B. The Panel Did Not Err in Finding the Mixed Evidence on Tariff Classification Inconclusive

111. With respect to tariff classification, the specific issue raised by the Philippines is the Panel’s treatment of the evidence of classification of brandy and whiskey at the six-digit level. This examination was one part of the tariff-classification evidence before the Panel, which included information about classification at the four-digit and six-digit level of the different spirits at issue in this dispute, including vodka, gin, rum, brandy, whiskey, and tequila.

112. At the four digit level, as discussed above, all the spirits at issue are classified under HS 2208. The Panel called this “an indication of similarity,” without drawing any stronger conclusion.¹⁴⁴ At the six-digit level, however, the evidence before the Panel was mixed between different types of spirits, and therefore the Panel ultimately did not draw any particular conclusion from the tariff classification evidence. It stated, “[b]ased on the totality of the evidence, we consider that tariff classification does not exclude the similarity between domestic and imported distilled spirits, made respectively from the designated raw materials or from other raw materials.”¹⁴⁵

¹⁴⁴ Panel Report, para. 7.63.

¹⁴⁵ Panel Report, para. 7.83.

113. The Philippines’ specific concern in its Article 11 claim is the Panel’s use of the six-digit tariff classification for brandy and whiskey. For brandies and whiskies (and rum), raw material may be relevant for tariff classification at the six digit level.

114. The Panel fully considered this evidence in its review on tariff classification. In fact, the Panel separately reviewed the evidence on tariff classification for each type of spirit, including brandy and whiskey, specifically noting the facts that the Philippines now alleges it neglected. The Panel stated, “brandies may be classified in different six-digit subheadings, depending on the raw materials from which they are made”¹⁴⁶ and “it seems that whiskies may be classified in different six-digit subheadings, depending on the raw materials from which they are made.”¹⁴⁷ Incidentally, the Panel also noted that the classification of rum depends on raw material. It stated, “HS subheading 2208.40 covers all rums . . . as they are all “[s]pirits obtained by distilling fermented sugarcane products’ (more specifically, sugar cane molasses.)”¹⁴⁸ This information on rum, however, is difficult to put together with the facts of this dispute, since it would suggest that all Philippine products are “rum” no matter what they look like, taste like, or how they are labeled.

115. In contrast to brandy and whiskey, raw material is not a factor for classification of gin or vodka.¹⁴⁹ In the case of tequila, there is no six-digit subheading, which the Panel noted in its review.¹⁵⁰

¹⁴⁶ Panel Report, para. 7.66.

¹⁴⁷ Panel Report, para. 7.69.

¹⁴⁸ Panel Report, para. 7.67.

¹⁴⁹ Panel Report, paras. 7.68 and 7.70.

¹⁵⁰ Panel Report, para. 7.70.

116. Given that the Panel reviewed the specific information on tariff classification for each type of spirit at the four-digit and six-digit level, it plainly carried its burden with respect to review of the evidence. As to its conclusions at the six-digit level, given that the significance of raw material varies for different types of spirits, the statement that at the six-digit level “HS classification does not give us conclusive guidance¹⁵¹” is perfectly reasonable and far from a breach of the Panel’s obligations under Article 11 of the DSU.

C. The Panel Closely Examined the Economic Studies on Substitutability and Drew Appropriate Conclusions in the Context of Other Related Evidence in this Dispute

117. In its challenge to the Panel’s use of the studies, the Philippines gives an imprecise picture of the Panel’s conclusions. Contrary to what the Philippines suggests, the Panel undertook a detailed review of the specifics of the studies on consumer preferences, and applied this review objectively to reach its findings. For example, at paragraph 171 of the Philippines’ submission, it challenges the Panel’s finding that, “despite the shortcomings of the studies submitted by the parties with regard to the competitive relationship between the relevant products, we consider that there is enough evidence to suggest a significant degree of competitiveness or substitutability for those distilled spirits in the Philippines market.”¹⁵² The Philippines asserts that the Abrenica & Ducanes study it provided does not support this conclusion.

¹⁵¹ Panel Report, para. 7.71. At the four-digit level, the Panel found an “indication of similarity” for all distilled spirits, since they are all classified under HS 2208. Panel Report, para. 7.63.

¹⁵² Panel Report, para. 7.62.

118. If one turns to the section where the Panel makes this statement, however, it is clear that the Panel did not solely base this conclusion on that study. This conclusion comes at the end of a more general section on the criteria “consumers’ tastes and habits.” In that section, the Panel took note of the similarity between marketing campaigns and sale locations for imported spirits and domestic Philippines spirits.¹⁵³ In that section, the Panel also emphasized the importance of the similar labels for domestic and imported products in terms of consumer perceptions, stating,

Generally speaking, labels of domestic Philippine distilled spirits made from the designated raw materials tend to mimic or replicate the names of products and designs of the similar imported spirits made from other raw materials. The raw materials used in the manufacture of domestic Philippine distilled spirits are not mentioned on the labels. Thus, there is nothing that would suggest to the consumer that these products are different from imported spirits made from other raw materials.¹⁵⁴

119. In other words, the Panel drew its conclusion based a review of the variety of evidence relevant to the specific criteria of consumer tastes and habits, specific to the facts of the Philippine market where consumers in stores face nearly indistinguishable Philippine and imported gins and brandies.¹⁵⁵

120. With respect to the more specific discussion of the Abrenica & Ducanes study and the Euromonitor International study, the Panel thoroughly weighed the evidence, including concerns with the methodology of each study.

121. Both studies were based on survey data on consumers’ reported preference. For the Euromonitor International study, respondents were selected at random from an online panel, “with specific adjustments to age, gender and living location that allowed for closer alignment

¹⁵³ Panel Report, para. 7.51.

¹⁵⁴ Panel Report, para. 7.61.

¹⁵⁵ *See, e.g.*, Exhibits US-30, 38, and 42.

with the total population.”¹⁵⁶ They answered detailed questions about imported and domestic brands of spirits by product type (*e.g.* gin) on when and where they consume different spirits, and how they drink each type.¹⁵⁷ These responses showed the strong similarity between domestic and imported distilled spirits. In addition, the respondents answered questions about their purchases under several counterfactuals, where imported brands decreased in price and domestic brands increased in price.¹⁵⁸ These data were not intended to be a cross-price elasticity study. They do, however, provide an indication of how Philippine consumers would respond if imported and domestic spirits were priced more similarly.

122. In the scenarios posed in the survey, imported spirits were still more expensive than domestic products. Yet, the respondents indicated that they would be more likely to purchase an imported brand if the price differential was smaller.¹⁵⁹ These responses, along with other data collected by the study, show the substitutability between imported and domestic products.

123. Similarly, the Abrenica and Ducanes study reported responses to a survey with questions based on hypothetical changes in prices of distilled spirits. Although the methodology applied by Abrenica and Ducanes was different from the methodology used by Euromonitor International, the hypothetical scenarios similarly included choices where imported spirits were relatively more expensive. Nonetheless, these respondents also show potential for greater willingness to purchase imported spirits if they were relatively less costly.

¹⁵⁶ Exhibit US-41, p. 6.

¹⁵⁷ Exhibit US-41, p. 17.

¹⁵⁸ Exhibit US-41, p. 30.

¹⁵⁹ Exhibit US-41, p. 30.

124. Given that distilled spirits are experience goods, and consumers may be unlikely to replace their usual brand with a new brand even if priced the same, the willingness of the survey respondents to try imported brands *even though they are more expensive* is a useful finding. The Panel did not err by taking these survey results into account.

125. The parties differ in the implications of the results of the studies for the dispute. In the Philippines' view, it is appropriate to jump from those results alone to the conclusion that there is no substitutability. It states that its own study showed "negligible levels of substitutability such that no substitutability could be properly found to exist."¹⁶⁰ In the view of the United States, no such conclusion is required. While small, the findings *did* show substitutability – in spite of the persistent price gaps between imported and domestic products, and in spite of other factors, such as brand loyalty, that may affect decisions.¹⁶¹ Moreover, the findings on substitutability should be considered in the context of this particular case and the evidence before the Panel. While cross-price elasticity is one means to examine the relevant market, it "is not necessarily a 'decisive criterion.'"¹⁶² In other words, it is a question of the weight of the evidence – the Philippines disagrees with the Panel on the weight to be accorded to the study results in the Panel's conclusions.

126. As noted above, there is other evidence besides the studies that the Panel considered with respect to consumer tastes, preferences, and substitutability of imported and domestic brands of distilled spirits. Taking this into consideration, the Panel made a modest, tailored finding with

¹⁶⁰ Philippines Appellant Submission, para. 164.

¹⁶¹ Panel Report, paras. 2.45 and 7.50. *Chile – Alcoholic Beverages (Panel)*, para 7.72, citing *Korea – Alcoholic Beverages (AB)*, para. 123.

¹⁶² Panel Report, para. 7.108, citing *Japan – Alcoholic Beverages II (AB)*.

respect to the studies: they *support the proposition* that there is a significant degree of competitiveness or substitutability in the Philippine market between the distilled spirits at issue in the present dispute.”¹⁶³

D. The Panel Did Not Fail to Consider Relevant Evidence in Its Findings on Market Segmentation

127. The Philippines has tried throughout this dispute to make the issue before the Panel the income of consumers. With respect to its Article 11 claims, this theme comes through most clearly in its challenge to the Panel’s finding that the Philippines does not have “two separate distilled spirits markets.”¹⁶⁴ It bases this challenge primarily on the evidence of the relatively low income of the majority of Filipinos, and secondarily on a misreading of evidence in the Euromonitor Study.

128. With respect to the data on income, neither the complainants nor the Panel contested the Philippine assertion that most Filipinos are low-income consumers. But that evidence does not necessarily lead to the conclusion that the market is segmented.

129. The Philippines’ statistics for market segmentation are based on the market “segments” which it introduced, using national statistics on income and average expenditures on alcoholic beverages.¹⁶⁵ There are several categories, each covering a range of income levels. Consumers can be included in the appropriate category, but this does not mean that each category is a distinct

¹⁶³ Panel Report, para. 7.113 (emphasis added).

¹⁶⁴ Panel Report, para. 7.40.

¹⁶⁵ Philippines First Written Submission, paras. 44-46.

“market segment.” In addition, the data on expenditures on spirits are based on averages,¹⁶⁶ and say little about how individual consumers choose which spirits to buy or how much to buy.

130. A primary reason that the income data do not lead to the conclusion the Philippines urges is that this dispute is not about price. The Philippines’ measures apply low taxes on the basis of raw material, not price or quality or any other factor. Within the basket of Philippine domestic distilled spirits, there are relatively low and relatively higher priced products.¹⁶⁷ There are also premium and specialty brands.¹⁶⁸ The Panel’s failure to draw the Philippines’ conclusion from the data on income demonstrates that it considered other evidence more relevant to the issues before it concerning the Philippine measures.

131. The Philippines tries to bolster its argument by claiming that the evidence of the Euromonitor Study show that quality, taste, and social acceptability may affect “the upper portion” of consumers’ choices regarding spirits. This conclusion, however, depends on two false premises: (1) seeing the Euromonitor Study as only pertaining to upper income consumers; and (2) assuming that other consumers do not consider quality, choice, or social acceptability in their purchases. Neither are valid. Although the average income of the respondents to the Euromonitor International survey was higher than the average Filipino, the study was based on questions of a group of consumers in the Philippines who frequently purchased or consumed spirits and was not restricted to an “upper income” segment. More importantly, there is no evidence that the factors other than price that influence purchases (*e.g.*, taste and quality) only

¹⁶⁶ *Id.*

¹⁶⁷ Panel Report, para. 7.118.

¹⁶⁸ Panel Report, para. 2.42.

affect some consumers. Indeed, the effect of factors other than price on purchasing decisions (e.g. brand loyalty) has been noted in past disputes.¹⁶⁹

132. Finally, within the claim on market segmentation, the Philippines also raises a tangential point regarding a comparison to *Korea – Alcoholic Beverages*. The Philippines’ concern centers on the differences between Korea and the Philippines (see paras. 48-49 above).

133. But in the analogy in question, the Panel did not compare the Korean and the Philippine market. The analogy was with respect solely to the potential difference between major purchases, such as automobiles, and a more frequent purchase, such as distilled spirits. As discussed above, the point made in *Korea – Alcoholic Beverages* was that because of the volume of purchases and the incremental cost of each purchase, it is relatively more likely that a lower-income consumer may splurge on a more expensive distilled spirit than that he or she will choose a luxury automobile. Citing this general principle does not require any similarity between the Philippine and Korean markets – other than that Filipino consumers frequently purchase distilled spirits as a general matter, which they do.

E. The Panel Did Not Err in Finding Potential Competition Between Imported and Domestic Products in the Philippines Market

134. The Philippines’ final claim of error fails because it misinterprets the Panel’s conclusion. The Philippines takes issue with the Panel’s finding that the products at issue are “capable of being directly competitive or substitutable in the future,” on the basis that the majority of Filipino consumers are too poor to have the capacity to purchase imported spirits.¹⁷⁰

¹⁶⁹ *Chile– Alcoholic Beverages (Panel)*, para 7.72, citing *Korea – Alcoholic Beverages (AB)*, para. 123.

¹⁷⁰ Philippines Appellant Submission, para. 185.

135. The “capacity” at issue for the purposes of whether Philippine distilled spirits and imported distilled spirits are directly competitive or substitutable (or “like”) is the capacity of the *products*. Products are “directly competitive or substitutable” within the meaning of the second sentence of Article III:2 if they “are interchangeable or if they offer ‘alternative ways of satisfying a particular need or taste.’”¹⁷¹

136. The United States does not suggest that lower-income Filipinos will purchase expensive products in the near future. Nor did the Panel. But income levels are not the right evidence for whether consumers would see two different “brandies,” or whether the two products would satisfy the same “need or taste.”

137. As noted at the beginning of Section IV, a panel has the discretion to address only the arguments necessary to resolve a claim. The Panel properly relied on evidence such as product characteristics,¹⁷² marketing,¹⁷³ and end-uses¹⁷⁴ to determine that Philippine distilled spirits and imported distilled spirits have the potential to be (indeed, are) directly competitive or substitutable.

138. Although the Philippines argues that the Panel should have relied on its different theory and different facts, the fact that it did not do so was within the discretion of the Panel and not a violation of its obligations under Article 11.

V. Conclusion

¹⁷¹ Panel Report, para. 7.100, citing *Korea – Alcoholic Beverages (AB)*, para. 115.

¹⁷² Panel Report, para. 7.127.

¹⁷³ Panel Report, para. 7.131.

¹⁷⁴ Panel Report, para. 7.129.

139. For all the above reasons, the United States respectfully requests the Appellate Body to reject the Philippines' appeal in its entirety.