Lesson 4 International Trade Law

Main Principles of the GATT: The National Treatment Principle and International taxation

National Treatment (Article III):

- Multilaterally negotiated **tariffs**' ceilings and the **prohibition of quantitative restriction**s are two powerful rules to implement a project of **liberalization of trade**.
  Why where they are not enough?
- States could easily undo the progress made in terms of liberalization of their markets adopting «**beyond the border measures**» (taxes and regulation)
- E.g.: the **same effects** on the price of imported products can be obtained through **a higher tariff rate** or imposing on them **heavier sale taxes or stricter technical specifications** as opposed to like domestic goods once they have cleared customs.
- GATT's scope had to be extended also on what States do within their borders in terms of taxation and regulation.
  How?
- **Instead of choosing to regulate internal policies** (WTO saying that t-shirt with less than 50% of cotton will not pass though countries border), in a way to avoid a negative impact on trade, **imposing positive standards** (with the risk to infringe on the sovereignty of its Members)
- **GATT founding fathers** chose a «softer approach»: they only **required** Members to commit themselves to a rule of **non-discrimination (negative integration).**
- **Behind the border measures are legal**, but they must be applied in a **non-discriminatory way**.
- ***GATT Article III National Treatment on Internal Taxation and Regulation***
  "The contracting parties recognize that **internal taxes and other internal charges and laws, regulations and requirements** affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products, and internal quantitative regulations requiring the mixture, processing or use of products in specified amounts or proportions**, should not be applied to imported or domestic products so as to afford protection to domestic production (SATAP principle has to be avoided).**"
- In other words, **imported products cannot be discriminated against domestic products.**Thanks to this rule the others we've seen (bound tariffs, ban on quantitative restriction) do not risk to become ineffective and Members are induced to engage seriously in trade negotiations.
- The **«not so as to afford protection (SATAP) provided for in Article III:1 is applied separately to: Tax Measures and Internal Regulations**
- **Difference between duties and taxes:**
  The obligation to pay a **custom duty** accrues (*matura*) at the moment
  and by virtue of importation.
  The obligation to pay a **tax** under Article III:2 relates to goods that have already been imported and is triggered by **an internal event** that takes place within the customs territory (like distribution, sale, use or transportation of the imported products)

- A further distinction is made in Article III:2, which sets out different requirements for the non –discriminatory taxation of:
  -Imported and «like domestic products» (first sentence of Article III:2);
  - Imported and «directly competitive or substitutable products» (second sentence of Article III:2)
- **GATT Article III**

The products of **the territory of any contracting party** imported into the territory of any other contracting party shall **NOT** be subject, directly, or indirectly, to internal taxes or other internal charges of any kind **IN EXCESS OF THOSE APPLIED**, **directly or indirectly, to similar (LIKE) domestic products**. Moreover, no contracting party shall otherwise apply internal taxes or other internal charges to imported or domestic products in a manner.
contrary to the principles set forth in paragraph 1.*
*A tax conforming to the requirements of the first sentence of paragraph 2 would be considered to be inconsistent with the provisions of the second sentence only in cases where competition was involved between, on the one hand, the **taxed product** and, on the other hand, a **directly competitive or substitutable product** which was not similarly taxed.
Notice that this article covers de iure and de facto discrimination.

- ***Japan-Taxes on alcoholic beverages (WT/DS8, 10, 11 – AB Rep. 1996)***
  Facts: *Canada, European Communities (EU) and United States (US) complain that the Japanese law on alcoholic beverages violates GATT Article III.*
  The law established a taxation system based on a double criterion:
  (a) belonging of the beverage to one of ten different categories (among which bier, wine, , "white spirits", liquor, sake, shochu);
  (b) Percentage of alcohol content.
  Under these two criteria, shochu was taxed less than vodka and whisky:

  - shochu (25°) 155 yen/liter
  - vodka (37°) 367 yen/liter
  - whisky (40°) 982 yen/liter

  Decision: *in its report* the Appellate Body confirmed the Panel decision. It found a violation of Article III.2 on the account that:
  - Vodka (mainly imported) and shochu (traditional japanese drink) **are like products**.
  - Vodka was **taxed in excess** in respect of shochu.
    de facto discrimination

  According to the AB only **for products which are not like but in competition on the market** ("*directly competitive or substitutable*") a "similar" **but not** "**identical**" **taxation is permit**ted, and only **when it is not aimed at protecting national production**. *That is why the similar taxation of shochu and whisky, brandy, rum, gin did not amount to a violation of Article III.2.*
  In *Japan-Taxes on alcoholic beverages* the Appellate Body has pointed out:
  1. the «**like product**» expression **in Article III:2 first sentence has to be construed narrowly**, on a case-by-case basis;
  2. **«Not …in excess of»** means that even the slightest difference in taxation would be too much: no differences are allowed

3. To give due meaning to **Article III:2 second sentence** «**directly competitive or substitutable products**» must be a broader group of products than «like products» identified by such matters as physical characteristics, tariff classification, **end-uses**, the latter being the **decisive criterion** (**elasticity of substitution).**
4. «**not similarly taxed**» means that an amount of excess taxation here is allowed
5. The reference to Article III:1 means that for DCS products to be taxed in a way that is forbidden by Article III, it has also to be proved that the tax is applied «**so as to afford protection**» to domestic products.

- **When are to products alike?** The following criteria is used:
  - Physical characteristics,
  - Consumer's habits and preferences,
  - **End uses.**
  - Tariff classification
- **To find out common end uses** (*elasticity of substitution*) is the center of the inquiry that Panels have to make because "**The aim of GATT Article III is to protect equal competitive opportunities between imports and domestic products**". Therefore to win a national treatment case the complainant doesn't have to prove that specific imports have been discriminated behind the border, but has only to point at discrimination as expressed in a statute or regulation
- **Chapter 9, pg.19:**Ver ppt grupo diciembre 1. Atención!: Pequeño error en respuesta de pregunta 1.
- **Patrias's Luxury producto**
- Patria is a developing country with a population of 1 billion people, many of whom live in rural areas. In recent years, Patria managed to achieve spectacular economic growth, largely driven by exports of low-tech consumer goods. With a growing middle class, Patria's imports have also increased significantly and Patrian firms, who mainly produce low price/low quality products, are increasingly subject to foreign competition. At the same time, Patria's economic growth has increased the gap between rich and poor people in Patria. To deal with these and other concerns, Patria's Parliament changed Patria's tax code to impose a "luxury tax" of 10 percent ad valorem on all products sold in Patria, be they imported or domestically produced, above 5,000 Patrian Pesos (PP) (the equivalent of US$2,000). For imports, this tax is levied at the border by Patria's customs authorities. For domestic products, it is levied at the time of production. When the new law was enacted, one Member of Parliament stated that "the goal of this new tax is to redistribute the gains of trade more fairly among Patria citizens." Another member of Parliament, Copyright © 2009. Aspen Publishers. All rights reserved. May not be reproduced in any form without permission from the publisher, except fair uses permitted under U.S. or applicable copyright law. heading the "Patria for Patrians" coalition, explained the tax as follows: "Now that we've joined the WTO, our companies are suffering from import competition. Real patriots buy Patrian goods. Why does anyone need a 6,000 PP watch from Helvetica if we can produce a watch for 50 PP at home?"

  Helvetica is a small, developed nation that created a niche for itself in the production and export of luxury goods such as watches, yachts, and limited-edition sports cars. In

response to Patria's new tax, Helvetica requested and obtained a WTO panel to examine Patria's new tax regime. Helvetica is of the view that the tax is a thinly disguised form of protectionism prohibited under WTO rules.
How would a WTO panel approach Patria's "luxury tax"? GATT, Article II regulates taxes (it is not a duty as it also applies for national products)
Does GATT Article III:2 apply to the tax and, if so, does the tax violate national treatment?

Lesson 4, part 2:

The National Treatment Principle and Internal Regulation

- **Behind the border regulations**:
  - Protection of domestic industries could be obtained through what is called «regulatory protectionism».
  - This consists in the setting out of domestic regulatory requirements which make it difficult or anti-economic for foreign companies to sell their goods in theimporting country.
  - (E.g.: a measure requiring all imported steel arrive in Italy by air rather than by
  - sea; all imported products undergo expensive and time-consuming inspections; be labeled in Italian; be sold only through specified distribution networks…
  - To prevent WTO Members from adopting such measures, the GATT requires them to respect theNATIONAL TREATMENT OBLIGATION
- GATT, Article III National Treatment and Regulations: The products of the territory of any contracting party importedinto the territory of any other contracting party shall be accorded
  - treatment no less favourable than that accorded to like products of
  - national origin in respect of all laws, regulations and requirements
  - affecting their internal sale, offering for sale, purchase, transportation,
  - distribution or use. (…)
- Ad note to Article III
  Any internal tax or other internal charge, or any law, regulation or requirement of the kind referred to in paragraph 1 which applies to an imported product and to the like domestic product and is collected or enforced in the case of the imported product at the time or point of importation, is nevertheless to be regarded as an internal tax or other internal charge, or a law, regulation or requirement of the kind referred to in paragraph 1 and is accordingly subject to the provisions of Article III.

- What about a domestic regulation requiring all imported vehicles to undergo a test at customs to assess that they respect the country's emissions standards against pollution?

- This also amounts to a regulation that can have a negative effect on trade, but here we could speak of a «good» regulation. GATT choice was not to distinguish between bad or good regulations: the rule is always that of non-discrimination between domestic and imported products.
- How would you rate "regulatory protectionism" from an economic standpoint? (in comparison to tariffs/quotas/subsidies)
  It has the same protectionist effects as tariffs or quantitative restrictions but compared to the other trade barriers:
  -the cost of tariffs generates higher revenues for the importing government.
  - the cost of quotas generates revenues for the foreign exporters who are able to reach the import market.
  -subsidies generate revenues for their beneficiaries
  Regulatory protectionism only **generates wasteful expenditures**: it increases the deadweight loss of the system.
- So why do policymakers choose it?
  It is the most difficult form of protection to identify (policymakers can try to disguise it as some sort of legitimate policy objective)
  - It is usually well accepted by the electoral body and doesn't have negative effects on political consent
  - (on the contrary higher tariffs may be unpopular as they mean higher prices in the domestic market)
- Leading case: EC-Asbestos (AB Report, 2001)
  1996: Decree enacted by France banning the manufacture, sale and importation of asbestos fibers and of products containing asbestos (alternative fibers like polyvinyl, cellulose and glass fibers were permitted)
  Canada starts a procedure before the panel/AB claiming the violation of GATT Article III:4
  As the Decree was «origin neutral», why Article III:4?(we are speaking of a BAN……)
  It's a landmark case because it clarifies the notion of «like products» under Article III:4; but also because, for the **first time**, the Appellate Body considers the carcinogenicity and/**or** **toxicity of a product as relevant in order to decide on products likeness**.
  Before EC-Asbestos such negative effects of a product on consumers' health could only trigger the applicability of the waiver provided for by Article XX (b).
- **When products are «like»** under Article III:4 of the GATT 1994? «The product scope of Article III:4, although broader than the first sentence of Article III:2, is certainly not broader than the combined scope of the two sentences of Article III:2 of the GATT 1994» (EC-Asbestos, AB Report, para. 99).
- The criterion to be used as a basis for comparison between imported and internal products is their competitive relationship in the marketplace (AB Report, par. 103)
- **How can the interpreter find out if there is such a relationship?**
  1. Likeness has to be examined on a case-by-case basis;
  2. All the pertinent evidence must be considered

- Broader way than “likeness” in Article 3.2.
- Once likeness has been assessed, one must establish that the contested regulation accords to the group of «like» imported products «less favourable treatment» than it accords to the group of «like» domestic products.
  «a detrimental impact on the conditions of competition» for imported products
- In EC-Seals (WT/DS401, AB Rep. 2014) the AB clarified the meaning of «less favorable treatment»
  «if there is less favorable treatment of the group of like imported products, there is, conversely, protection of the group of like domestic products»
  In other words, there is less favorable treatment of imports if the measure affects competitive opportunities to the detriment of imports (so affording protection to domestic products)
- Process and production methods could be in themselves harmful for the environment or could violate social rights of workers.
- In consideration of the language used in Article III:4 and in the Ad Note toArticle III, it has been highly controversial if Article III covers measures designed not in view of the product physical features, but which relate to the process or production method (PPMs) by which the product has been obtained.
  -If GATT Article III does not cover them, then they would fall under the prohibition provided for under Article XI.
  -States could not adopt them as legitimate policy tools.
- In EC-Seals the AB has examined the European seal ban and the two related exceptions under Article III:4.
  this means that a PPM measure (in EC-Seals a nonproduct-related PPM) will violate Article III:4 only if one can demostrate:
  1. «likeness» and
  2. «a detrimental impact on the conditions of competition» for the imported product («treated less favourably»)
  What if this detrimental impact is inevitable to pursue a legitimate policy objective? the measure will still violate Article III:4
  ….but even a de facto national treatment violation could be justified under GATT Article XX (General Exceptions)