Mexico – Tax Measures on Soft Drinks and Other Beverages
(WT/DS308)

December 20, 2004

Answers of the United States to Questions of the Panel in Relation to the First Substantive Meeting with the Parties

For Both Parties

> **Q1. Mexico has alluded to the exercise of "judicial economy" as a reference for its argument that panels have certain implied jurisdictional powers that would allow them to decline from exercising substantive jurisdiction. Could Parties please comment on the relevance of the exercise of "judicial economy" in the context of Mexico's request for the present Panel to decline to exercise its jurisdiction.**

1. Mexico is confusing two wholly separate concepts – "judicial economy" is distinct from "substantive jurisdiction."[1] Judicial economy is not a concept whereby panels decline to exercise substantive jurisdiction either over a dispute or certain claims forming the basis of a dispute. Rather, judicial economy is a concept under which panels – *recognizing that they have substantive jurisdiction and in their exercise of that jurisdiction* – decline to make findings on certain claims when resolution of such claims is not necessary in order for the panel to fulfill its mandate. A panel's mandate is to make findings to "assist the DSB in making the recommendations and providing the rulings provided for in the covered agreements."[2] This mandate is found in Article 11 of the DSU as well as in the standard terms of reference provided in Article 7.1 of the DSU and this Panel's terms of reference in particular. Judicial economy is a well-recognized and common-sense concept under the DSU. However, there is no basis in the DSU for a panel to decline to carry out the functions for which the DSB established it nor to disregard the tasks that the DSB assigned to it. Accordingly, the concept of "judicial economy" does not support Mexico's position that panels have certain implied jurisdictional powers to decline to exercise substantive jurisdiction.

2. The Appellate Body's examination of judicial economy in *Australia – Salmon* is illustrative. In that dispute, the Appellate Body accepted that panels may exercise judicial economy, but it considered the concept in keeping with the purpose of WTO dispute settlement and a panel's mandate. This is in contrast to Mexico's request for the Panel to decline jurisdiction which even Mexico admits finds no basis in the DSU or elsewhere in the WTO Agreement. The Appellate Body in *Australia – Salmon* stated:

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[1] The United States notes that "substantive jurisdiction" is not a term used in the DSU or the WTO agreements. Accordingly, the United States assumes that by "substantive jurisdiction" Mexico is referring to carrying out the terms of reference of the Panel.

[2] DSU, Art. 11.

> The principle of judicial economy has to be applied keeping in mind the aim of the dispute settlement system. This aim is to resolve the matter at issue and "to secure a positive solution to a dispute". To provide only a partial resolution of the matter at issue would be false judicial economy. A panel has to address those claims on which a finding is necessary in order to enable the DSB to make sufficiently precise recommendations and rulings so as to allow for prompt compliance by a Member with those recommendations and rulings in order to ensure effective resolution of disputes to the benefit of all Members.[3]

3. The Appellate Body's finding in *US – Wool Shirts* is also instructive: "A panel need only address those claims which must be addressed in order to resolve the matter in issue in the dispute."[4] "The 'matter in issue' is the 'matter referred to the DSB' pursuant to Article 7 of the DSU."[5] The Panel cannot resolve the matter in dispute – *i.e.*, the U.S. claims that Mexico's tax measures are inconsistent with Article III of the GATT – unless it exercises jurisdiction over that matter and issues findings thereon.

Q2. Could Parties please comment whether they are of the view that there is nothing in the WTO agreements that explicitly spells out the implied jurisdictional power that panels may have that allows them to decline to exercise substantive jurisdiction, as Mexico has suggested. Or do they rather consider that there is nothing in the WTO agreements that explicitly rules out the existence of such power? If there are no such explicit rules in the WTO agreements, then what conclusions, if any, should the present Panel draw in order to respond to Mexico's request to decline to exercise its jurisdiction?

4. Under the provisions of the WTO Agreement, a panel lacks the power to decline to "exercise substantive jurisdiction" over a matter which has been properly brought before it. For the reasons that follow, Mexico's request not only lacks any basis in the WTO Agreement but is, in fact, incompatible with it. Specifically, Mexico's request for the Panel to decline to exercise jurisdiction over this dispute is incompatible with Articles 11 and 7 of the DSU and the Panel's terms of reference. Mexico is simply inviting the Panel to breach its obligations under the DSU just as (or perhaps because) Mexico has breached its own WTO obligations.

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[3] Appellate Body Report, *Australia – Measures Affecting Importation of Salmon*, WT/DS18/AB/R, adopted 6 November 1998, para. 223. In *Australia – Salmon*, while the Appellate Body recognized the use of judicial economy, it did not accept that particular panel's exercise of it.

[4] Appellate Body Report, *United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India* (*US – Wool Shirts*), WT/DS33/AB/R and Corr.1, adopted 23 May 1997, p. 19; *see also* Appellate Body Report, *United States – Imposition of Countervailing Duties on Certain Hot-Rolled Lead and Bismuth Carbon Steel Products Originating in the United Kingdom* (*US – Lead Bismuth II)* , WT/DS138/AB/R, adopted 7 June 2000, para. 70 (quoting the Appellate Body in *Wool Shirts*).

[5] Appellate Body Report, *US – Wool Shirts*, p. 19, n. 30.

5. Article 11 of the DSU provides that panels shall make "findings as will assist the DSB in making the recommendations and in giving the rulings provided for in the covered agreements." The Panel's terms of reference provide that the Panel shall "make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in [the GATT 1994]."[6] For the Panel to decline to exercise jurisdiction over this dispute would mean that the Panel would make no findings on the U.S. claims that Mexico's tax measures are inconsistent with Article III of the GATT 1994. This in turn would leave the DSB unable to make any recommendations or rulings in accordance with the rights and obligations under the DSU and the GATT 1994. Such a result is incompatible with the text of the DSU. As noted above, it would require a panel to disregard the reason for its existence and the mandate given it by the DSB.

6. Mexico's request is also incompatible with Article 7 of the DSU and the Panel's terms of reference. Article 7.1 of the DSU states that panels (with standard terms of reference as this Panel has) are required " to examine ... the matter" referred to the DSB by the complaining party and "to make such findings as will assist the DSB" in making recommendations and rulings. Article 7.2 of the DSU further states that panels "*shall address* the relevant provisions in any covered agreement or agreements cited by the parties" to a dispute.[7] The Panel's own terms of reference in this dispute instruct the Panel "to examine ... the matter referred to the DSB by the United States" – the consistency of Mexico's tax measures with Article III of the GATT – and "to make such findings as will assist the DSB in making" the recommendations and rulings provided for under that Agreement.[8]

7. These conclusions with respect to Articles 11 and 7 of the DSU are supported by the context provided by other provisions of the DSU. Article 3.3 of the DSU provides that "[r]ecommendations or rulings made by the DSB shall be aimed at achieving a satisfactory settlement of the matter *in accordance with the rights and obligations under [the DSU] and under the covered agreements*."[9] Article 3.7 provides that the "aim of the dispute settlement system is to secure a positive solution to a dispute,"[10] and Article 3.2 states that the dispute settlement system "serves to preserve the rights and obligations of Members under the covered agreements."[11] Article 12.7 provides that where the parties have not resolved the dispute, "the report of the panel shall set out the findings of fact, the applicability of relevant provisions and the basic rationale behind any findings and recommendations that it makes." An approach that would permit a panel to decline to exercise jurisdiction over a dispute would be contrary to the ordinary meaning of those provisions and fail to preserve the rights and obligations at issue in the dispute.

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[6] WT/DS308/5.Rev.1.

[7] DSU Art. 7.2 (emphasis added).

[8] WT/DS308/5/Rev.1.

[9] DSU Art. 3.3 (emphasis added).

[10] DSU Art. 3.7.

[11] DSU Art. 3.2.

8. The text of the DSU cannot be rendered *inutile,* as it would be were a panel to grant a party's request for the panel to decline to exercise jurisdiction over a dispute. As the Appellate Body recognized in the earlier case regarding Mexico's antidumping measures on HFCS, "as a matter of due process, and the proper exercise of the judicial function, panels are required to address issues that are put before them by the parties to a dispute."[12]

9. The United States also refers the Panel to the Appellate Body report in *India – QRs* cited by the United States in its oral statement and the panel's findings in *United States – FSC* and *Turkey – Textiles*.[13] In the FSC dispute, for example, the United States argued that text in the SCM Agreement stating that "Members shall normally attempt to resolve their differences using the facilities of existing bilateral tax treaties or other specific international mechanisms" "expressly directs WTO Members to resolve certain issues raised by exemptions from direct taxes in an appropriate tax forum before resorting to WTO dispute settlement."[14] The panel disagreed, stating that the text cited by the United States did not provide "a clear and unambiguous basis for circumscribing the right to resort to WTO dispute settlement at any time."[15] The panel explained:

> Under Article XXIII of GATT 1994, the DSU and Article 4 of the SCM Agreement, a Member has the right to resort to WTO dispute settlement at any time by making a request for consultations in a manner consistent with those provisions. This fundamental right to resort to dispute settlement is a core element of the WTO system. Accordingly, we believe that a panel should not lightly infer a restriction on this right into the WTO Agreement; rather, there should be a clear and unambiguous basis in the relevant legal instruments for concluding that such a restriction exists.[16]

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[12] Appellate Body Report, *Mexico – Anti-Dumping Investigation of High Fructose Corn Syrup (HFCS) from the United States – Recourse to Article 21.5 of the DSU by the United States* (*Mexico – Corn Syurp (21.5)*), WT/DS132/AB/RW, adopted 21 November, para. 36.

[13] Appellate Body Report, *India – Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products*, WT/DS90/AB/R, adopted on 22 September 1999, para. 84; Panel Report, *United States – Tax Treatment for "Foreign Sales Corporations"*, WT/DS108/R, adopted as modified on 20 March 2000, paras. 7.12-7.19; Panel Report, *Turkey – Restrictions on Imports of Textile and Clothing Products* (*Turkey – Textiles*), *WT/DS34/R,* adopted as modified 19 November 1999, paras. 9.15-9.17 (rejecting Turkey's argument that the appropriate forum for resolution of India's claims under the GATT 1994 was in the first instance the WTO Textile Monitoring Body (TMB) and, therefore, that the panel lacked jurisdiction over the dispute until India's remedies under the TMB had been exhausted).

[14] Panel Report, *US – FSC*, para. 7.12.

[15] Panel Report, *US – FSC*, para. 7.19.

[16] Panel Report, *US – FSC,* para. 7.17.

10. Finally, we note that Mexico does not contest that the U.S. claims have been properly brought before this Panel and even concedes that this Panel has "*prima facie* jurisdiction" over those claims.

11. For all the foregoing reasons, there is absolutely no basis for the Panel to grant Mexico's request.

Q3. Can Parties please comment whether, in their opinion, it would be appropriate for the Panel to look at the issues concerning bilateral trade in sweeteners between Mexico and the United States which have been raised by Mexico in this case.

12. To the extent the Panel's question is directed at knowing whether it may interpret the provisions of the NAFTA and determine whether certain obligations thereunder have or have not been met, the answer is no. Such an examination would clearly exceed the Panel's mandate. The DSB established this Panel to "examine, in the light of the relevant provisions of the covered agreements cited by the United States in document WT/DS308/4, the matter referred to the DSB by the United States in that document, and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements."[17] The relevant provision of the covered agreements cited by the United States is Article III of the GATT 1994 and the matter referred to the DSB by the United States is the consistency of Mexico's tax measures with Article III of the GATT 1994.[18] These terms of reference define the limited mandate for which this Panel was established. The Panel's mandate simply does not extend to examining the issues raised by Mexico that the United States has breached its NAFTA obligations with respect to market access for Mexican sugar or has "refus[ed] to submit" to dispute settlement under the NAFTA.

13. Moreover, it would be inappropriate for the Panel substantively to address these "bilateral trade in sweeteners" issues because, with respect to Mexico's request for the Panel to decline jurisdiction, the Panel lacks the power to decline jurisdiction over the matter for which it was established (much less in favor of dispute settlement under NAFTA) and, with respect to Mexico's Article XX(d) defense, obligations under international agreements such as the NAFTA are not "laws or regulations" within the meaning of Article XX(d).

Q4. Can Parties indicate whether, in their opinion, is there anything in the North American Free Trade Agreement (NAFTA) that would prevent the United States from bringing the present case to the WTO dispute settlement system.

14. Nothing in the WTO Agreement precludes a Member from exercising its rights under the WTO Agreement – including the right to bring a claim under the DSU – based on the terms of

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[17] WT/DS308/5.Rev.1.
[18] WT/DS308/4.

the NAFTA. Similarly, there is nothing in the WTO Agreement which would authorize a panel to fail to make the findings, rulings and recommendations required by DSU Article 11 based on the terms of the NAFTA. Having said this, there is nothing in the NAFTA that provides that the United States may not bring the present dispute to the WTO dispute settlement system, although the United States notes that a determination of rights and obligations under the NAFTA is outside this Panel's terms of reference.

Q5. If, as requested by Mexico, the Panel were to decline to exercise its jurisdiction in favour of NAFTA, could the Parties please comment how the NAFTA system would deal comprehensively with all the issues that Mexico considers affect the bilateral trade in sweeteners between Mexico and the United States. Could the Parties please also comment whether the NAFTA system could provide the same remedies that the United States is seeking in this case under the WTO.

15. For the reasons set forth above, there is no basis in the WTO Agreement for Mexico's request that the Panel decline to exercise its jurisdiction in this dispute. This is the case regardless of how the NAFTA system would deal with matters that were not identified in the U.S. panel request and, thus, are not within the Panel's terms of reference of this dispute.

16. Furthermore, not even the WTO deals "comprehensively" with issues. Mexico has raised a number of issues that are distinct, some involving measures by Mexico, some involving alleged measures by the United States. The DSU, in Article 3.10, explicitly requires that complaints and counter-complaints on distinct matters not be linked. Accordingly, Mexico could not even request the WTO to make "comprehensive" findings on these various matters, even if they were all WTO matters. Mexico certainly cannot then expect a WTO panel to seek a comprehensive solution through other means.

17. That said, the NAFTA system could not provide the same remedies that the United States is seeking under the WTO. To take just one example, the remedies under the NAFTA are limited to NAFTA concessions. WTO remedies are broader.

Q6. If, as requested by Mexico, the Panel were to decline to exercise its jurisdiction in favour of NAFTA, could the Parties please comment whether the United States right to request a panel under NAFTA to examine the claims that have been brought to this Panel may be affected by the United States having previously brought this same case to the WTO.

18. As discussed above, there is no basis in the WTO Agreement for Mexico's request that the Panel decline to exercise its jurisdiction in this dispute. This is the case regardless of how U.S. NAFTA rights would be affected by this dispute.

19. Having said this, Article 2005(6) of the NAFTA states: "Once dispute settlement procedures have been initiated under Article 2007 or dispute settlement proceedings have been

initiated under the GATT, the forum selected shall be used to the exclusion of the other, unless the Party makes a request pursuant to paragraph 3 and 4." Article 2005(3) and (4) deal with matters concerning certain environmental, health or safety related issues. Article 2005(7) states: "For purposes of this Article, dispute settlement proceedings under the GATT are deemed to be initiated by a Party's request for a panel, such as under Article XXIII:2 or the *General Agreement on Tariffs and Trade 1947*, or for a committee investigation, such as under Article 20.1 of the Customs Valuation Code."

Q7. Could the Parties please inform the Panel what is the present state of the dispute that Mexico has brought against the United States under NAFTA concerning the bilateral trade in sweeteners.

20. The United States recalls again that NAFTA dispute settlement matters are outside the Panel's terms of reference. That said, the dispute Mexico has brought against the United States under NAFTA (regarding the U.S. tariff-rate-quota on Mexican sugar) is presently in the panelist selection stage. Prior to that stage, the United States and Mexico engaged in consultations pursuant to the NAFTA's dispute settlement provisions, and, having been unable to resolve the matter through consultations, the NAFTA Free Trade Commission established a panel. In addition, the United States and Mexico, as well as their affected industries, have held negotiations throughout this period, as recently as October 2004 (affected industries) and March 2003 (governments of United States and Mexico).

Q8. The Panel has noted that in paragraph 2(g) of the written version of its oral statement dated 2 December, Mexico has stated that it "triggered the dispute settlement mechanism [in NAFTA]" ("activó el mecanismo de solución de controversias") concerning its complaint against the United States related to the bilateral trade in sweeteners. Could the Parties please clarify when are dispute settlement procedures in NAFTA considered to have been triggered ("activados").

21. The United States recalls again that NAFTA dispute settlement matters are not within the Panel's terms of reference. That said, it is unclear what Mexico means by "triggered the [NAFTA] dispute settlement mechanism," which consists of several phases.

Q9. The Panel notes that, in its first submission dated 1 November, Mexico did not present any responses as to the substance of the alleged violations of Article III of the GATT 1994 claimed by the United States in its first submission (except by saying that any violations would be justified under Article XX(d) of the GATT). Could the Parties please comment what conclusions, if any, should the Panel draw from Mexico's lack of response on the claims under Article III. Should the Panel consider the evidence on the record and, drawing the appropriate legal conclusions from the fact that Mexico has not raised any substantive defence against the United States' claims under Article III, undertake an examination of whether the conditions

required by the different provisions of Article III are met, before making its findings?

22. The Panel should construe Mexico's lack of response on U.S. claims under Article III of the GATT 1994 to mean that Mexico does not contest that its tax measures are in breach of its Article III obligations. The panel in *US – Shrimp* took the U.S. statement that it did not dispute that the measure at issue "amounts to a restriction on the importation of shrimp within the meaning of Article XI:1 of GATT 1994" to mean that the United States "basically admits that a given measure amounts to a restriction prohibited by GATT 1994."[19] Similarly, the panel in *Turkey – Textiles* found that "given the absence of a defense by Turkey (other than its defense based on Article XXIV of GATT) to India's claims that discriminatory import restrictions have been imposed, India has made a *prima facie* case of violation of Articles XI and XIII of GATT."[20] Accordingly, in this dispute the Panel should undertake a brief analysis confirming that the United States has made its *prima facie* case. In this regard, all uncontested facts presented by the United States should be accepted for purposes of the Panel's factual and legal findings in this dispute.

23. In light of Mexico's decision not to contest the Article III breach and the extensive evidence and argumentation the United States submitted in its first submission, the Panel should similarly conclude that the United States has made a *prima facie* case of Mexico's breach of the provisions of Article III at issue in this dispute.

Q10. In its oral statements, the European Communities raised issues concerning the treatment accorded in Mexico to soft drinks sweetened with beet sugar. Could Parties share with the Panel any views they may have regarding the treatment accorded in Mexico to soft drinks and syrups sweetened with products different from cane sugar and High-Fructose Corn Syrup (HFCS), such as, for example, beet sugar and saccharine. Would these soft drinks and syrups (those sweetened with products different from cane sugar and HFCS) be covered by the scope of the United States' claims?

24. Mexico's tax measures also treat beet sugar and non-nutritive sweeteners such as saccharine less favorably than cane sugar. In particular, as explained in the U.S. First Written Submission (paras. 38-39), Mexico's tax measures (as embodied in the IEPS) apply to all sweeteners other than cane sugar and all soft drinks and syrups made with any sweetener other than cane sugar. Mexico's tax measures, therefore, afford the same less favorable treatment and impose the same excess taxation on all non-cane sugar sweeteners – including beet sugar and saccharine – and soft drinks and syrups made with those sweeteners as it does on HFCS and soft drinks and syrups made with HFCS.

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[19] Panel Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/R, adopted 6 November 1998, para. 7.15.

[20] Panel Report, *Turkey – Textiles*, para. 9.66.

25. The United States notes that beet sugar is chemically and functionally identical to cane sugar.[21] It is, therefore, "like" and "directly competitive or substitutable" with cane sugar. Thus, Mexico's tax measures also breach the provisions of Article III with respect to beet sugar and soft drinks sweetened with beet sugar, and the Panel should so find. Having said this, as Mexico has made clear, its measures are intended to discriminate against HFCS and soft drinks and syrups sweetened with HFCS and this is the focus of the U.S. complaint.

Q11. Could the Parties please clarify whether, in their opinion, a measure, as applied to a product, may be at the same time an "internal tax measure" for such a product within the meaning of Article III:2 of the GATT, as well as a "law or regulation affecting the use" of such product within the meaning of Article III:4.

26. The IEPS is both an "internal tax" on HFCS for use in soft drinks and syrups within the meaning of Article III:2 and a "law ... affecting the internal ... use" of HFCS within the meaning of Article III:4. The United States refers the Panel to its response to Question 21.

Q12. Could the Parties please comment whether, in their opinion, the Panel could accept the contentions made by the United States of the issues regarding their claims under Article III of the GATT and at what level. Is there any difference in the manner in which the Panel should treat facts and legal arguments in the case?

27. In light of the evidence and arguments set forth in the U.S. first submission and Mexico's decision not to respond, the Panel should find that the United States has established a *prima facie* breach of each of the cited provisions of GATT 1994 Article III, as set forth in the U.S. request for findings in paragraph 163 of its first submission. Like the panels in *US – Shrimp* and *Turkey – Textiles*, this Panel should undertake a brief analysis confirming that the U.S. has made its *prima facie* case. In this regard, all uncontested facts should be taken as given.

Q13. Are any soft drinks or sweetened syrups other than those sweetened with cane sugar exempted from the tax? Are soft drinks or sweetened syrups from any particular origin exempted from the tax?

28. The text of the IEPS before the Panel provides that with the exception of the public sales exemption,[22] all soft drinks or syrups other than those sweetened solely with cane sugar are subject to the tax.[23] Article 1(I) of the IEPS taxes the "transfer in national territory, or as applicable, the final importation, of goods identified in the Law." Article 2(I)(G) and (H) apply the 20 percent tax rate to the "transfer or, as applicable, the importation of" soft drinks and

[21] U.S. First Written Submission, para. 22.

[22] *See* U.S. First Written Submission, para. 41(discussing the public sales exemption).

[23] *See* Exhibit US-4A and US-4B (Ley Del Impuesto Especial Sobre Produccióny y Servicios (IEPS), Dec. 31, 2003); U.S. First Written Submission, paras. 37-47 (quoting relevant portions of the IEPS).

syrups. Similarly, Article 1(II) taxes the "provision of services indicated in this Law" and Article 2(II) applies the 20 percent tax to the provision of services (*i.e.* representation, brokerage, agency, consignment and distribution) "for the purpose of transferring" soft drinks and syrups. Articles 1 and 2 make no distinction between soft drinks and syrups based on the type of sweetener used. That distinction appears in Article 8 of the IEPS which exempts from payment of the tax "transfers" of the "goods referred to in Article 2(I)(G) and (H) of this Law, provided only sugarcane is used as a sweetener." Therefore, the only soft drinks and syrups exempt from the IEPS are those sweetened only with cane sugar.

29. The tax does not exempt soft drinks and syrups imported from any particular country from payment of the tax. The IEPS taxes the importation of all soft drinks and syrup regardless of the type of sweetener used.[24] Soft drinks and syrups of Mexican origin, however, if sweetened only with cane sugar are exempt for the IEPS.

Q14. Does the difference in the treatment between "transfers" and "importations", if there is such a difference, also apply to the tax imposed by Mexico on the "agency, representation, brokerage, consignment and distribution" of imported soft drinks and sweetened syrups?

30. The text of the IEPS before the Panel appears to distinguish between "transfers" and "importations." As mentioned above, Article 1(I) of the IEPS taxes the "transfer in national territory, or as applicable, the final importation, of goods identified in the Law." Article 2(I)(G) and (H) also specify that the tax applies to the"transfer or, as applicable, the importation of" soft drinks and syrups." Article 8 of the IEPS, however, specifies that the tax "shall not be paid [o]n the following transfers" and identifies soft drinks and syrups sweetened only with cane sugar as exempt from the tax. Article 8 does not include reference to "importation" as do Articles 1 and 2 of the IEPS. Thus, only internal transfers of soft drinks and syrups are subject to the exemption provided for in Article 8.[25]

31. After importation, however, a soft drink or syrup may be transferred internally. Therefore, if that soft drink or syrup were sweetened only with cane sugar, it would be subject to the exemption provided for in Article 8.

32. As for the tax on the agency, representation, brokerage, consignment and distribution of soft drinks and syrups ("distribution tax"), Article 2(II) of the IEPS states that it applies to representation, brokerage, agency, consignment and distribution "for the purpose of transferring" soft drinks and syrups. The United States understands the exemption for internal transfers of soft drinks and syrups provided for in Article 8 of the IEPS to cover both an exemption from the tax

[24] *See* Exhibit US-4A and US-4B (IEPS, Dec. 31, 2003), Arts 1, 2 and 8..

[25] *See* Exhibit US-4A and US-4B (IESP, Dec. 31, 2003), Arts. 1, 2 and 8.

on internal transfers of soft drinks and syrups (the HFCS soft drink tax as referenced in the U.S. first submission) and the distribution tax.[26]

Q15. In the view of the Parties, are sweeteners, when they are used as inputs in the preparation of soft drinks and syrups, subject to the tax measures at issue in this case, or are taxes only applied to the soft drinks and syrups?

33. The IEPS applies a 20 percent tax on the importation, internal transfer and distribution of soft drinks and syrups sweetened with any sweetener other than cane sugar. The IEPS is both a tax on soft drinks and syrups and a tax on non-cane sugar sweeteners such as HFCS.

34. Specifically, on the one hand, the IEPS is a tax on soft drinks and syrups – in particular on soft drinks and syrups imported from the United States where HFCS is the dominant soft drink and syrup sweetener. On the other hand, the IEPS is a tax on HFCS for soft drink and syrup use. The IEPS happens to apply this tax at the time when the soft drink or syrup containing HFCS is sold or distributed. (It should be pointed out that by doing so, Mexico is able to convert the 20 percent tax on the soft drink or syrup to a 400 percent tax on the HFCS in that soft drink or syrup). The timing of tax collection, however, does not change the fact that it is the use of HFCS as a sweetener in the soft drink or syrup that determines whether any tax is owed. Thus, even though the IEPS more directly applies to soft drinks and syrups, it is also a tax on the HFCS used to make those soft drinks and syrups. In fact, Mexico essentially concedes this point when it states that the IEPS was imposed to stop the displacement of cane sugar by HFCS.

Q16. In paragraph 17 of the written version of its oral statement dated 3 December, the European Communities stated that "the Panel may take into account that at the time [the] Mexican measure was imposed, a certain percentage of soft drinks produced in Mexico were equally sweetened with HFCS, and thus affected by the higher taxation." Could Parties please share with the Panel any comments they may have on this assertion and what consequences, if any, should this fact have for the Panel's analysis.

35. At the time the IEPS was imposed on soft drinks and syrups, some Mexican soft drink bottlers, as recounted in the U.S. submission, were beginning to use blends of HFCS and cane sugar to sweeten their soft drinks.[27] By 2001, the year prior to imposition of the IEPS on soft drinks and syrups, nutritive sweetener consumption by the soft drink industry was 30 percent HFCS and 70 percent cane sugar.[28] The use of blends of HFCS and cane sugar by the Mexican soft drink industry demonstrates that HFCS and cane sugar as sweeteners for soft drinks and syrups are interchangeable and, prior to the tax, competed head-to-head in the Mexican market.

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[26] *See* Exhibit US-4A and US-4B (IEPS, Dec. 31, 2003), Arts 1, 2 and 8..
[27] U.S. First Written Submission, para 34.
[28] U.S. First Written Submission, para. 23 and Exh. US-8.

It likewise demonstrates that soft drinks and syrups sweetened with HFCS and soft drinks and syrups sweetened with cane sugar were also competing in the Mexican market prior to imposition of the IEPS on soft drinks and syrups. Nevertheless, at the time Mexico imposed its tax, cane sugar remained the dominant sweetener for Mexican soft drinks and syrups as compared to U.S. soft drinks and syrups which were sweetened with HFCS.

36. The United States does not otherwise see the relevance of the EC's statement. In this regard, we note that the fact that some domestic producers may be affected by a measure does not excuse a breach of Article III. In the *Chile – Alcoholic Beverages* report, the Appellate Body found that, although domestic products comprised the majority of sales subject to the highest tax rate, that tax rate as applied to imported products nonetheless constituted a breach of Article III:2, second sentence. "The relative proportion of domestic versus imported products within a particular fiscal category is not, in and of itself, decisive of the appropriate characterization of the total impact of the New Chilean System under Article III:2, second sentence, of the GATT 1994."[29]

Q17. China expressed in its oral statement of 3 December that "when the tax law says that it is applicable to a product… the scope of taxation will not extend to the components of the taxed product." Do Parties have any comment on this assertion?

37. The United States does not agree with China's assertion. As stated in response to Question 15, the IEPS is both a tax on soft drinks and syrups and a tax on non-cane sugar sweeteners such as HFCS.

38. In any event, Article III:2 of the GATT 1994 covers taxes applied, "directly or indirectly", to imported products. China's reliance on the Ad Note to GATT Article III:2 is misplaced. The Ad Note clarifies the types of products covered by the second sentence as compared to the first sentence of GATT Article III:2 (*i.e.*, that the first sentence covers "like" products while the second covers "directly competitive or substitutable" products). It does not undo the fact that Article III:2 disciplines taxes applied, directly or indirectly, to a product. Thus, as a legal matter, the United States does not agree with China's interpretation of Article III:2 as stated in its oral statement.

Q18. Could the Parties please inform the Panel whether they agree that imported soft drinks and sweetened syrups are "alike" to Mexican domestic soft drinks and sweetened syrups. Do the Parties consider that imported soft drinks and sweetened syrups are "directly competitive or substitutable" with Mexican domestic soft drinks and sweetened syrups.

[29] Appellate Body Report, *Chile – Taxes on Alcoholic Beverages*, WT/DS87/AB/R, WT/DS110/AB/R, adopted 12 January 2000, para. 67.

39. The United States first submission, at paragraphs 63 through 83, explains that imported soft drinks and syrups sweetened with HFCS are like products relative to Mexican domestic soft drinks and syrups sweetened with cane sugar. Paragraphs 141-145 of the same submission argue in the alternative that these two groups of products are directly competitive or substitutable.

Q19. Could the Parties please also inform the Panel whether they agree that High-Fructose Corn Syrup (HFCS) is "alike" to cane sugar, for the purpose of Article III:4.

40. HFCS is "like" cane sugar for purposes of Article III:4 as discussed in paragraphs 156-58 of the U.S. first submission. Paragraphs 103-105 of the same submission note that in a 1998 antidumping determination on HFCS imports from the United States, the Mexican government determined that cane sugar and HFCS are "like" products for the purposes of Mexico's antidumping law and Article 2.6 of the Antidumping Agreement

Q20. China expressed in its oral statement of 3 December its opinion that the question of "whether the conclusion that cane sugar and HFCS are 'like products' under Article III:4 [cannot] be exclusively established by referring to the analysis on 'directly competitive and substitutable product' in the meaning of Article III:2 second sentence." Do Parties have any comment on this assertion?

41. The analysis presented in the U.S. First Written Submission that HFCS is "like" cane sugar for purposes of Article III:4 is supported by more than a reference to its analyses of why HFCS and cane sugar are directly competitive or substitutable for purposes of Article III:2, second sentence. The United States refers the panel to its first submission at paragraphs 156-58.

Q21. If the tax measures imposed by Mexico have any effect on High-Fructose Corn Syrup (HFCS), in the view of the Parties, should they be more properly examined in this regard – with respect to their effect on HFCS – under Article III:2 or under Article III:4 of the GATT 1994?

42. The IEPS as a tax on HFCS may properly be examined under both Article III:2 and III:4 of the GATT 1994.

43. Article III:2 prohibits dissimilar taxation of imported and domestic products. Article III:4 prohibits less favorable treatment of imported products as compared to domestic products with respect to laws affecting their internal sale, use, etc. Thus, to the extent the less favorable treatment of the imported product takes the form of dissimilar taxation that affects its internal sale, use, etc., the measure at issue may constitute a breach of both Articles III:2 and III:4 of the GATT 1994.

44. In the context of this dispute, the measure at issue is the IEPS. The IEPS imposes a tax on HFCS for use in soft drinks and syrups; cane sugar for use in soft drinks and syrups is exempt

from the tax. As a result, the IEPS applies a tax on HFCS that is not similarly applied to cane sugar within the meaning of Article III:2. Through this dissimilar taxation (a 400 percent tax on HFCS and no tax on cane sugar), the IEPS also affects the internal sale and use of HFCS and affords it less favorable treatment than cane sugar within the meaning of Article III:4. With respect to the bookkeeping and reporting requirements imposed by the IEPS, these requirements are not in themselves a tax and, therefore, are appropriately viewed as requirements affecting the internal use of HFCS within the meaning of Article III:4.

45. Articles III:2 and III:4 also overlap in the imported and domestic products to which they apply. The first sentence of Article III:2 addresses "like" products while the second sentence of Article III:2 addresses "directly competitive or substitutable" products. Article III:4 addresses "like" products. While the analysis of whether an imported and domestic product are "like" or "directly competitive or substitutable" under Article III:2 is not identical to the analysis of whether the products are "like" under Article III:4, there is nothing in the text of either Article that prevents "like" products within the meaning of Article III:4 from also being "like" or "directly competitive or substitutable products" within the meaning of Article III:2 or vice versa.

46. In the context of this dispute, HFCS and cane sugar are both "like" products within the meaning of Article III:4[30] and "like" and "directly competitive or substitutable" products within the meaning of Article III:2.[31]

47. In *Indonesia – Autos*, for example, the complaining parties argued that a local content requirement required to obtain a lower tax rate constituted a breach of Indonesia's obligations under Article 2 of the Agreement on Trade-Related Investment Measures ("TRIMS") and Articles III:2 and III:4 of the GATT 1994. Article 2 of TRIMS read in conjunction with its annex prohibits local content requirements that are inconsistent with Article III:4 of the GATT. The panel first examined whether the local content requirement was a breach of Article 2 of TRIMS and, specifically, whether the local content requirement was "inconsistent with the obligation of national treatment provided for in paragraph 4 of Article III of the GATT 1994." Having found the local content requirement a breach of Article 2 of TRIMS, the panel exercised judicial economy with respect to the separate Article III:4 claim. The panel then examined whether taxing imported cars at a higher rate because they lacked a certain percentage of local content was a breach of Article III:2, first sentence. The panel found in the affirmative. Thus, in *Indonesia – Autos*, the panel found it proper to examine the same local content requirement under both Article 2 of TRIMS (which includes examination of the measure's consistency with GATT Article III:4) and under Article III:2 of the GATT.[32]

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[30] U.S. First Written Submission, paras. 156-158.

[31] U.S. First Written Submission, paras. 94-130.

[32] *See* Panel Report, *Indonesia – Certain Measures Affecting the Automobile Industry,* WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R, adopted on 23 July 1998, paras. 14.83-14.117.

Q22. Could the Parties please comment whether, in their opinion, the bookkeeping and reporting requirements identified by the United States inter alia in paragraph 4.(2) of its first submission should be considered as separate measures from the tax on soft drinks and the distribution tax. In the opinion of the Parties, should the Panel make a separate determination on the consistency of those bookkeeping and reporting requirements with the provisions of the GATT 1994, even if it found that the tax on soft drinks and the distribution tax were inconsistent with the GATT 1994?

48. The United States considers the bookkeeping and reporting requirements, the HFCS soft drink tax, and the distribution tax to be separate measures, even though they share the common context of the IEPS and its application to soft drinks and syrups. The Panel should make findings on the consistency of each of these measures with Mexico's obligations under the GATT 1994. With respect to the bookkeeping and reporting requirements, the United States notes that imposition of these requirements on soft drinks and syrups sweetened with HFCS (or other non-cane sugar sweeteners) but not on soft drinks and syrups sweetened only with cane sugar affords imported HFCS less favorable treatment than Mexican cane sugar.[33] Regardless of whether Mexico continued to tax HFCS sweetened soft drinks and syrups dissimilarly from, or in excess of, cane sugar sweetened soft drinks and syrups, imposition of bookkeeping and reporting requirements with respect to HFCS-sweetened soft drinks and syrups (for example a requirement to report a bottler's top 50 customers) that are not also applied to cane sugar-sweetened soft drinks and syrups would continue to disadvantage the use of HFCS as compared to cane sugar as a sweetener for soft drinks in Mexico. A complete resolution of this dispute therefore requires separate findings, rulings and recommendations with respect to the bookkeeping and reporting requirements.

49. The United States draws attention to the Appellate Body's discussion of judicial economy in *Australia – Salmon*. There the Appellate Body found the panel in error for not making findings with respect to certain kinds of salmon. The Appellate Body explained that to make findings with respect to only one kind of salmon would leave the DSB unable to make sufficiently precise recommendations and rulings so as to allow for compliance by the defending party with is WTO obligations.[34]

Q23. Could the Parties please comment whether, in their opinion, the bookkeeping and reporting requirements identified by the United States, inter alia in paragraph 4.(2) of its first submission, should be considered as internal measures which affect the internal use of High-Fructose Corn Syrup (HFCS).

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[33] U.S. First Written Submission, paras. 159-161.

[34] Appellate Body Report, *Australia – Salmon*, paras. 223-226.

50. The bookkeeping and reporting requirements are internal measures which affect the internal sale and use of HFCS. Specifically, the bookkeeping and reporting requirements are imposed pursuant to a Mexican law, the IEPS. The IEPS taxes the internal transfer of soft drinks and syrups sweetened with HFCS or other non-cane sugar sweeteners. The IEPS requires individuals and entities subject to the IEPS (*i.e.*, those transferring soft drinks and syrups sweetened with HFCS or other non-cane sugar sweeteners) to follow certain bookkeeping and reporting requirements. Soft drinks and syrups sweetened with cane sugar are exempt from the IEPS and, therefore, also exempt from the bookkeeping and reporting requirements.

51. These bookkeeping and reporting requirements include the requirements, for example, to provide an annual listing of the goods "produced, transferred or imported in the previous year, as regards consumption by state and the corresponding tax, as well as the services provided by establishment in each state" and to report quarterly "information regarding [the taxpayer's] 50 main clients and suppliers."[35] Compliance with these requirements demand both the time and expense of doing so in addition to the risk that business sensitive information, such as a producer's top clients and suppliers, may not be adequately safeguarded. Accordingly, the bookkeeping and reporting requirements impose a burden on the use of HFCS that is not also applied to cane sugar.

52. As prior panels have explained, the word "affecting" in Article III:4 of the GATT has been interpreted to cover not only laws and regulations which directly govern the conditions of sale or purchase but also any laws or regulations which might adversely modify the conditions of competition between domestic and imported products.[36] Imposing a burden on the use of HFCS that is not also imposed on the use of cane sugar (or, said another way, granting an advantage to the use of cane sugar that is not also granted to HFCS) has an impact on the conditions of competition between cane sugar and imported HFCS and, thus, affects the use of HFCS in Mexican soft drink and syrup production.[37] The Appellate Body has previously found a tax exemption granted conditional on use of domestic content to be a law affecting the internal use of an imported product.[38]

Q24. In paragraph 6 of the written version of its oral statement dated 3 December, Guatemala stated that "the Panel should respond to Mexico's request and consider, in its deliberations, the importance that the sugar activity has in Mexico and the implications for the country of the reforms undertaken in this sector". Could

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[35] U.S. First Written Submission, para. 46.

[36] *See, e.g.,* GATT Panel Report, *Italian Discrimination Against Imported Agricultural Machinery*, L/833, adopted 23 October 1958, BISD 7S/60, para. 12; Panel Report, *Canada – Certain Measures Affecting the Automotive Industry*, WT/DS139/R, WT/DS142/R, adopted 19 June 2000, para. 10.80; *see also* U.S. First Written Submission, para. 159.

[37] *See* U.S. First Written Submission, para. 160.

[38] Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/AB/RW, adopted 29 January 2002, paras. 212-213.

Parties share any views they may have regarding Guatemala's statement and, particularly, in what manner, if any, should the Panel consider it in its deliberations the factors highlighted by Guatemala.

53. The United States does not consider that the importance of the sugar industry in Mexico is relevant to whether Mexico's discriminatory tax on HFCS soft drinks and syrups sweetened with HFCS is consistent with its obligations under Articles III:2 and III:4 of the GATT nor to whether Mexico's discriminatory tax is justified under Article XX(d). The United States also considers its domestic HFCS industry and its ability to export to Mexico important. The importance of a domestic industry does not justify discriminating against like and directly competitive or substitutable imported products. Indeed, if the suggested approach is to excuse discrimination based on the importance of a domestic industry, then such an approach would have the perverse result that the larger the adverse trade impact of the discrimination, the more easily a Member could discriminate.

Q25. Could the Parties please confirm whether they consider that Article XX(d) of the GATT 1994 would justify measures adopted by one Member which are "necessary to secure compliance" by another Member with international obligations arising from a treaty which is not part of the WTO "covered agreements". Are there any WTO or GATT precedents which could be relevant for this question?

54. Article XX(d) of the GATT does not justify measures adopted by one Member to secure compliance by another Member with international obligations arising from a treaty which is not part of the WTO "covered agreements."

55. The United States is not aware of any prior GATT or WTO panel or Appellate Body reports addressing whether Article XX(d) of the GATT justifies measures adopted by one Member to secure compliance by another Member with international obligations arising from a treaty which not part of the WTO "covered agreements." The United States notes that in all prior reports where a Contracting Party or WTO Member has asserted an Article XX(d) defense, the "law or regulation" with which compliance was sought has universally been an internal law or regulation of the defending party.

Q26. Do Parties consider that the manner in which the US - Shrimp case was resolved in the WTO, and particularly the manner in which efforts at international cooperation were taken into account in the analysis of the defence under Article XX of the GATT, is relevant for the present case?

56. The issue of international cooperation that arose in *US – Shrimp* is not relevant to Mexico's Article XX(d) defense.

57. Contrary to Mexico's contention, the Appellate Body's discussion of efforts at international cooperation in *US – Shrimp* are not supportive of Mexico's defense under Article

XX(d). In *US – Shrimp*, the Appellate Body considered efforts at international cooperation in the context of the chapeau to Article XX, specifically whether the United States import ban on shrimp – which the Appellate Body had already found to be "relating to the conservation of exhaustible natural resources" under subparagraph (g) with respect to sea turtles – was, nonetheless, "applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail." In answering the question, the Appellate Body in its original report concluded that the U.S. import ban was applied in an manner resulting in arbitrary and unjustifiable discrimination *inter alia* because, prior to imposing its ban, the United States had engaged in negotiations with some exporting countries, but had not engaged in negotiations on a solution to the protection of sea turtles with each country affected by the import ban and, in particular, with the complaining parties in the dispute. The Appellate Body considered it arbitrary and unjustifiable to negotiate with only some countries but to impose the ban on all of them.[39]

58. This is not the situation in the present case. First, the Appellate Body's discussion of international negotiations in *US – Shrimp* concerned the chapeau to Article XX, specifically the application of a measure and the words "arbitrary or unjustifiable discrimination." Prior to examining the chapeau, however, the Appellate Body had already found the U.S. ban to be "relating to the conservation of" sea turtles and, therefore, to have met the requirements of subparagraph (g). In the present dispute, Mexico cannot show that its tax measures meet the requirements of any of the subparagraphs of Article XX. Therefore, the question of whether Mexico's tax measures are applied in a manner that is "arbitrary or unjustifiable" under the chapeau is simply not relevant. Mexico has not demonstrated that its tax measures are "necessary to secure compliance with laws or regulations" within the meaning of paragraph (d). Further, there is no issue here of Mexico's having attempted to negotiate with some countries but not others before imposing its tax measures. For that reason as well, *US - Shrimp* is not relevant.

For the United States

Q27. Could the United States please clarify whether, in its opinion, the measures at issue are inconsistent with Article III "on their face" (de jure) or "as applied " (de facto).

59. The IEPS is inconsistent with GATT Article III because it discriminates against imported HFCS and soft drinks and syrups made with HFCS. The IEPS discriminates against HFCS and soft drinks and syrups made with HFCS both on its face (*de jure*) and in fact (*de facto*).[40]

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[39] Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/RW, adopted 21 November 2001, paras. 122-123 (summarizing its early findings), 128.

[40] The United States would respectfully suggest that "in fact" is a better term to use for "*de facto*" than "as applied" since to the uninformed reader, "as applied" could be confused with the challenge to a measure "as such" versus "as applied." For example, a measure could breach an obligation *de facto* without having ever been applied

60. First as a tax on soft drinks and syrups, the IEPS discriminates *de jure* and *de facto* against soft drinks and syrups imported from the United States. The IEPS discriminates *de jure* against imported soft drinks and syrups by allowing a tax exemption for certain Mexican produced soft drinks and syrups – those sweetened only with cane sugar – but denying that same exemption to the importation of soft drinks and syrups sweetened with HFCS or any other sweetener, including cane sugar.

61. The IEPS discriminates *de facto* against imported soft drinks and syrups by taxing the internal sale and distribution of soft drinks and syrups sweetened with HFCS, but not the internal sale and distribution of soft drinks and syrups sweetened only with cane sugar. As detailed in the U.S. first submission, soft drinks and syrups sweetened with HFCS and soft drinks and syrups sweetened with cane sugar are "like products."[41] As also detailed in the U.S. first submission, most soft drinks and syrups produced in the United States are sweetened with HFCS, while cane sugar is the dominant sweetener in Mexican produced soft drinks and syrups.[42] Consequently, by taxing the internal sale and distribution of soft drinks and syrups sweetened with HFCS, the IEPS taxes soft drinks and syrups imported from the United States. At the same time, the IEPS exempts from the tax the type of soft drinks and syrups produced most widely in Mexico – those sweetened with cane sugar. In this manner, the IEPS constitutes *de facto* discrimination against soft drinks and syrups imported from the United States and sweetened with HFCS.

62. Second, as a tax on HFCS for use in soft drinks and syrups, the IEPS discriminated *de facto* against imported HFCS. As explained in the U.S. first submission, cane sugar is by far the dominant sweetener in Mexico comprising between 90 and 95 percent of Mexican sweetener production prior to imposition of the IEPS.[43] HFCS on the other hand dominates sweetener imports comprising over 99 percent of sweetener imports prior to imposition of the IEPS.[44] Accordingly, by taxing the internal transfer and distribution of soft drinks and syrups sweetened with HFCS but not those sweetened only with cane sugar, the IEPS *de facto* aims at the imported sweetener, HFCS, while excluding from taxation the domestic sweetener, Mexican cane sugar. The IEPS bookkeeping and reporting requirements similarly discriminate *de facto* against imported HFCS.

Q28. Could the United States please clarify the units in which the different figures contained in its Exhibit US-8, part of its first submission, are provided.

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because its design, structure or architecture are such as to demonstrate the discrimination by origin even though the measure on its face does not specify origin as a criterion.

[41] U.S. First Written Submission, paras 64-83.

[42] U.S. First Written Submission, paras. 30-34, 86.

[43] U.S. First Written Submission, paras 24, 137.

[44] U.S. First Written Submission, para. 25, 137.

63. As contained in Exhibit US-8, all consumption figures are in metric tons unless otherwise indicated; the first set of GDP figures are in pesos; the second set of GDP figures are in U.S. dollars; per capita GDP figures are in U.S. dollars. HFCS figures are provided on a "dry basis."

64. For ease of reference, the United States has attached Exhibit US-57. Exhibit US-57 is the same as Exhibit US-8 except with the addition of units for each set of figures provided therein.

Q29. Could the United States please confirm whether, in its opinion, the challenged tax measures are applied by Mexico "so as to afford protection" to its domestic production of soft drinks and syrups? If so, how are those tax measures applied so as to afford protection to domestic production of soft drinks and syrups? Or are they instead, or additionally, applied by Mexico so as to afford protection to its domestic production of cane sugar?

65. The IEPS is applied by Mexico "so as to afford protection" to domestic production of soft drinks and syrups as well as "so as to afford protection" to domestic production of cane sugar.

66. As the Appellate Body has related on more than one occasion:

> an examination in any case of whether dissimilar taxation has been applied so as to afford protection requires a comprehensive and objective *analysis of the structure and application* of the measure in question on domestic as compared to imported products. We believe it is possible to examine objectively the underlying criteria used in a particular tax measure, its structure, and its overall application to ascertain whether it is applied in a way that affords protection to domestic products. [45]

67. With respect to soft drinks and syrups, the IEPS is structured and applied such that imported soft drinks and syrups are subject to a 20 percent tax,[46] while soft drinks and syrups sweetened with cane sugar and produced in Mexico are exempt from that tax.[47] A 20 percent tax that applies to imported soft drinks and syrups but not to domestic soft drinks and syrups clearly disadvantages imports in favor of domestic production and, thus, affords protection to domestic production.

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[45] Appellate Body Report, *Japan – Taxes on Alcoholic Beverages* (*Japan – Alcoholic Beverages II*), WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, p. 31; *see also* Appellate Body Report, *Chile – Taxes on Alcoholic Beverages* (*Chile – Alcoholic Beverages*), WT/DS87/AB/R, WT/DS110/AB/R, adopted 12 January 2000, para. 61.

[46] *See supra* U.S. Response to Question 27 (discussing how the IEPS *de jure* and *de facto* discriminates against imported soft drinks and syrups).

[47] U.S. First Written Submission, paras. 149-52.

68. With respect to HFCS, the IEPS is structured and applied such that the imported sweetener HFCS is subject to a 400 percent tax on its use in soft drinks and syrups while the domestic sweetener cane sugar is exempt from that tax.[48] A 400 percent tax that applies to the imported sweetener HFCS but not to the domestic sweetener cane sugar clearly disadvantages HFCS – in fact, effectively prohibits its use – in favor of domestic production of cane sugar and, thus, affords protection to domestic production of cane sugar.[49]

69. As concerns HFCS, the protectionist structure of the IEPS is confirmed by a series of legislative statements and judicial interpretations that the purpose of the IEPS is to protect the Mexican cane sugar industry.[50] The stated purpose of the IEPS to protect the Mexican cane sugar industry does not, however, detract from the fact that the IEPS is also structured and applied so as to discriminate against imported soft drinks and syrups and afford protection to domestic production of soft drinks and syrups.

70. As the first U.S. submission has discussed, the tax on soft drinks and syrups that are not exclusively sweetened with cane sugar has as an object to afford protection to domestic production of cane sugar. However, because Mexico essentially requires its domestic soft drink and syrup producers to use high-priced Mexican sugar, the tax necessarily must also protect these downstream producers against imports of competing soft drinks and syrups sweetened with lower-cost sweeteners such as HFCS.

Q30. The Panel has noted that in paragraph 8 of the written version of its oral statement dated 2 December, the United States has stated that "NAFTA is not a 'law or regulation,' and Mexico's tax is not 'necessary to secure compliance.'" Could the United States please elaborate on those two assertions. In particular, why does the United States consider that Mexico's taxes may not be considered "necessary" to secure compliance?

71. The U.S. statement that "NAFTA is not a 'law or regulation'" was made in the context of rebutting Mexico's contention that a breach of its Article III obligations was necessary to secure compliance with obligations Mexico has unilaterally and erroneously determined that the United States has breached under the NAFTA, without any finding by a NAFTA panel to that effect. As the United States explained in its oral statement, however, international obligations owed Mexico by other countries under the NAFTA and other international agreements are not "laws" or "regulations" within the meaning of Article XX(d).[51] As contained in Article XX(d), "laws or regulations" means the laws and regulations of a state, not an international agreement or obligations assumed thereunder.

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[48] U.S. First Written Submission, paras. 45, 131.
[49] U.S. First Written Submission, paras. 134-138.
[50] U.S. First Written Submission, para. 139.
[51] U.S. First Oral Statement, para. 9.

This interpretation of "laws or regulations" is based on the ordinary meaning of those words. Black's Law Dictionary defines the word "laws":

> *Rules promulgated by government* as a means to an ordered society. Strictly speaking, session laws or statutes and not decisions of court; though in common usage refers to both *legislative and court made law*, as well as to administrative rules, regulations and ordinances.[52]

It defines the word "regulations":

> Such are *issued by various governmental departments* to carry out the intent of the law. Agencies issue regulations to guide the activity of those regulated by the agency and of their own employees to ensure uniform application of the law.[53]

In contrast, Black's Law Dictionary defines "international agreement":

> Treaties and other agreements of a contractual character between different countries or organizations of states (foreign) creating legal rights and obligations.[54]

Thus, the ordinary meaning of "laws" and "regulations" is that these are rules (e.g, in the form of a statute) issued by a government and not obligations under an international agreement.

72. This interpretation is supported by the context in which "laws or regulations" appear – namely, Article XX of the GATT and more broadly the GATT and the WTO Agreement as a whole. In particular, Article XX itself distinguishes between "laws" and "regulations" on the one hand and "obligations" under an international agreement on the other. Thus, while Article XX(d) provides a defense for measures necessary to secure compliance with "laws or regulations," Article XX(h) provides a defense for measures "undertaken in pursuance of obligations under any intergovernmental commodity agreement." There would be no reason for the different phrasing had the drafters intended "law or regulations" to mean the same thing as "obligations under" an international agreement.

73. Other provisions of the GATT support the distinction between "laws" and "regulations" on the one hand and "agreements" and "obligations" on the other. For example, Article X:1

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[52] *Black's Law Dictionary* 887 (1990) (emphasis added).
[53] *Black's Law Dictionary* 1286 (1990) (emphasis added).
[54] *Black's Law Dictionary* 816 (1990).

makes a distinction between "laws, regulations, judicial decisions and administrative rulings" and "agreements affecting international trade policy between government[s]" Article X:1 states:

> *Laws, regulations, judicial decisions and administrative rulings* of general application, made effective by any contracting party, pertaining to the classification or the valuation of products for customs purposes, or to rates of duty, taxes or other charges, or to requirements, restrictions or prohibitions on imports or exports or on the transfer of payments therefor, or affecting their sale, distribution, transportation, insurance, warehousing inspection, exhibition, processing, mixing or other use, shall be published promptly in such a manner as to enable governments and traders to become acquainted with them. *Agreements affecting international trade policy which are in force between the government or a governmental agency of any contracting party and the government or governmental agency of any other contracting party* shall also be published.[55]

Article III of the GATT distinguishes an "internal tax" from a "trade agreement" and "obligation" thereunder. Article III:3 states:

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

74. Further,"obligations under this Agreement" appears throughout the GATT – itself an international agreement.[56] Not once does the GATT reference "*laws* under this Agreement." In addition, Article XXI:(c) references "obligations under the United Nations Charter"; it similarly does not reference "laws" under the Charter. This phrasing is, of course, in recognition of the fact that commitments under an international agreement are "obligations" not "laws."

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[55] GATT Art. X:1 (emphasis added).

[56] *See, e.g.,* GATT Arts. XII:4(d), XV:6, XVIII:12, XVIII:16, XVIII:18, XVIII:21, XVIII:22, XIX:1 and XXIII.

75. With respect to the fact that Mexico's tax measures are not "necessary to secure compliance," the United States points out that the Panel need not even reach the issue. Because U.S. obligations under the NAFTA are not "laws or regulations," Mexico's tax measures cannot be "necessary to secure compliance with laws or regulations."

76. In any event, Mexico's tax measures are not "necessary to secure compliance" with U.S. NAFTA obligations. In the first instance, Mexico's contention is based on its own determination that United States is not already in compliance with those obligations. As Mexico even admits, however, there is a genuine disagreement between Mexico and the United States over the market access commitments undertaken by both side during the NAFTA negotiations. Mexico's tax measure, therefore, cannot be necessary to secure compliance with U.S. NAFTA obligations when it even admits there are different understanding regarding what those obligations are.

77. Moreover, negotiations between the United States and Mexico, as well as private sector interests, concerning the bilateral sweeteners trade under the NAFTA have been on-going. In fact, during the consultation phase of this dispute, Mexico acknowledged these discussions and expressed its belief that requesting a WTO panel was premature given these ongoing discussions.[57] It is difficult to understand how Mexico's tax measures are a response to the failure of these discussions, and therefore in Mexico's eyes "necessary", when the discussions continued well after enactment of Mexico's tax measures even through the consultation phase of this dispute.

78. In addition, as the Appellate Body stated in *Korea – Beef ,* whether a measure is "necessary" involves the extent to which the measure contributes to the enforcement of the law or regulation at issue, the measure's impact on trade and the importance of the law or regulation to be enforced.[58] While Mexico apparently attributes a great deal of importance to a viable cane sugar industry and its ability to export, the United States has difficulty understanding how a breach of Mexico's WTO obligations contributes to these goals. As reviewed in our first written submission, this breach has had a devastating impact on U.S. HFCS exports to Mexico. It has not, however, solved any of Mexico's or the U.S. concerns under the NAFTA and, in fact, has only contributed to the tensions on both sides.

79. Moreover, Mexico's tax measures apply not just to imports from the United States, but imports from any country. Again, the United States finds it difficult to understand how, in seeking to enforce the alleged obligations of the United States under the NAFTA, it is necessary to breach the national treatment obligations Mexico has undertaken with respect to every other WTO Member.

[57] *See Dispute Settlement Body: Minutes of the Meeting Held on 22 June 2004*, WT/DSB/M/171, para. 26.

[58] Appellate Body Report in *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS 161/AB/R, WT/DS169/AB/R, adopted on 10 January 2001, paras. 163-64.

80. Furthermore, no matter what Mexico's complaint might be, Mexico could have sought NAFTA compliance through any number of means – diplomatic or otherwise – short of breaching its WTO obligations.

Q31. Could the United States please comment on Mexico's assertion that the list of laws and regulations in paragraph (d) of Article XX is illustrative and not exhaustive. What conclusion, if any, should be drawn from this fact?

81. The United States agrees that the laws and regulations listed in Article XX(d) is illustrative and not exhaustive. Specifically, the laws and regulations listed in Article XX(d) are introduced by the word "including" indicating that what follows is not an exhaustive list but rather examples of what comprise "laws or regulations."

82. However, any additional items to those illustrated in the list would still need to be "laws and regulations." As explained above, this would exclude obligations under international agreements. The mere fact that the listing is illustrative cannot be construed to mean that "laws and regulations" as used in Article XX(d) also encompass obligations of another WTO Member under an international agreement.

Q32. Could the United States please comment on Mexico's assertion that its tax measures are necessary to secure compliance by the United States with international obligations arising under the North American Free Trade Agreement.

83. The United States refers to the Panel to its response to Question 30.

Q33. Assuming that the tax measures applied by Mexico were to be examined under Article XX(d) of the GATT, could the United States suggest whether in its opinion there are alternative measures which would be reasonably available to Mexico and which would achieve the same objective.

84. Mexico could have sought to achieve its bilateral trade objectives with the United States through any of the diplomatic means customarily employed in trade negotiations; it did not have to breach its multilateral trade obligations to the United States.

For Mexico

Q37. The Panel has noted that in paragraph 38 of the written version of its oral statement, Mexico has stated that the WTO case on Argentina - Poultry differs from the present case in several important aspects and that it may not be used as a precedent. Could Mexico please explain, in its opinion, in what ways do the two cases differ and why should the Argentina - Poultry case not be relevant as a precedent.

85. *Argentina – Poultry* is an example of a dispute in which the responding party asked the panel to refrain from making findings on the issues in the dispute due to dispute settlement proceedings under a non-WTO agreement. The panel rejected Argentina's request. The panel explained that proceedings under a non-WTO tribunal (MERCUSOR) did not impose obligations on a WTO panel to find in a particular way and that Argentina's request had "no basis in Article 3.2 of the DSU, or any other provision."[59]

86. The Panel may find the panel's findings in *Argentina – Poultry* as useful guidance in this dispute because it presents a similar situation to what Mexico argues in this dispute. In both disputes the responding party argues that dispute settlement proceedings before a non-WTO tribunal (whether those that have already occurred or may occur sometime in the future) justify the panel from declining to make findings on claims within the panel's terms of reference. The panel in *Argentina – Poultry* rejected the responding party's contention, as should the Panel in this dispute.

Q42. Could Mexico provide figures on the Mexican market of sweeteners for the production of soft drinks and sweetened syrups for the most recent ten years of available information. In particular, could Mexico provide information on: (a) yearly Mexican production of High-Fructose Corn Syrup (HFCS), of cane sugar and of other sweeteners, in value and kilograms; (b) yearly Mexican consumption of HFCS, of cane sugar and of other sweeteners, in value and kilograms, by the Mexican producers of soft drinks and sweetened syrups; (c) yearly Mexican exports, if any, of HFCS, of cane sugar and of other sweeteners Could Mexico please provide figures on the Mexican market for soft drinks and on the Mexican market for sweetened syrups; and, (d) yearly Mexican imports (by origin), if any, of HFCS, of cane sugar and of other sweeteners for the production of soft drinks and sweetened syrups.

87. As an initial comment, the United States notes that the data presented in the U.S. first submission more than adequately satisfies the U.S. burden to establish a *prima facie* case on its Article III claims. That data comes from a variety of official sources including from the Mexican Government itself. Mexico has not contested this data, and it should therefore be taken as a given for purposes of this dispute.

88. The United States notes, however, that the information requested of Mexico regarding the Mexican sweeteners market appears in the U.S. first submission as follows:

[59] Panel Report, *Argentina - Definitive Anti-Dumping Duties on Poultry from Brazil* (*Argentina – Poultry*), WT/DS241/R, adopted 19 May 2003Panel Report, para. 7.41.

(a) yearly Mexican production of HFCS in metric tons: U.S. First Written Submission, para. 24 (company data) and footnote 38 (FAS data); Exhibit US-11A through 11E (FAS data);

(b) yearly Mexican production of cane sugar in metric tons: Exhibit US-11A through 11E (FAS data); Exhibit US-15 (FAS data);

(c) yearly Mexican consumption of HFCS by Mexican producers of soft drinks and syrups: Exhibit US-8 and Exhibit US-57 (attached as revised Exhibit-8) (ERS data);

(d) yearly Mexican consumption of cane sugar by Mexican producers of soft drinks and syrups: Exhibit US-8 and Exhibit US-57 (attached as revised Exhibit-8) (ERS data);

(d) yearly Mexican exports of HFCS: Exhibit US-11A through 11E (Mexico Secretary of Economy data);

(e) yearly Mexican exports of cane sugar: Exhibit US-11A through 11E (Mexico Secretary of Economy data);

(f) yearly Mexican imports of HFCS: Exhibit US-10 (from the US) (Mexico Secretary of Economy data); Exhibit US-11A through US-11E (by country) (Mexico Secretary of Economy data); and

(f) yearly Mexican imports of cane sugar: Exhibit US-15 (from US and world) (Mexico Secretary of Economy data); Exhibit US-11A through US-11E (by country) (Mexico Secretary of Economy data).

89. Additionally, information on Mexican soft drink and syrup imports appears in the U.S. first submission at Exhibit US-13. Information on Mexican soft drink and syrup production and consumption can be found in the U.S. first submission *inter alia* at paragraphs 28 and 30, Exhibit US-16, Exhibit US-18, Exhibit US-19, Exhibit US-23 and Exhibit US-48.

Q43. Could Mexico identify the main producers of soft drinks and sweetened syrups in the Mexican market. Could it also clarify whether, for each producer, the products are sweetened with High-Fructose Corn Syrup (HFCS), cane sugar or other sweeteners.

90. The main producers of soft drinks and syrups in the Mexican market are identified in the U.S. first submission at paragraph 31. Mexican soft drink and syrup producers using HFCS/cane sugar pre- and post-imposition of the IEPS are identified in the U.S. first submission at paragraphs 30 and 34. The use of HFCS verus cane sugar by Mexican soft drink and syrup producers is contained in Exhibit US-8 and Exhibit US-57 (attached to this response as revised Exhibit US-8).

TABLE OF EXHIBITS

Exhibit US-	Title of Exhibit
57	USDA ERS Model (revised to specify units)