xhibit 20

OVERVIEW OF THE WTO AGREEMENTS

1) Basic Objectives of the WTO

As stated in the preamble of the Agreement Establishing the World Trade Organization, the objectives of the WTO Agreements include "raising standards of living, ensuring full employment and a large and steadily growing volume of real income and effective demand, and expanding the production of and trade in goods and services"; in other words, developing the world economy under market-economy principles. In order to contribute to these objectives, the WTO Agreements are established for the purpose of entering into reciprocal and mutually advantageous arrangements designed for "the substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international trade relations." This means that the WTO Agreements are structured, for the purpose of introducing market-economy principles into international trade, on the basis of the two ideals: (1) reducing trade barriers, and (2) applying nondiscriminatory rules.

Such an approach conforms to the traditional spirit of GATT (The General Agreement on Tariffs and Trade), which was carried over from the preamble of the GATT 1947 to the new WTO preamble. In light of the subsequent changes, two objectives were added to the WTO. One is environmental consideration, which entails "allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and enhance the means for doing so in a manner consistent with their respective needs and concerns at different levels of economic development." The other is consideration for developing countries, which seeks to recognize "that there is need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development." The WTO Agreements also provide more consideration to the interests of developing countries, because the number of its members is by far larger than when GATT was established and single undertaking was a condition of entry.

2) Basic Principles of the WTO Agreements

(a) Basic Principles of the WTO Agreements

As explained above, the WTO Agreement is based on the concept of reducing trade barriers and applying nondiscriminatory rules. These ideals are embodied in the following basic principles of the WTO.

Principle of MFN (Most-Favored-Nation) Treatment

GATT Article I provides that with respect to tariffs, *etc.* on exports and imports, the most advantageous treatment accorded to the products of any country must be accorded immediately and unconditionally to the like products of all other members (*see* Chapter 1 "Most-Favored-Nation Treatment Principle").

Principle of National Treatment

GATT Article III requires that with respect to internal taxes, internal laws, *etc.* applied to imports, treatment not less favorable than that which is accorded to like domestic products must be accorded to all other Members (*see* Chapter 2 "National Treatment Principle").

Principle of General Prohibition of Quantitative Restrictions

GATT Article XI stipulates that "No prohibitions or restrictions other than duties, taxes or other charges shall be instituted or maintained by any contracting party" and generally prohibits quantitative restrictions. One reason for this prohibition is that quantitative restrictions are considered to have a greater protective effect than tariff measures and are more likely to distort the free flow of trade (*see* Chapter 3 "Quantitative Restrictions").

Principle regarding Tariffs as Legitimate Measures for the Protection of Domestic Industries

GATT accepts the imposition of tariffs as the only method of trade control, and attempts to gradually reduce tariff rates for individual items in tariff negotiations. Member countries make "concessions" ("bind" themselves to maximum rates) according to GATT Article XXVIII the imposition of tariffs beyond such maximum rates ("bound rates") or the unilateral raise in bound rates is banned. In addition, tariff rates are to be reduced in negotiations "on a reciprocal and mutually advantageous basis" according to GATT Article XXVIII bis (*see* Chapter 4 "Tariffs").

(b) Exceptions to the Basic Principles

The WTO Agreements provide important exceptions to the above basic principles. There are two chief reasons for the necessity of these exceptions. The first is that, in order to maintain the multilateral trade system, it is necessary to permit exceptional measures in a controlled manner when specific criteria are met. Thus, the GATT and WTO have provisions that permit exceptions to the basic principles when it is necessary to take measures (so-called trade remedies) to countervail the effects of other countries' trade actions (*see* Chapter 5 "Anti-Dumping Measures", Chapter 6 "Subsidies and Countervailing Measures" and Chapter 7 "Safeguards" for trade remedies). The second involves a need to consider the ability of a country to implement its obligations based on the degree of its economical development. Thus, the WTO Agreements permit the protection of domestic industries via tariffs and contain various exception provisions to its principles for developing countries.

The exceptions are established because of the difficulty involved in applying the principles of the multilateral system to the real international economy. The WTO Agreements try to harmonize reality and principles by specifying the requirements for allowing exceptions in certain cases. While the WTO's attitude can be highly praised for its forward-looking realism, there exist abuses of the exception provisions because of ambiguities among the requirements. The WTO Agreements improved some provisions of GATT that were hotbeds of abuse by clarifying their requirements. However, there still remain some unsatisfactory provisions. Further clarification is one of the challenges facing the WTO.

3) Overview of the WTO Agreements

Figure II-1 provides an overview of the WTO Agreements. The WTO Agreements comprise the Agreement Establishing the World Trade Organization and its Annexes. Annexes 1A to 3 are integral parts of the Agreement and are binding on all members of the WTO ("single undertaking" mentioned earlier). As shown in Figure II-2, the members are 150 economies as of February 2007. In contrast, the agreements included in Annex 4 are independent agreements and, therefore, binding only on the members that have accepted them. Below, we briefly describe each agreement of the WTO.

<The Marrakesh Agreement Establishing the World Trade Organization>

This is an agreement for implementing the results of the Uruguay Round and establishing the World Trade Organization, which will be a framework for future multilateral trade negotiations. The Agreement comprises general provisions on the WTO's organization, membership, decision-making, *etc.*

<Annex 1A: Multilateral Agreement on Trade in Goods>

General Agreement on Tariffs and Trade 1994 (GATT 1994)

The General Agreement consists of: (i) the provisions of GATT 1947 (including those amended by the terms of legal instruments that have taken effect before the entry

into force of the WTO Agreement); (ii) legal instruments, such as protocols and certifications relating to tariff concessions, protocols of accession, *etc.*, that have taken effect under the GATT 1947 before the entry into force of the WTO Agreement; and (iii) the six understandings that are deemed to be an integral part of the GATT 1994, such as Article II:1(b) and Article XVII.

Agreement on Agriculture

The Agreement on Agriculture includes specific and binding commitments made by WTO Member governments in the three areas of market access, domestic support and export subsidization for strengthening GATT disciplines and improving agricultural trade. These commitments were implemented over a six-year period. The Agreement also includes provisions on the implementation of these commitments (*see* Chapter 3 "Quantitative Restrictions" and Chapter 6 "Subsidies and Countervailing Measures" for quantitative restrictions and domestic support).

Agreement on the Application of Sanitary and Phytosanitary (SPS) Measures

This agreement establishes multilateral frameworks for the planning, adoption and implementation of sanitary and phytosanitary measures to prevent such measures from being used for arbitrary or unjustifiable discrimination or for camouflaged restraint on international trade and to minimize their adverse effects on trade (*see* Chapter 10 "Standard and Conformity Assessment Systems").

Agreement on Textiles and Clothing

Textile trade was governed by the Multi-Fiber Arrangement (MFA) since 1974. However, the GATT principles had been undermined by import protection policies, *etc.* The agreement provides that textile trade should be deregulated by gradually integrating it into GATT disciplines over a 10-year transition period, which expired at the end of 2004 (*see* Chapter 7 "Safeguards").

Agreement on Technical Barriers to Trade (TBT)

Standards and conformity assessment systems, such as industrial standards and safety/environment regulations, may become trade barriers if they are excessive or abused. This agreement aims to prevent such systems from becoming unnecessary trade barriers by securing their transparency and harmonization with international standards (*see* Chapter 10 "Standards and Conformity Assessment Systems").

Agreement on Trade-Related Investment Measures (TRIMs)

In relation to cross-border investment, countries receiving foreign investment may take various measures, including imposing requirements, conditions and restrictions (investment measures) on investing corporations. In the Uruguay Round, negotiations were initially conducted with an eye toward expanding disciplines governing investment measures. However, the Agreement on Trade-Related Measures, which was the result of the negotiations, banned only those investment measures inconsistent with the provisions of Article III (principle of national treatment) and Article XI (general elimination of quantitative restrictions) which have direct adverse effects on trade in goods. As examples, the Agreement cited local content requirements (which require that certain components be domestically manufactured) and trade balancing requirements. (*see* Chapter 8 "Trade-Related Investment Measures").

Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (Anti-Dumping Agreement)

This agreement aims to tighten and codify disciplines for calculating dumping margins and conducting dumping investigations, *etc.* in order to prevent anti-dumping measures from being abused or misused to protect domestic industries (*see* Chapter 5 "Anti-Dumping Measures").

Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994 (Customs Valuation Agreement)

In order to implement GATT Article VII (customs valuation) in a more consistent and reliable manner, this agreement specifies rules for the application of the article and aims to harmonize customs valuation systems on an international basis by eliminating arbitrary valuation systems (Chapter 4 "Tariffs").

Agreement on Pre-shipment Inspection (PSI)

This agreement aims to secure transparency of PSI and to provide a mechanism for the solution of disputes between PSI agencies and exporters.

Note: Pre-shipment Inspection is a system under which a pre-shipment inspection company designated by the importing country (mostly developing countries) conducts inspection of the quality, volume, price, tariff classification, customs valuation, *etc.* of merchandise in the territory of the exporting country on behalf of the importing country's custom office and issues certificates

Agreement on Rules of Origin

This agreement provides a program for the harmonization of rules of origin for application to all non-preferential commercial policy instruments. It also establishes disciplines that must be observed in instituting or operating rules and provides for dispute settlement procedures and creates the rules of origin committee. However, details on the harmonization of rules of origin are left for future negotiations (*see* Chapter 9 "Rules of Origin").

Agreement on Import Licensing Procedures

In order to prevent import licensing procedures of different countries from becoming unnecessary trade barriers, this agreement aims to simplify administrative procedures and ensure their fair operation.

Agreement on Subsidies and Countervailing Measures

This agreement aims to clarify definitions of subsidies, strengthen disciplines by subsidy type (extension of the range of prohibited subsidies, *etc.*), and to strengthen and clarify procedures for adopting countervailing tariffs (*see* Chapter 6 "Subsidies and Countervailing Measures").

Agreement on Safeguards

This agreement aims to, in relation to the application of safeguards (emergency measures to restrict imports) of GATT Article XIX, clarify disciplines for requirements and procedures for imposing safeguards, and related measures, *etc.* (*see* Chapter 7 "Safeguards").

<Annex 1B>
General Agreement on Trade in Services (GATS)

This agreement provides general obligations regarding trade in services, such as most- favored-nation treatment and transparency. In addition, it enumerates 155 service sectors and stipulates that a member country cannot maintain or introduce, in the service sectors for which it has made commitments, market access restriction measures and discriminatory measures that are severer than those on the commitment table (*see* Chapter 11 "Trade in Services").

<Annex 1C>
Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS)

This agreement stipulates most-favored-nation treatment and national treatment for intellectual properties, such as copyright, trademarks, geographical indications, industrial designs, patents, IC layout designs and undisclosed information. In addition, it requires Member countries to maintain high levels of intellectual property protection and to administer a system of enforcement of such rights. It also stipulates procedures for the settlement of disputes related to the agreement (*see* Chapter 12 "Protection of

Intellectual Property Rights").

<Annex 2>
Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU)

This "agreement" provides the common rules and procedures for the settlement of disputes related to the WTO Agreements. It aims to strengthen dispute settlement procedures by prohibiting unilateral measures, establishing dispute settlement panels whose reports are automatically adopted, setting time frames for dispute settlement, establishing the Appellate Body, *etc.*

<Annex 3>
Trade Policy Review Mechanism (TPRM)

Annex 3 provides the procedures for the Trade Policy Review Mechanism to conduct periodical reviews of Members' trade policies and practices conducted by the Trade Policy Review Body (TPRB).

<Annex 4> Plurilateral Trade Agreements [1]
Agreement on Trade in Civil Aircraft

Concurrently with the Uruguay Round, negotiations were under way to revise the civil aircraft agreement (an agreement from the Tokyo Round) and strengthen disciplines on subsidies. However, no agreement has yet been reached and the agreement reached under the Tokyo Round remains in effect.

Agreement on Government Procurement

This agreement requires national treatment and non-discriminatory treatment in the area of government procurement (purchase or lease of goods and services by governments) and calls for fair and transparent procurement procedures. It also stipulates complaint and dispute settlement procedures. The new Government Procurement Agreement is based on the Agreement of 1979 (an agreement from the Tokyo Round), but expands its scope. The new Agreement covers the procurement of services (in addition to goods) and the procurement by sub-central government entities and government-related agencies (in addition to central government). (*See* Chapter 13 "Government Procurement")

4) Organization of the WTO

The WTO is an organization established for achieving the objectives of the WTO Agreements and other multilateral trade agreements. Under the WTO system, the

[1] The International Dairy Agreement and the International Bovine Meat Agreement, which were in effect for three years from 1995, ceased to be effective as of the end of 1997 because of a decision not to renew them.

operation and implementation of agreements, including dispute settlement and trade policy review, are accomplished and multilateral trade negotiations are carried out to further liberalize, strengthen and expand trade rules. The ministerial conference, general council, councils for trade in goods, services and TRIPs, *etc.* have been established in the WTO for these purposes (*see* Figure II-3).

5) History of Liberalization Negotiations under the GATT and the WTO

What is a round?

GATT members have engaged in eight intensive series of multilateral trade negotiations. Since the fifth series of negotiations (Dillon Round), multilateral negotiations under the GATT have been called the "XX Round Negotiations" or simply the "XX Round."

During the Doha Ministerial Conference, it was decided to launch a new series of negotiations. This series of negotiations is called the Doha Development Agenda, because some developing countries oppose the word "Round." Figure II-4 outlines a brief history of trade liberalization negotiations.

Tariffs were gradually reduced over the course of several negotiating rounds. In addition, trade rules other than tariffs were developed. In particular, the Uruguay Round produced landmark results, including the strengthening of trade rules and the development of binding dispute settlement procedures.

GATT round negotiations

Year	GATT round negotiations	Countries
1947	1st (Geneva)	23
1949	2nd (Annecy)	13
1951	3rd (Torquay)	38
1956	4th (Geneva)	26
1960-62	Dillon Round	26
1964-67	Kennedy Round	62
1973-79	Tokyo Round	102
1986-93	Uruguay Round	123
2001-	Doha Development Agenda	150

Source: WTO webpage (http://www.wto.org/);
Note: The number of participating countries and regions in the Doha Development Agenda represents the total number of WTO Member countries as of the end of February 2007.

Figure II -1 Marrakech Protocol for the Establishment of the World Trade Organization

(WTO Protocol)

Marrakech Protocol to establish the World Trade Organization (WTO Establishment Protocol)

- Multilateral Agreements on Trade in Goods (Annex 1A)
  - General Agreement on Tariffs and Trade 1994 (1994 GATT)
  - Agreement on Agriculture
  - Agreement on the Application of Sanitary and Phytosanitary Measures
  - Agreement on Textiles and Clothing (expired at the end of 2004)
  - Agreement on Technical Barriers to Trade (TBT)
  - Agreement on Trade-Related Investment Measures (TRIMs)
  - Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (Anti-Dumping Agreement)
  - Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1994 (Customs Valuation Agreement)
  - Agreement on Preshipment Inspection (PSI)
  - Agreement on Rules of Origin
  - Agreement on Import Licensing Procedures
  - Agreement on Subsidies and Countervailing Measures
  - Agreement on Safeguards
- General Agreement on Trade in Services (GATS) (Annex 1B)
- Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) (Annex IC)
- Understanding on Rules and Procedures Governing the Settlement of Disputes (Annex 2)
- Trade Policy Review Mechanism (TPRM) (Annex 3)
- Plurilateral Trade Agreements (Annex 4) [2]
  - Agreement on Trade in Civil Aircraft
  - Agreement on Government Procurement

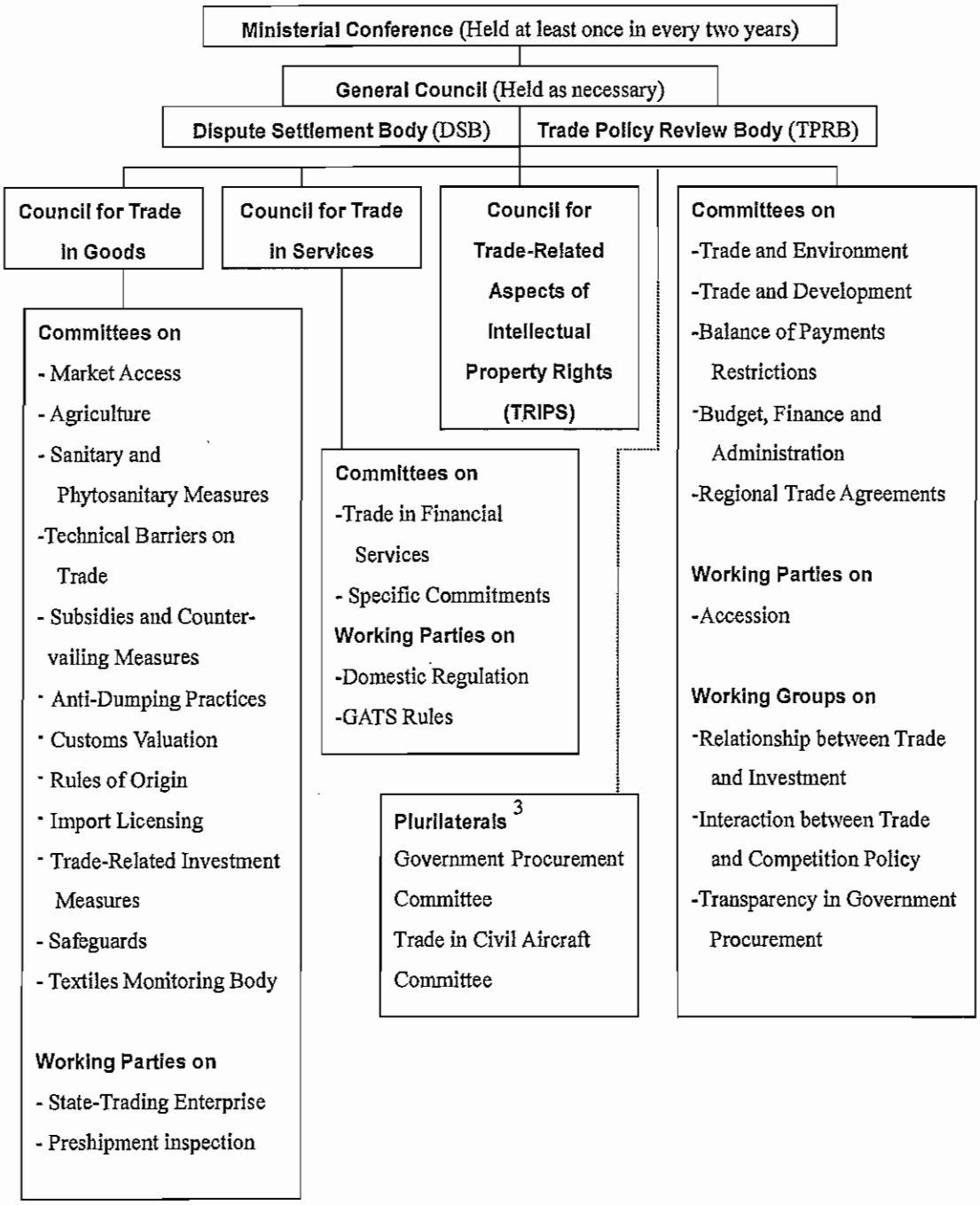
[2] International Dairy agreement and International Bovine Meat Agreement were valid for 3 years from 1995, but revoked at the end of 1997 due to the resolution of non-extension for 1998 and beyond.

Figure II -2 WTO Member Countries and Regions

As of February 2007

	Year	Asia	Europe	Americas	Africa	Oceania
WTO member countries and regions (150)	1995 (112)	Bahrain (1995.1.1) Brunei (1995.1.1) Bangladesh (1995.1.1)Japan (1995.1.1) Hong Kong (1995.1.1) India (1995.1.1) Indonesia (1995.1.1) Sri Lanka (1995.1.1) Rep. of Korea (1995.1.1) Kuwait (1995.1.1) Singapore (1995.1.1) Malaysia (1995.1.1) Pakistan (1995.1.1) Myanmar (1995.1.1) Thailand (1995.1.1) Philippines (1995.1.1) Macao (1995.1.1) Turkey (1995.3.26) Israel (95.4.21) Maldives (95.5.31) Cyprus (95.7.30) (21)	Austria (1995.1.1) Belgium (1995.1.1) Czech (1995.1.1) Denmark (1995.1.1) EC (1995.1.1) UK (1995.1.1) Finland (1995.1.1) France (1995.1.1) Germany (1995.1.1) Greece (1995.1.1) Hungary (1995.1.1) Iceland (1995.1.1) Ireland (1995.1.1) Italy (1995.1.1) Sweden (1995.1.1) Malta (1995.1.1) Luxemburg (1995.1.1) Netherlands (1995.1.1) Norway (1995.1.1) Portugal (1995.1.1) Romania (1995.1.1) Slovakia (1995.1.1) Spain (1995.1.1) Poland (1995.7.1) Switzerland (1995.7.1) Slovenia (95.7.30) Lichtenstein (1995.9.1) (27)	Antigua-Barbuda (1995.1.1) Argentine (1995.1.1) Belize (1995.1.1) Barbados (1995.1.1) Canada (1995.1.1) Paraguay (1995.1.1) Chile (1995.1.1) Brazil (1995.1.1) Honduras (1995.1.1) Costa Rica (1995.1.1) Mexico (1995.1.1) Dominica (1995.1.1) Guiana (1995.1.1) St Vincent and the Grenadines (1995.1.1) St Lucia (1995.1.1) Suriname (1995.1.1) Peru (1995.1.1) Uruguay (1995.1.1) USA (1995.1.1) Venezuela (1995.1.1) Trinidad Tobago (1995.3.1) Dominican Republic (1995.3.9) Jamaica (1995.3.9) Cuba (95.4.20) Colombia (95.4.30) El Salvador (95.5.7) Guatemala (95.7.21) Nicaragua (95.9.3) Bolivia (95.9.13) (29)	Senegal (1995.1.1) South Africa (1995.1.1) Tanzania (1995.1.1) Ivory Coast (1995.1.1) Nigeria (1995.1.1) Ghana (1995.1.1) Mauritius (1995.1.1) Morocco (1995.1.1) Kenya (1995.1.1) Gabon (1995.1.1) Uganda (1995.1.1) Zambia (1995.1.1) Namibia (1995.1.1) Swaziland (1995.1.1) Zimbabwe (1995.3.3) Tunisia (1995.3.29) Guinea Bissau (1995.5.31) Botswana (1995.5.31) Lesotho (1995.5.31) Central African Repub. (1995.5.31) Malawi (1995.5.31) Mali (1995.5.31) Mauritania (1995.5.31) Togo (1995.5.31) Djibouti (1995.5.31) Burkina Faso (1995.6.3) Egypt (1995.6.30) Burundi (1995.7.23) Sierra Leone (1995.7.23) Mozambique (1995.8.26) Guinea (1995.10.25) Madagascar (1995.11.17) Cameroon (1995.12.13) (33)	Australia (1995.1.1) New Zealand (1995.1.1) (2)
	1996 (16)	Qatar (1996.1.13.) United Arab Emirates (1996.4.10) (2)	Bulgaria (1996.12.1) (1)	Ecuador (1996.1.21) Haiti (1996.1.30) St. Kitts and Nevis (1996.2.21) Grenada (1996.2.22) (4)	Benin (1996.2.22) Rwanda (1996.5.22) Chad (1996.10.19) Gambia (1996.10.23) Angola (1996.12.1) Niger (1996.12.13) (6)	Fiji (1996.1.14) Papua New Guinea (1996.6.9) Solomon Islands (1996.7.26) (3)
	1997 (4)	Mongol (1997.1.29) (1)		Panama (1997.9.6) (1)	Congo Repub. (1997.1.1) Congo (1997.3.27) (2)	
	1998 (1)		Kyrgyz (1998.12.20) (1)			
	1999 (2)		Latvia (1999.2.10) Estonia (1999.11.13) (2)			
	2000 (5)	Jordan (2000.4.11) Oman (2000.11.9) (2)	Georgia (2000.6.14) Albania (2000.9.8) Croatia (2000.11.30) (3)			
	2001 (3)	China (2001.12.11) (1)	Lithuania (2001.5.31) Moldova (2001.7.27) (2)			
	2002 (1)	Chinese Taipei (2002.1.1) (1)				
	2003 (2)		Armenia (2003.2.5) Macedonia (2003.4.4) (2)			
	2004 (2)	Nepal(2004.4.23) Cambodia(04.10.13) (2)				
	2005 (1)	Saudi Arabia,(2005.12.11) (1)				
	2006 (0)					
	2007 (1)	Vietnam(2007.01.11) (1)				
Before coming into force of the Protocol (1)						Tonga (2005.12.11) (1)
Applying for membership (28)		Bhutan, Laos, Lebanon, Vietnam, Yemen, Syria, Iran, Iraq, Afghanistan (10)	Andorra, Azerbaijan, Belarus, Bosnia-Herzegovina, Kazakhstan Russia, Ukraine, Uzbekistan, Yugoslavia Tajikistan (10)	Bahamas (1)	Algeria, Seychelles, Sudan, Cape Verde Ethiopia, Libya (6)	Vabuatu,Samoa (3)

Figure II -3 The WTO Organization



3 The Committees on Dairy Products and Beef Products were dissolved at the end of 1997 when the International Agreement on Dairy Products and the International Agreement on Beef Products.

Figure Ⅱ-4 Flow of Trade Liberalization Negotiation at WTO

<Market Access>				<Rules>			
	Tariff on Industrial and Mining Products	1947	1st Round (Geneva)				
	Jan. 1948 GATT entered into force						
	Tariff on Industrial and Mining Products	1949-1962	2nd Round (Annecy) ～ Dillon Round				
	Tariff on Industrial and Mining Products	1973-1979	Tokyo Round	AD TBT Government Procurement Subsidies Licensing etc.			
Services Agriculture	Tariff on Industrial and Mining Products	1986-1993	Uruguay Round	AD TBT Government Procurement Subsidies Licensing etc.	Textile Agreement PSI Country of Origin TRIPS, SPS DSU, TRIM		
Jan. 1995 WTO Agreements enter into force							
<u>Services</u> <u>Agriculture</u> Energy Distribution e-Commerce	Tariff on Industrial and Mining Products	2001-	Doha Development Agenda	AD Subsidies Regional Trade Agreement	TRIPS Partial negotiation	Trade Facilitation Investment * Competition * Transparency of Government Procurement * e-Commerce	Environment

Underlined is Built-in Agenda item
* : Start preparatory negotiation

Exhibit 21

Panel Report
Japan - Taxes on Alcoholic Beverages
(WT/DS8,10,11/R) / DSR 1996:I, 125

Parties
Complainants: Canada, EC, U.S.
Respondent: Japan
Third Parties: None

Timeline of Dispute
Panel Request (EC): September 14, 1995
Panel Request (Canada): September 14, 1995
Panel Request (U.S.): September 14, 1995
Panel Established: September 27, 1995
Panel Composed: October 30, 1995
Interim Report Issued: May 20, 1996
Final Report Circulated: July 11, 1996
Notice of Appeal: August 8, 1996
AB Report Circulated: October 4, 1996
Adoption: November 1, 1996

Panelists
Mr. Hardeep Puri (Chairperson),
Dr. Luzius Wasescha, Mr. Hugh McPhail

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Key Findings

- Adopted GATT panel reports are "subsequent practice" that must be "taken into account" by WTO panels and the Appellate Body, although these reports do not have to be "followed." **[Panel's finding that adopted panel reports constitute "subsequent practice" reversed by Appellate Body.]**
- Unadopted GATT panel reports do not have to be taken into account, but they may provide "useful guidance." **[Upheld by Appellate Body.]**
- Under GATT Article III:2, first sentence, whether products are "like" is to be determined on a case-by-case basis. Relevant criteria for determining "likeness" include: (1) the product's properties, nature and quality, and its end-uses; (2) consumers' tastes and habits; and (3) the product's tariff classification. **[Upheld by Appellate Body.]**
- Shochu and vodka are "like" products. Because vodka is taxed in excess of shochu, Japan has violated Article III:2, first sentence. **[Upheld by Appellate Body.]**
- The text of GATT Article III:2, first sentence, does not provide for an "aim-and-effect" test. **[Upheld by Appellate Body.]**
- Shochu and the other products at issue are "directly competitive or substitutable." Because these products are "not similarly taxed" so as to afford protection to shochu, Japan has violated Article III:2, second sentence. **[Panel's conclusion upheld, but reasoning modified by Appellate Body.]**
- Under GATT Article III:2, second sentence, elasticity of substitution between products is relevant for determining whether they are "directly competitive or substitutable." **[Upheld by Appellate Body.]**

BACKGROUND

This dispute concerns the Japanese Liquor Tax Law (Shuzeiho), Law No. 6 of 1953, as amended. This law established a system of internal taxes applicable to all liquors, defined as domestically produced or imported beverages having an alcohol content of not less than one degree and intended for consumption in Japan. The Liquor Tax Law classifies the various types of alcoholic beverages into ten categories (as well as additional sub-categories): sake, sake compound, shochu (group A, group B), mirin, beer, wine (wine, sweet wine), whisky/brandy, spirits, liqueurs and miscellaneous (various sub-categories).

Different tax rates are applied at the wholesale level to each of the various categories and sub-categories defined by the Liquor Tax Law. The rates are expressed as a specific amount in Japanese Yen ("¥") per litre of beverage. For each category or sub-category, the Liquor Tax Law sets out a specific alcohol content per litre for that beverage and the corresponding tax rate. Under this methodology, the liquors covered by the dispute are subject to the following tax rates:

Shochu A (shochu distilled with a continuous still)

Alcohol Strength	Tax Rate (per 1 kilolitre)
(1) 25 to 26 degrees	¥155,700
(2) 26 to 31 degrees	¥155,700 plus ¥9,540 for each degree above 25
(3) 31 degrees and above	¥203,400 plus ¥26,230 for each degree above 30
(4) 21 to 25 degrees	¥155,700 minus ¥9,540 for each degree below 25 (fractions are rounded up to 1 degree)
(5) below 21 degrees	¥108,000

Shochu B (other shochu)

Alcohol Strength	Tax Rate (per 1 kilolitre)
(1) 25 to 26 degrees	¥102,100
(2) 26 to 31 degrees	¥102,100 plus ¥6,580 for each degree above 25
(3) 31 degrees and above	¥135,000 plus ¥14,910 for each degree above 30
(4) 21 to 25 degrees	¥102,100 minus ¥6,580 for each degree less than 25 (fractions are rounded up to 1 degree)
(5) below 21 degrees	¥69,200

Whisky

Alcohol Strength	Tax Rate (per 1 kilolitre)
(1) 40 to 41 degrees	¥982,300
(2) 41 degrees and above	¥982,300 plus ¥24,560 for every degree above 40
(3) 38 to 40 degrees	¥982,300 minus ¥24,560 for each degree below 40 (fractions are rounded up to 1 degree)
(4) below 38 degrees	¥908,620

Spirits

Alcohol Strength	Tax Rate (per 1 kilolitre)
(1) below 38 degrees	¥367,300
(2) 38 degrees and above	¥367,300 plus ¥9,930 for each degree above 37

Liqueurs

Alcohol Strength	Tax Rate (per 1 kilolitre)
(1) below 13 degrees	¥98,600
(2) 13 degrees and above	¥98,600 plus ¥8,220 for each degree over 12

A special formula is applied to determine the tax rate for beverages having an alcohol strength below 13 degrees or, in the case of "liqueurs," below 12 degrees.

(Paras. 2.1-4)

The complaining parties claimed that this system violates GATT Article III:2, first sentence and Article III:2, second sentence because it taxes shochu at a lower rate than the other products.

SUMMARY OF PANEL'S FINDINGS

PROCEDURAL AND SYSTEMIC ISSUES

Terms of Reference

The United States made a claim with respect to the Japanese Taxation Special Measures Law. Japan argued that the claim was outside the Panel's terms of reference. The Panel found that because there is no mention of this law in its terms of reference, it is not permitted to examine claims regarding the law. (Para. 6.5)

Status of Prior Panel Reports

In setting out the general principles of interpretation to be followed under DSU Article 3.2, the Panel referred to Articles 31 and 32 of the Vienna Convention on the Law of Treaties ("VCLT"). As part

of its approach, the Panel emphasized that VCLT Article 31(3)(b) provides that "any subsequent practice ... which established the agreement of the parties regarding [the treaty's] interpretation" shall be taken into account together with the context. The Panel noted that previous GATT and WTO panels have interpreted GATT Article III, the provision at issue in this case, and it considered that those previous panel reports that were adopted constitute "subsequent practice" under VCLT Article 31(3)(b). Moreover, it said that these reports constitute "other decisions of the CONTRACTING PARTIES to GATT 1947" under "Article 1(b)(iv) of GATT 1994," confirming that they constitute "subsequent practice." Therefore, the Panel concluded that such panel reports must be "taken into account" by subsequent panels dealing with similar issues, although their reasoning and results do not necessarily have to be "followed." (Para. 6.10) (On appeal, the Appellate Body reversed the Panel's conclusions that adopted panel reports are "subsequent practice" and "other decisions." See *DSC for Japan - Alcohol (AB).*)

The Panel further stated that *unadopted* panel reports have no legal status in the WTO legal system, since they have not been "endorsed" through decisions of the CONTRACTING PARTIES or WTO Members. Thus, they do not have to be "taken into account." However, the Panel added that the reasoning in these reports could nevertheless provide "useful guidance" to panels. (Para. 6.10) (On appeal, the Appellate Body upheld this conclusion. See *DSC for Japan - Alcohol (AB).*)

SUBSTANTIVE ISSUES

GATT Article III - General

The complaining parties argued that the Liquor Tax Law violates GATT Article III:2. In its findings on this issue, the Panel quoted the relevant provisions. Article III:2 reads:

> The products of the territory of any contracting party imported into the territory of any other contracting party shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products. 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.*

The asterisk at the end of the second sentence refers to an Interpretive Note to Article III:2, which provides:

> 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.

Finally, Article III:1 provides as follows:

> 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.

(Para. 6.6)

The Panel noted that Article III:2, first sentence is concerned with the treatment of "like products," whereas Article III:2, second sentence concerns the treatment of "directly competitive or substitutable products." (Para. 6.11) Further, the Panel observed that Article III:2, second sentence contains a reference "to the principles set forth in paragraph 1," whereas there is no such reference in Article III:2, first sentence. In this regard, the Panel stated that Article III:1 sets forth general principles that do not contain legally binding obligations. The Panel concluded, therefore, that Article III:1 should only be taken into account as *context* to the extent relevant and necessary. (Para. 6.12). Finally, the Panel recalled, as context, the findings of the GATT panels in *Canada - Alcohol Distribution (1992)* and *U.S. - Malt Beverages*, which both held that one of the basic purposes of GATT Article III is to ensure that internal taxes and regulations are not used to undermine tariff concessions granted under GATT Article II. (Para. 6.13)

The Panel then considered separately the complaining parties' claims of a violation of Article III:2, first sentence and of a violation of Article III:2, second sentence.

GATT Article III:2, first sentence

The European Communities and the United States alleged that the Liquor Tax Law violates Article III:2, first sentence because it taxes vodka and certain other products "in excess of" shochu, a "like product." In examining this claim, the Panel first rejected the "aim-and-effect" test proposed by both Japan and the United States. The Panel recalled that this test finds its textual basis in the words "so as to afford protection" in *Article III:1*, but has no basis in the words of *Article III:2, first sentence*. Furthermore, the Panel said, any examination of the "aim" of a measure is problematic, as the aim is sometimes "indiscernible." This difficulty is a result of the fact that there are often multiple "aims" behind a measure, and access to the complete legislative history of a national law or regulation could be impossible to obtain. In addition, the list of exceptions in GATT Article XX could become redundant if the "aims" specified there were taken into account under an Article III analysis. (Para. 6.17) Finally, while recognizing that the GATT panel in *U.S. - Malt Beverages* (as well as the panel in the unadopted *U.S. - Auto Taxes* report) had applied the "aim-and-effect" test in the context of Article III:2, the Panel reiterated that this approach was without a textual basis. (Para. 6.18)

Having rejected the "aim-and-effect" test, the Panel crafted the following test for GATT Article III, first sentence, consisting of three elements:

> (i) whether the products concerned are like, (ii) whether the contested measure is an "internal tax" or "other internal charge" (not an issue in this case) and (iii) if so, whether the tax imposed on foreign products is in excess of the tax imposed on like domestic products.

(Para. 6.19). If all three elements were answered in the affirmative, a violation of Article III:2, first sentence would be found.

The Panel then applied this test to Japan's Liquor Tax Law, turning first to the issue of whether the products concerned are "like." Referring to early GATT panel and working party reports, including the working party on *Border Tax Adjustments*, the Panel noted that this analysis should be carried out on a "case-by-case" basis, and that previous panels had examined a number of criteria, including: (1) the product's properties, nature and quality, and its end-uses; (2) consumers' tastes and habits; (3) and the

product's tariff classification. While "like" products need not be "identical" in all respects, the Panel pointed out that the "like product" standard should be construed "narrowly," with "like products" being a "subset" of "directly competitive or substitutable products," referred to in Article III:2, second sentence. (Paras. 6.21-22)

Applying its legal interpretation of "like products" to the facts of this case, the Panel first considered whether *vodka* and *shochu* are "like products." In this regard, the Panel noted that vodka and shochu share "most physical characteristics," and "except for filtration, there is virtual identity in the definition of the two products." It noted that this same conclusion had been drawn by the 1987 *Japan - Alcohol* GATT panel. Further, vodka and shochu were currently classified in the same Japanese tariff heading (although there would be a slight shift under the new heading that was to come into effect in 1996). For these reasons, the Panel considered that vodka and shochu are "like products." (Para. 6.23)

With regard to the *other products* at issue, by contrast, the Panel said that there were "[s]ubstantial noticeable differences in physical characteristics" with shochu. In particular, the "use of additives" would disqualify liqueurs, gin and genever; the "use of ingredients" would disqualify rum; and "appearance" would disqualify whisky and brandy. Therefore, these products were not "like" shochu. (Para. 6.23)

Because the second element, whether the measure is an "internal tax" or "other internal charge," was not at issue, the Panel then turned to the third element, whether taxes imposed on imported products are in excess of those imposed on like domestic products. Specifically, the Panel examined whether "vodka is taxed in excess of the tax imposed on shochu." In this regard, the Panel noted that vodka is taxed at 377,230 Yen per kilolitre whereas shochu A is taxed at 155,700 Yen per kilolitre, and there are similar differences when the tax is measured as a function of the degree of alcohol. Based on these figures, the Panel found that the facts showed that "it is obvious that the taxes imposed on vodka are higher than those imposed on shochu," and further stated that "the tax imposed on vodka is in excess of the tax imposed on shochu." (Para. 6.24)

The Panel then rejected Japan's argument that the Liquor Tax Law keeps the tax/price ratio of alcoholic beverages "roughly constant," stating the following: (1) it is irrelevant whether "roughly" the same treatment is given, under the wording of Article III:2, first sentence; (2) there were problems with Japan's methodology for calculating tax/price ratios; and (3) the legislation never mentioned that its purpose was to maintain a "roughly constant" tax/price ratio. (Para. 6.25)

The Panel concluded that by taxing vodka in excess of shochu, Japan is in violation of its obligations under Article III:2, first sentence. (Para. 6.27) (On appeal, the Appellate Body upheld the Panel's conclusion. See *DSC for Japan - Alcohol (AB).*)

GATT Article III:2, second sentence

The Panel then examined the complaining parties' claim that the Liquor Tax Law is inconsistent with the obligation in Article III:2, second sentence to tax "directly competitive or substitutable products" similarly. In the Panel's view, there are two elements to a claim under this provision:

> (i) whether the products concerned (whisky, brandy, gin, genever, rum and liqueurs) are directly competitive or substitutable, and (ii) if so, whether the treatment afforded to foreign products is contrary to the principles set forth in paragraph 1 of Article III.

(Para. 6.28)

The Panel first examined whether whisky, brandy, gin, genever, rum and liqueurs are "directly competitive or substitutable" with shochu. At the outset, the Panel recalled that this term should be interpreted more broadly than the term "like products." In this respect, the Panel stated that "greater emphasis should be placed on elasticity of substitution," and it noted that factors like "marketing strategies" could prove relevant. (Para. 6.28) The Panel cautioned, however, that consumer preference surveys must be done according to appropriate statistical methodologies.

The Panel concluded that the above-mentioned products are "directly competitive or substitutable" with shochu, for the following reasons: (1) the products concerned are all distilled spirits; (2) the 1987 GATT *Japan - Alcohol* panel report had made similar findings; (3) the evidence demonstrates that there is a "significant elasticity of substitution" among the products; and (4) there is evidence that whisky and shochu are "essentially competing for the same market." (Para. 6.32)

Turning to the second element, the Panel recalled the Interpretive Note to Article III:2, which establishes that a violation of Article III:2, second sentence will occur if "directly competitive or substitutable" products are not "similarly taxed" and if that tax "favours domestic products." (Para. 6.33) The Panel recalled that the 1987 GATT *Japan - Alcohol* panel report concluded that "the higher (i.e., dissimilar) Japanese taxes on imported alcoholic beverages and the existence of substitutability were 'sufficient evidence of fiscal distortions of the competitive relationship between imported distilled liquors and domestic shochu affording protection to domestic producers of shochu'." The Panel agreed with the 1987 GATT panel's conclusion. (Para. 6.33) In this regard, the Panel noted that for dissimilar taxation to afford protection, it would be sufficient to find that the dissimilarity in taxation is not *de minimis*. The Panel also stated that "the purpose or aim" of tax legislation need not be established to succeed on a claim under this provision. (Para. 6.33)

Having established this legal standard for the second element, the Panel then applied the law to the facts of this case. Looking at the actual tax rates under the Liquor Tax Law, the Panel concluded that the products in dispute are not "similarly taxed," because the taxes on shochu are lower than the taxes on the other products. Therefore, the Panel concluded that "protection is afforded to shochu" in a manner that is inconsistent with Article III:2, second sentence. (Para. 6.33)

On this basis, the Panel found that the Liquor Tax law is inconsistent with Article III:2, second sentence. (On appeal, the Appellate Body upheld the Panel's conclusion, but modified its reasoning. See *DSC for Japan - Alcohol (AB).*)

COMMENTARY

Status of Prior Panel Reports

The Panel's statements on the status of adopted panel reports were substantially modified by the Appellate Body. The Appellate Body did uphold, however, the Panel's conclusion that *unadopted* panel reports do not have to be taken into account, but could nevertheless provide "useful guidance" to panels. *See DSC for Japan - Alcohol (AB).*

Article III:2

See DSC for Japan - Alcohol (AB).

Last Update: March 2, 2005

Appellate Body Report
Japan - Taxes on Alcoholic Beverages
(WT/DS8,10,11/AB/R) / DSR 1996:I, 97

Participants
Appellant/Appellee: Japan
Appellant/Appellee: U.S.
Appellees: Canada, EC
Third Participants: None

Timeline of Dispute
Panel Request (EC): September 14, 1995
Panel Request (Canada): September 14, 1995
Panel Request (U.S.): September 14, 1995
Panel Established: September 27, 1995
Panel Composed: October 30, 1995
Interim Report Issued: May 20, 1996
Final Report Circulated: July 11, 1996
Notice of Appeal: August 8, 1996
AB Report Circulated: October 4, 1996
Adoption: November 1, 1996

Appellate Body Division
Lacarte-Muró (Presiding Member),
Bacchus, El-Naggar

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Key Findings

- Reversed Panel's conclusion that adopted panel reports constitute "subsequent practice" or "other decisions" that "must" be taken into account. Instead, found that adopted panel reports, while not binding on future panels, create "legitimate expectations" among WTO Members, and therefore "should" be taken into account where they are relevant to a dispute.

- Upheld Panel's finding that Article III:2, first sentence requires an examination of the conformity of an internal tax measure by determining, first, whether the taxed imported and domestic products are "like" and, second, whether the taxes applied to the imported products are "in excess of" those applied to the like domestic products. Upheld Panel's finding that vodka is taxed in excess of shochu, in violation of Article III:2, first sentence.

- Article III:2, second sentence requires an examination of whether: (1) the imported products and the domestic products *are "directly competitive or substitutable products" which are in competition with each other*; (2) the directly competitive or substitutable imported and domestic products *are "not similarly taxed"*; and (3) the dissimilar taxation of the directly competitive or substitutable imported products *is "applied ... so as to afford protection to domestic production."*

- Upheld the Panel's finding that shochu and certain "directly competitive or substitutable" products are not similarly taxed so as to afford protection to domestic production in violation of Article III:2, second sentence.

BACKGROUND

This dispute concerns the Japanese Liquor Tax Law (Shuzeiho), Law No. 6 of 1953, as amended. This law established a system of internal taxes applicable to all liquors, defined as domestically produced or imported beverages having an alcohol content of not less than one degree and intended for consumption in Japan. The Liquor Tax Law classifies the various types of alcoholic beverages into ten categories (as well as additional sub-categories): sake, sake compound, shochu (group A, group B), mirin, beer, wine (wine, sweet wine), whisky/brandy, spirits, liqueurs and miscellaneous (various sub-categories).

Different tax rates are applied at the wholesale level to each of the various categories and sub-categories defined by the Liquor Tax Law. The rates are expressed as a specific amount in Japanese Yen ("¥") per litre of beverage. For each category or sub-category, the Liquor Tax Law sets out a specific alcohol content per litre for that beverage and the corresponding tax rate. Under this methodology, the liquors covered by the dispute are subject to the following tax rates:

Shochu A (shochu distilled with a continuous still)

Alcohol Strength	Tax Rate (per 1 kilolitre)
(1) 25 to 26 degrees	¥155,700
(2) 26 to 31 degrees	¥155,700 plus ¥9,540 for each degree above 25
(3) 31 degrees and above	¥203,400 plus ¥26,230 for each degree above 30
(4) 21 to 25 degrees	¥155,700 minus ¥9,540 for each degree below 25 (fractions are rounded up to 1 degree)
(5) below 21 degrees	¥108,000

Shochu B (other shochu)

Alcohol Strength	Tax Rate (per 1 kilolitre)
(1) 25 to 26 degrees	¥102,100
(2) 26 to 31 degrees	¥102,100 plus ¥6,580 for each degree above 25
(3) 31 degrees and above	¥135,000 plus ¥14,910 for each degree above 30
(4) 21 to 25 degrees	¥102,100 minus ¥6,580 for each degree less than 25 (fractions are rounded up to 1 degree)
(5) below 21 degrees	¥69,200

Whisky

Alcohol Strength	Tax Rate (per 1 kilolitre)
(1) 40 to 41 degrees	¥982,300
(2) 41 degrees and above	¥982,300 plus ¥24,560 for every degree above 40
(3) 38 to 40 degrees	¥982,300 minus ¥24,560 for each degree below 40 (fractions are rounded up to 1 degree)
(4) below 38 degrees	¥908,620

Spirits

Alcohol Strength	Tax Rate (per 1 kilolitre)
(1) below 38 degrees	¥367,300
(2) 38 degrees and above	¥367,300 plus ¥9,930 for each degree above 37

Liqueurs

Alcohol Strength	Tax Rate (per 1 kilolitre)
(1) below 13 degrees	¥98,600
(2) 13 degrees and above	¥98,600 plus ¥8,220 for each degree over 12

A special formula is applied to determine the tax rate for beverages having an alcohol strength below 13 degrees or, in the case of "liqueurs," below 12 degrees.

(Panel Report, paras. 2.1-4)

The complaining parties claimed that this system violates GATT Article III:2, first sentence and Article III:2, second sentence because it taxes shochu at a lower rate than the other products. The Panel found violations of both of these provisions.

On appeal, Japan argued that the Panel erred in finding violations of these provisions. The United States, although it agreed with the Panel's ultimate conclusions with regard to these provisions, cross-appealed certain aspects of the Panel's legal reasoning, relating to both the interpretation of Article III:2 and the Panel's statements on the status of adopted panel reports.

SUMMARY OF APPELLATE BODY'S FINDINGS

PROCEDURAL AND SYSTEMIC ISSUES

Treaty Interpretation

The Appellate Body first addressed the issue of "Treaty Interpretation." It noted that DSU Article 3.2 directs the Appellate Body to clarify the provisions of GATT and the other "covered agreements" of the WTO Agreement "in accordance with customary rules of interpretation of public international law." Further, the Appellate Body recalled that in *U.S. - Gasoline* it had stressed the need to achieve such clarification by reference to the fundamental rule of treaty interpretation set out in Article 31(1) of the Vienna Convention on the Law of Treaties ("VCLT"), as this general rule of interpretation "has attained the status of a rule of customary or general international law." Article 31(1) provides:

> A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.

The Appellate Body stated that Article 32 of the VCLT, dealing with the role of supplementary means of interpretation, has also attained the same status. (Pages 10-12)

Status of Prior Panel Reports

In response to an appeal by the United States, the Appellate Body next examined the issue of the "Status of Adopted Panel Reports." The Panel had found that "panel reports adopted by the GATT CONTRACTING PARTIES and the WTO Dispute Settlement Body constitute subsequent practice in a specific case" under VCLT Article 31(3)(b), and that adopted panel reports in themselves constitute "other decisions of the CONTRACTING PARTIES to GATT 1947" for the purposes of "Article 1(b)(iv) of GATT 1994."

The Appellate Body reversed the Panel's findings. According to the Appellate Body, the CONTRACTING PARTIES to the GATT, when adopting a panel report, did not intend that their decision would constitute a "definitive interpretation" of the GATT provision at issue, nor is this contemplated under the WTO Agreement. The Appellate Body noted that WTO Agreement Article IX:2 provides: "The Ministerial Conference and the General Council shall have the exclusive authority to adopt interpretations of this Agreement and of the Multilateral Trade Agreements." In the Appellate Body's view, the fact that such an "exclusive authority" in interpreting the treaty has been established so specifically in the WTO Agreement is reason to conclude that such authority does not exist. (Page 13)

However, the Appellate Body made clear that it does not view prior adopted panel reports as having no relevance whatsoever. The Appellate Body stated that WTO Agreement Article XVI:1 and paragraph 1(b)(iv) of the language of Annex 1A incorporating the GATT 1994 into the WTO Agreement affirm the importance of the experience acquired by the CONTRACTING PARTIES to the GATT. According to the Appellate Body:

> Adopted panel reports are an important part of the GATT *acquis*. They are often considered by subsequent panels. They create legitimate expectations among WTO Members, and, therefore, should be taken into account where they are relevant to any dispute. However, they are not

> binding, except with respect to resolving the particular dispute between the parties to that dispute.

(Page 14) Then, in a footnote, the Appellate Body said, "[i]t is worth noting that the Statute of the International Court of Justice has an explicit provision, Article 59, to the same effect. This has not inhibited the development by that Court (and its predecessor) of a body of case law in which considerable reliance on the value of previous decisions is readily discernible." (Page 14) **On this basis, the Appellate Body considered the Panel's conclusion that adopted panel reports constitute "subsequent practice" and "other decisions" to be in error, but at the same time found that such reports create "legitimate expectations" which should be taken into account.**

Finally, the Appellate Body agreed with the Panel's conclusion that *unadopted* panel reports "have no legal status in the GATT or WTO system since they have not been endorsed through decisions by the CONTRACTING PARTIES to GATT or WTO Members." Likewise, the Appellate Body agreed that "a panel could nevertheless find useful guidance in the reasoning of an unadopted panel report that it considered to be relevant." (Pages 14-15)

Terms of Reference

In the context of its findings related to "directly competitive or substitutable products," the Appellate Body noted that the Panel's conclusions on "like products" and on "directly competitive or substitutable products" "fail to address the full range of alcoholic beverages included in the Panel's Terms of Reference." The Appellate Body "consider[ed] this failure to incorporate into its conclusions all the products referred to in the Terms of Reference ... to be an error of law by the Panel." (Page 26)

SUBSTANTIVE ISSUES

GATT Article III - General

In its appeal, Japan claimed that the Panel's findings that the Liquor Tax Law violates GATT Article III:2, first sentence and second sentence, were in error.

The Appellate Body began with a general examination of Article III, which is titled "National Treatment on Internal Taxation and Regulation," and provides:

> 1. The contracting parties recognize that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products, and internal quantitative regulations requiring the mixture, processing or use of products in specified amounts or proportions, should not be applied to imported or domestic products so as to afford protection to domestic production.
>
> 2. The products of the territory of any contracting party imported into the territory of any other contracting party shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products. Moreover, no contracting party shall otherwise apply internal taxes or other internal charges to imported or domestic products in a manner contrary to the principles set forth in paragraph 1.*

The asterisk to paragraph 2 refers to a note, which provides:

> 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.

(Pages 15-16) The Appellate Body first discussed GATT Article III and the National Treatment obligation generally. It asserted that: "The broad and fundamental purpose of Article III is to avoid protectionism in the application of internal tax and regulatory measures." (Page 16) In this regard, the Appellate Body made clear that the scope of Article III is not limited to products that are the subject of tariff concessions under Article II.

GATT Article III:1

The Appellate Body examined the first paragraph of Article III. It agreed with the Panel that Article III:1 articulates a general principle that internal measures should not be applied so as to afford protection to domestic production, and considered that this general principle informs the rest of Article III. The Appellate Body also agreed with the Panel that there is a distinction between Article III:1, which "contains general principles," and Article III:2, which "provides for specific obligations regarding internal taxes and internal charges." (Pages 17-18)

The Appellate Body added that Article III:1 constitutes part of the context of Article III:2, in the same way that it constitutes part of the context of each of the other paragraphs in Article III. However, the Appellate Body concluded that because of the textual differences in the two sentences, Article III:1 informs the first sentence and the second sentence of Article III:2 in different ways. (Page 18)

GATT Article III:2, first sentence

The Appellate Body first interpreted Article III:2, first sentence. It began its analysis by noting that while Article III:1 informs Article III:2 as a whole, Article III:2, first sentence does not specifically refer to Article III:1. Based on this omission, the Appellate Body concluded that the presence of a "protective application" need not be established as a separate element under the first sentence. The Appellate Body stated that the first sentence of Article III:2 is, in effect, an "expression of" the general principle set forth in Article III:1. (Page 18) In this regard, the Appellate Body observed that the text of Article III:2, first sentence confirms this interpretation. That sentence requires a determination of only two elements: (1) whether the taxed imported and domestic products are "like"; and (2) whether the taxes applied to the imported products are "in excess of" those applied to the like domestic products. If both of these conditions are met, then the measure is inconsistent with Article III:2, first sentence. (Pages 18-19)

The Appellate Body therefore turned to an examination of whether the products at issue in this case are "like." Here, the Appellate Body affirmed the Panel's finding that shochu and vodka are "like" products for the purpose of Article III:2, first sentence. The Appellate Body noted that this analysis should be carried out on a "case-by-case" basis, and referred to the GATT working party report on *Border Tax Adjustments*, in which various criteria were suggested: the product's end-uses in a given market; consumers' tastes and habits, which change from country to country; the product's properties, nature and quality. (Pages 20-21) Moreover, the Appellate Body noted that the concept of "likeness" is "a relative one that evokes the image of an accordion." The accordion of "likeness" "stretches and squeezes" in different places as different provisions of the WTO Agreement are applied. The Appellate Body stated that "[w]e believe that, in Article

III:2, first sentence of the GATT 1994, the accordion of 'likeness' is meant to be narrowly squeezed." (Page 21) The Appellate Body also noted the relevance of tariff classifications. (Page 23) For these reasons, the Appellate Body affirmed the Panel's finding that vodka and shochu are "like." (Page 23)

With regard to whether taxes on imported products are "in excess of" those on "like" domestic products, the Appellate Body agreed with the Panel's legal reasoning and with its conclusion on this issue that *shochu* is taxed in excess of *vodka*. The Appellate Body noted that even the "smallest amount" of excess is too much, and there is no *de minimis* qualification to the standard. (Page 23)

Thus, the Appellate Body found that both required elements under Article III:2, first sentence are present, and therefore upheld the Panel's finding of violation of this provision. (Pages 22-23)

GATT Article III:2, second sentence

In its examination of Article III:2, second sentence, the Appellate Body asserted that Article III:1 plays a more important role here than for Article III:2, first sentence. The Appellate Body noted that unlike Article III:2, first sentence, the text of Article III:2, second sentence specifically invokes Article III:1. Applying Article III:1 along with Article III:2, second sentence, the Appellate Body found that three separate issues must be addressed to determine whether an internal tax measure is inconsistent with Article III:2, second sentence:

> (1) the imported products and the domestic products *are "directly competitive or substitutable products" which are in competition with each other*;
>
> (2) the directly competitive or substitutable imported and domestic products *are "not similarly taxed*;" and
>
> (3) the dissimilar taxation of the directly competitive or substitutable imported domestic products *is "applied ... so as to afford protection to domestic production.*"

(Page 24) The Appellate Body looked at each of these issues in turn.

The Appellate Body first looked at whether the imported and domestic products at issue are "directly competitive or substitutable". The Appellate Body noted that this category is broader than the category of "like" products, but exactly how broad can only be determined on a "case-by-case" basis. The Appellate Body agreed with the Panel's emphasis on the need to look not only at such matters as physical characteristics, common end-uses, and tariff classifications, but also at the "market place," including the elasticity of substitution between products. (Page 25) Finally, the Appellate Body agreed with the Panel's application of this legal standard to the facts of this case, and therefore upheld the Panel's conclusion that "shochu, whisky, brandy, rum, gin, genever, and liqueurs" are "directly competitive or substitutable." The Appellate Body did add, however, that the Panel erred by failing to address all the products specified in its terms of reference. (Page 26)

The Appellate Body then examined whether imported and domestic "directly competitive or substitutable products" are "not similarly taxed." The Appellate Body concluded that the "not similarly taxed" standard is less strict than the "in excess of" standard contained in Article III:2, first sentence. Under the "in excess of" standard, imported and domestic goods must be taxed identically. By contrast, under the "not similarly taxed" standard, the tax burden on imported products must not be heavier, by a more than *de minimis* amount, than on domestic "directly competitive or substitutable" products. The Appellate Body

agreed with the Panel's legal conclusion on this issue, but emphasized that the "not similarly taxed" element is separate from the "so as to afford protection" element, and the Panel's blurring of this distinction was in error. (Pages 26-27)

Finally, the Appellate Body considered whether the "directly competitive or substitutable" products at issue are taxed "so as to afford protection" to domestic products. The Appellate Body stated first that "[t]his is not an issue of intent." Thus, in deciding this issue, the Appellate Body said, it is not necessary to look at the reasons legislators and regulators have for what they do. (Page 27) However, the Appellate Body noted that "[a]lthough it is true that the aim of a measure may not be easily ascertained, nevertheless its protective application can most often be discerned from the design, the architecture, and the revealing structure of a measure." It emphasized that this is an issue of how a measure is applied. Further, the Appellate Body stated, "[t]he very magnitude of the dissimilar taxation may be evidence of its protective application." (Page 29)

Then, although the Appellate Body considered that the Panel erred by blurring the distinction between the "not similarly taxed" element and the "so as to afford protection" element, the Appellate Body upheld the Panel's finding that the Liquor Tax Law had been applied "so as to afford protection." In reaching this conclusion, the Appellate Body quoted with approval the following statement from paragraph 6.35 of the Panel Report:

> ...the combination of customs duties and internal taxation in Japan has the following impact: on the one hand, it makes it difficult for foreign produced shochu to penetrate the Japanese market and, on the other, it does not guarantee equality of competitive conditions between shochu and the rest of "white" and "brown" spirits. Thus, through a combination of high import duties and differentiated internal taxes, Japan manages to "isolate" domestically produced shochu from foreign competition, be it foreign produced shochu or any other of the mentioned white and brown spirits.

(Page 31)

Based on the analysis above, the Appellate Body upheld the Panel's finding that the Liquor Tax Law violates GATT Article III:2, second sentence.

COMMENTARY

For further reading on this case, see:

Steve Charnovitz, "The WTO's *Alcoholic Beverages* Decision," Review of European Community & International Environmental Law, Volume 6, Issue 2, pp. 198-203 (July 1997).

Status of Prior Panel Reports

The Appellate Body's findings on the status of prior panel reports provide useful guidance, but left some questions unanswered. First, in its reasoning on this issue, the Appellate Body did not distinguish between panel reports adopted under the *GATT* and panel reports adopted under the *WTO*. Presumably, such reports have the same status. However, it could be argued that different weight should be given to reports adopted before and after the creation of the WTO because of the difference in the

adoption process, with adopted GATT panel reports, unlike adopted WTO reports, having been explicitly endorsed by each of the Contracting Parties.

Second, the Appellate Body mentioned adopted *panel* reports, but made no reference to adopted *Appellate Body* reports. However, in *U.S. - Shrimp, Article 21.5*, the Appellate Body made clear that its reasoning applied to adopted Appellate Body reports as well. *See DSC for U.S. - Shrimp, Article 21.5 (AB).*

For further reading on this issue, see:

Raj Bhala, *The Myth about Stare Decisis and International Trade Law*, 14 Am. U. Int'l L. Rev. 4 (1999); Raj Bhala, *The Precedent Setters: De Facto Stare Decisis in WTO Adjudication*, 9 Florida State U. J. Transnational L. & Policy 1 (1999); Raj Bhala, *The Power of the Past: Towards De Jure Stare Decisis in WTO Adjudication*, 33 G.W. Int'l L. Rev (3 & 4) (2001).

Adrian Chua, *The Precedential Effect of WTO Panel and Appellate Body Reports*, 11 Leiden Journal of International Law 1 (1998).

David Palmeter and Petros Mavroidis, *Dispute Settlement in the World Trade Organization* (Kluwer Law International, 1999), at 47 (citing Mohamed Shahabuddeen, *Precedent in the World Court* (Grotius, 1996), at 238).

GATT Article III:2

It is often said that GATT Article III is one of the core "non-discrimination" provisions of the GATT. But what exactly is meant by "discrimination"? Because most people have an intuitive understanding of the concept, there is rarely a discussion of its specific elements. However, the approach chosen is of fundamental importance for the application of the principle of non-discrimination, particularly when the measure does not on its face discriminate against imports (note that the measure in this case simply established higher taxes for certain *products*, and did not refer explicitly to the *origin* of the products).

In general terms, there are two elements that can be used to identify discrimination: (1) the *intent* to discriminate (also referred to as "aim" or "purpose"), and (2) the *effect* of discriminating (also referred to as "differential impact"). A finding of discrimination could be based on the existence of *either one* of these two elements, or on the existence of *both* elements. The so-called "aim-and-effects" test applied by the GATT panels in *U.S. - Malt Beverages* and *U.S. - Auto Taxes* reflects an approach under which discrimination, in the sense of GATT Article III, will be found only when the existence of both discriminatory intent and effect is demonstrated.

In the context of GATT Article III:2, the easier of the two elements to understand is intent. In the case at hand, the Panel clearly rejected the use of "aim" under Article III:2, *first sentence*, and the Appellate Body upheld the Panel's finding. In the context of Article III:2, *second sentence*, though, it appears that the Appellate Body has relied on "aim" in a limited way. Specifically, the Appellate Body said that the "protective application" of a measure (through its "design," "architecture," and "revealing structure") can be examined, although the subjective intent of the measure (for example, statements of legislators in passing the law) may not. This issue was further clarified by the Appellate Body in *Chile – Alcohol*, where the "objective" intent, or "statutory purpose," of the measure was examined under this provision. *See DSC for Chile - Alcohol (AB).* The Appellate Body's insistence on an examination of only "objective" intent -- as evidenced by the words of the measure -- has made the rules on this issue fairly clear, although it is likely that evidence regarding statements made by government officials will still be submitted,

in an effort to convince panels and the Appellate Body of the subjective protectionist intent behind a measure.

The issue of discriminatory effect is more complicated. The Panel here did not appear to recognize, or did not explicitly acknowledge anyway, the different approaches that it could have taken with respect to the effect of the measure. One approach, using the facts of this case as an example, would be as follows. For a claim under Article III:2, first sentence, first define the universe of "like products," and separate these products into the different tax categories and into imported and domestic products. Then, if *most* foreign products are subject to the higher tax rates, while *most* domestic products are subject to the lower tax rates, a discriminatory effect exists and Article III:2, first sentence is violated. The following chart, with hypothetical figures inserted, illustrates the existence of discriminatory effect:

Chart 1

Type of Liquor	*Tax rate*	*Imports*	*Domestic*
shochu	low tax	[A] 100,000 (20% of imports)	[C] 3 million (75% of domestic)
vodka	high tax	[B] 400,000 (80% of imports)	[D] 1 million (25% of domestic)

Here, the discriminatory effect is apparent, as 75% of domestic goods are taxed at the low rate, whereas 80% of imports are taxed at the high rate.

On the other hand, there is an alternative approach to the effect of the measure that is not concerned with the proportion of imports and domestic products in each category. Rather, it simply looks at whether *any* imported products are taxed in excess of *any* domestic products. This approach can be illustrated as follows:

Chart 2

Type of Liquor	*Tax rate*	*Imports*	*Domestic*
shochu	low tax	[A] Not examined	[C] Any amount
vodka	high tax	[B] Any amount	[D] Not examined

Under this approach, only cells [B] and [C] are relevant for the analysis. As long as there are *some* imports that are taxed at a high rate and *some* domestic products that are taxed at a low rate, there is a violation of Article III:2, first sentence. This approach appears to have been used by the panel in *EC - Asbestos* in the context of Article III:4. *See DSC for EC - Asbestos (Panel).*

The difference between the two approaches can be illustrated by the following example.

Chart 3

Type of Liquor	*Tax rate*	*Imports*	*Domestic*
shochu	low tax	[A] 200,000 (50% of imports)	[C] 1 million (50% of domestic)
vodka	high tax	[B] 200,000 (50% of imports)	[D] 1 million (50% of domestic)

In this example, a violation of Article III:2, first sentence would *not* be found using the *discriminatory effect* approach, as imports and domestic product are distributed evenly over the two tax categories. By contrast, a violation *would* be found with the alternative approach, because there are *some* imports (in cell [B]) that are taxed at a higher rate than *some* domestic products (in cell [C]).

It is not clear which approach the Panel in this case used. For Article III:2, first sentence, the Panel found that the facts showed that "it is obvious that the taxes imposed on vodka are higher than those imposed on shochu. Accordingly, ... the tax imposed on vodka is in excess of that tax imposed on shochu." (Para. 6.24) The Panel then concluded that by taxing vodka in excess of shochu, Japan is in violation of its obligations under Article III:2, first sentence. (Para. 6.27) The Panel's conclusions on "directly competitive or substitutable products" under Article III:2, second sentence are similar. (Para. 6.33) Thus, the Panel did not make any reference to the *distribution* of imported and domestic products in the two tax categories. Its only finding was that *vodka* was taxed at a higher rate than *shochu*. It did not make a finding as to whether *most vodka* was imported and *most shochu* was domestic. As this was undoubtedly the case, it is possible that the Panel implicitly based its finding on the fact that foreign products (*e.g.*, vodka) were predominantly taxed at a higher rate. However, the Panel did not make any factual findings in support of this proposition, and, furthermore, it explicitly acknowledged that *foreign*-produced shochu exists, as do *domestically*-produced spirits. (Paras. 6.25, 6.35) Because it limited its findings to statements that vodka is taxed in excess of shochu, and that other spirits are not taxed similarly to shochu, it is not clear which approach the Panel was using. On the facts of this case, it probably did not matter which approach the Panel used, as there is little doubt that most domestic products were shochu and most imported products were vodka or other spirits. However, because the Panel did find that there was shochu produced outside of Japan (para. 6.35) and that spirits, whisky and brandy were produced in Japan (para. 6.25), it may have been helpful to conduct an examination of discriminatory effect. The Appellate Body upheld the Panel's conclusions under both provisions without providing much additional guidance.

In *Chile - Alcohol*, a later case, the Appellate Body appears to have relied on a discriminatory effect approach in the context of Article III:2, *second sentence*. *See DSC for Chile - Alcohol (AB)*. However, the approach to be applied under Article III:2, *first sentence* remains unclear.

For further reading on this issue, see:

William J. Davey and Joost Pauwelyn, *MFN Unconditionality: A Legal Analysis of the Concept in View of its Evolution in the GATT/WTO Jurisprudence with Particular Reference to the Issue of "Like Product,"* in *Regulatory Barriers and the Principle of Non-Discrimination in World Trade Law* (Thomas Cottier and Petros C. Mavroidis, eds.), U. of Michigan Press, at 38-41 (2000).

Robert Hudec, "GATT/WTO Constraints on National Regulation: Requiem for an 'Aim and Effects' Test," 32 International Lawyer 3 (1998).

Donald H. Regan, "Regulatory Purpose and 'Like Products' in Article III:4 of the GATT (With Additional Remarks on Article III:2)," 36 Journal of World Trade 3, pp. 443-478 (2002).

Last Update: August 23, 2008

Exhibit 22

Panel Report
Japan - Measures Affecting Consumer Photographic Film and Paper
(WT/DS44/R) / DSR 1998:IV, 1179

Parties
Complainant: U.S.
Respondent: Japan
Third Parties: EC, Mexico

Panelists
Mr. William Rossier (Chairperson),
Mr. Adrian Macey, Mr. Victor Luiz do Prado

Timeline of Dispute
Panel Request: September 20, 1996
Panel Established: October 16, 1996
Panel Composed: December 17, 1996
Interim Report Issued: December 5, 1997
Final Report Issued to Parties: January 30, 1998
Final Report Circulated: March 31, 1998
Adoption: April 22, 1998

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Key Findings

- Japan's distribution "measures," restrictions on large stores, and promotion "measures" do not nullify or impair benefits under GATT Article XXIII:1(b) (non-violation nullification or impairment).
- Japan's distribution "measures" do not result in "less favourable treatment" for imported products under GATT Article III:4.
- Japan is not in violation of the publication requirement in GATT Article X:1.

BACKGROUND

This dispute concerns actions that the United States attributed to the Japanese Government and which, according to the United States, affect the distribution, offering for sale, and internal sale of imported consumer photographic film and paper. At the time of the dispute, four manufacturers supplied Japan's photographic materials market: two domestic companies (Fuji and Konica) and two foreign companies (Kodak and Agfa).

The United States challenged three broad categories of "measures." The Panel explained:

> These three categories of "measures" cover: (1) distribution "measures", which allegedly encourage and facilitate the creation of a market structure for photographic film and paper in which imports are excluded from traditional distribution channels; (2) restrictions on large retail stores, which allegedly restrict the growth of an alternative distribution channel for imported film; and (3) promotion "measures", which allegedly disadvantage imports by restricting the use of sales promotion techniques.

(Para. 10.22) More specifically, the United States challenged the following:

- Distribution "Measures": The United States challenged a variety of decisions and recommendations made by the Japanese Government in the late 1960s and early 1970s. Specifically, the United States argued that while Japan was "liberalizing" its markets and opening them up to foreign investment pursuant to new OECD commitments, the Japanese Government took several "countermeasures" to protect domestic companies, such as Fuji, from the expected influx of imported products. The measures challenged by the United States included the following eight measures that were ultimately examined by the Panel: 1967 JFTC Notification 17 on Premiums to Business; 1967 Cabinet Decision Concerning Liberalization of Inward Direct Investment; 1968 Sixth Interim Report on "Distribution Modernization Outlook and Issues"; 1969 Seventh Interim Report on "Systemization of Distribution Activities"; 1969 Survey Report on Transaction Terms; 1970 Guidelines for Rationalizing Terms of Trade for Photographic Film; 1971 Basic Plan for the Systemization of Distribution; 1975 Manual for Systemization of Distribution by Industry: Camera and Film.

- Restrictions on Large Retail Stores: On this issue, the U.S. claims focused on Japan's Large Scale Retail Store Law ("Large Stores Law"), which was passed on October 1, 1973 and entered into force on March 1, 1974. The Large Stores Law requires retailers intending to open a large store containing floor space over 1,500 square meters, or retailers of that size desiring to open a new store of any size, to notify the proper authority and obtain a permit from the Ministry of International Trade and Industry ("MITI"). In 1979, the Large Stores Law was amended, lowering the threshold size to 500 square meters and dividing jurisdiction between MITI and prefectural governments, depending upon store size. Moreover, in 1982, MITI issued a directive requiring builders to provide local retailers with a "prior explanation" of their plans before submitting an official notification to the government authority. At the time of the dispute, the Large Stores Law required notification, explanation of the store plans to the proper authority, and a waiting period before opening the store,

during which the relevant government authority was entitled to issue recommendations regarding store size and opening date.

- Promotion "Measures": The United States challenged various provisions of, and actions taken under, Japan's Antimonopoly Law and the Premiums Law, both of which are enforced by the Japan Fair Trade Commission ("JFTC"). These laws, and the rulings under them, regulate certain retailers' ability to market their products. In particular, the use of advertising and marketing tools such as cash, goods, and other benefits or prizes to attract customers were limited, and restrictions were placed on misleading or misrepresentative advertising. In this regard, the United States challenged standards enacted by the Fair Trade Promotion Council, which had been established by the national photographic industry in 1982, arguably under JFTC auspices, to regulate the dispatch of employees and the use of promotional money in the photographic industry. This Council also issued standards regarding photographic developing fees in 1984. In 1987, the JFTC, acting pursuant to the Premiums Law, approved a Fair Competition Code Regarding Representations in the Camera and Related Products/Camera Category Retailers Industry which provided rules for store fronts and fliers, standards on dual price offers and use of certain advertising techniques, and prohibitions on misleading representation and loss-leader advertising. The specific eight measures ultimately examined by the Panel were: 1967 JFTC Notification 17 on Premiums to Business; 1967 Cabinet Decision Concerning Liberalization of Inward Direct Investment; 1977 JFTC Notification 5 on Premiums to Consumers; 1981 JFTC Guidance on Dispatched Employees; 1982 Self-regulating Rules Concerning Fairness in Trade with Business; 1982 Establishment of Fair Trade Promotion Council; 1984 Self-Regulating Standards Concerning Display of Processing Fees for Colour Negative Film; 1987 JFTC approval of the Retailers Fair Competition Code and its enforcement body, the Retailers Fair Trade Council.

(Paras. 2.1-52)

The United States claimed that all three categories of measures, individually and in combination, nullify or impair benefits under GATT Article XXIII:1(b) arising from tariff concessions made by Japan on black and white and color consumer photographic film and paper in the Kennedy Round, Tokyo Round and Uruguay Round of multilateral tariff negotiations. It also argued that the distribution "measures" are inconsistent with GATT Article III:4, and that Japan failed to publish certain of these measures in accordance with the requirements contained in GATT Article X:1.

SUMMARY OF PANEL'S FINDINGS

PROCEDURAL AND SYSTEMIC ISSUES

Translation Issues

Because the dispute involved a large volume of documents in the Japanese language that were translated into English, the Panel considered that it was essential that such translations be correct, and that in the event of any disagreement between the parties as to the correct translation, a mechanism be established to resolve the translation problems. Therefore, the Panel, in consultations with the parties, drew up Procedures for the Resolution of Possible Translation Issues, and it appointed two translation experts. (Paras. 1.8-11)

DSU Article 6.2 - Identification of Measures

Japan requested that the panel exclude from its consideration eight separate "measures" mentioned in the first U.S. submission, on the grounds that the United States did not specifically identify these measures in its panel request. (Paras. 10.1-2)

The Panel excluded five of these measures from its consideration, but found that the other three were within its terms of reference. It began by quoting the relevant portion of DSU Article 6.2:

> The request for the establishment of a panel shall be made in writing. It shall indicate whether consultations were held, *identify the specific measures at issue* and provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly. ...

(Para. 10.4, emphasis added by Panel) Both parties agreed that the eight measures identified by Japan were not specifically listed in the U.S. panel request. Therefore, the issue, as stated by the Panel, was whether the DSU Article 6.2 requirement to "identify the specific measures at issue" can still be met even if a measure is not "explicitly described" in the panel request. (Paras. 10.7-8)

Based on the ordinary language of DSU Article 6.2, as confirmed by its context, object and purpose and past panel practice, the Panel found it "clear that a 'measure' not explicitly described in a panel request must have a clear relationship to a 'measure' that is specifically described therein, so that it can be said to be 'included' in the specified 'measure.'" In defining the nature of the requisite "clear relationship," the panel emphasized that there are two key elements -- a "close relationship" and "notice." It elaborated on these requirements as follows: "only if a 'measure' is subsidiary or closely related to a specifically identified 'measure' will notice be adequate." (Paras. 10.7-11)

The Panel then examined each of the eight alleged "measures" at issue under this standard. It first found two notifications issued by the JFTC to have a "close association" with the Premiums Law, which was specifically identified in the U.S. panel request. Specifically, Article 3 of the Premiums Law authorizes the JFTC to complete the specific actions taken in the notifications at issue, thereby giving Japan adequate notice of the U.S. challenge. The Panel described the notification actions as "subsidiary" and "closely related" to the Premiums Law. For similar reasons, the Panel found the Sixth Interim Report of the Industrial Structure Council's Distribution Committee to be "closely related" (although not "subsidiary") to measures listed in the U.S. panel request, and therefore its inclusion within the claims would not cause prejudice to Japan or third parties. In particular, the Panel considered that this report is part of a series of reports, and it observed that the Seventh Report in that series was specifically mentioned in the U.S. panel request. Therefore, because Japan was on notice that the U.S. claims "concerned the reports of the Industrial Structure Council's Distribution Committee," the Panel found there to be a "close relationship" between the Sixth and Seventh Reports. (Paras. 10.12-14)

The Panel then decided to exclude the other five "measures" at issue here. It found two measures to be only "indirectly" related to those measures identified in the U.S. panel request. In particular, the Panel was hesitant to find that reference to Japan's Anti-Monopoly Law alone is sufficient to justify a challenge to *any* action taken pursuant to that law. The Panel observed that the reference to the Anti-Monopoly law in the U.S. panel request was for the purpose of identifying a "measure" dealing with dispatched employees. Yet, the measures taken pursuant to that law which the United States mentioned in its first submission included JFTC notifications on open lotteries and international contract notification requirements. Because these issues are "unrelated" to dispatched employees, the Panel found that they are not properly before the Panel.

The Panel rejected the other three measures as "clearly not related to any 'measure' specifically identified in the panel request." Here, the Panel considered the supposed "close relationships" asserted by the United States to be too tenuous. For example, the Panel found a general reference in one of the identified measures to "positive support and guidance from the government" insufficient to justify the U.S. challenge of specific subsidies provided by the Japan Development Bank and another entity. Similarly, it could find no relationship between any of the measures identified in the request and the JFTC guidance on loss-leader advertising and dumping rules, which was mentioned for the first time in the U.S. response to the Panel's first set of questions. (Paras. 10.15-19)

Sequence of Claims To Be Addressed

The Panel noted that panel proceedings typically deal with violation claims first and then move to claims of non-violation nullification or impairment under GATT Article XXIII:1(b). However, given the parties' focus on the non-violation claims in this case, the Panel decided to address these claims first. (Paras. 10.26-27)

Burden of Proof

The Panel noted the traditional rules governing the burden of proof in WTO disputes, as explained by the Appellate Body in *U.S. - Shirts and Blouses*, under which "it is for the party asserting a fact, claim or defence to bear the burden of providing proof thereof." It also noted that in the non-violation context, under DSU Article 26.1, the United States "bears the burden of providing a detailed justification for its claim in order to establish a presumption that what is claimed is true." Japan would then have to rebut any such presumption. (Paras. 10.28-32)

SUBSTANTIVE ISSUES

GATT Article XXIII:1(b) - Non-Violation Nullification or Impairment

The United States argued, under GATT Article XXIII:1(b), that all three categories of measures, operating individually and in combination, nullify or impair benefits accruing to the United States based on tariff concessions made by Japan on black and white and color film at the end of three successive multilateral rounds of trade negotiations -- the Kennedy Round, the Tokyo Round and the Uruguay Round. (Para. 10.33)

The Panel rejected the U.S. claims. It began its analysis by discussing GATT Article XXIII:1(b), which contains the non-violation remedy. With regard to the underlying purpose of GATT Article XXIII:1(b), the Panel quoted from paragraph 148 of the GATT panel report on *EEC - Oilseeds*:

> The idea underlying [the provisions of Article XXIII:1(b)] is that the improved competitive opportunities that can legitimately be expected from a tariff concession can be frustrated not only by measures proscribed by the General Agreement but also by measures consistent with that Agreement. In order to encourage contracting parties to make tariff concessions they must therefore be given a right of redress when a reciprocal concession is impaired by another contracting party as a result of the application of any measure, whether or not it conflicts with the General Agreement.
>
> . . .

> The Panel considered that the main value of a tariff concession is that it provides an assurance of better market access through improved price competition. Contracting parties negotiate tariff concessions primarily to obtain that advantage. They must therefore be assumed to base their tariff negotiations on the expectation that the price effect of the tariff concessions will not be systematically offset. If no right of redress were given to them in such a case they would be reluctant to make tariff concessions and the General Agreement would no longer be useful as a legal framework for incorporating the results of trade negotiations.

(Para. 10.35) Based on this statement, the Panel observed that "the safeguarding of the process and the results of negotiating reciprocal tariff concessions under Article II is fundamental to the balance of rights and obligations to which all WTO Members subscribe." In addition, while recognizing that the non-violation remedy is an important tool, the Panel also noted that this remedy "should be approached with caution and treated as an exceptional remedy."

With these principles in mind, the Panel considered some general aspects of the application of the non-violation remedy in this dispute. First, while the Panel recognized that traditional GATT non-violation cases had dealt with the introduction or modification of a *subsidy* following the grant of a tariff concession, the Panel stated that it found it appropriate to apply the non-violation remedy to *governmental actions other than subsidies as well*, including a Member's industrial policy. However, in the context of this dispute, the Panel noted that many of the challenged measures are relatively old, a fact which, according to the Panel, makes the presentation of a detailed justification in support of a non-violation claim more difficult. (Paras. 10.35-40)

The Panel next identified the specific elements that are required under the non-violation provision. It first quoted the relevant portion of GATT Article XXIII:1(b), which provides that a member may have recourse to WTO dispute settlement in the following circumstances:

> If any Member should consider that any *benefit* accruing to it directly or indirectly under this Agreement is being *nullified or impaired* ... as the result of ... (b) the *application* by another Member of any *measure*, whether or not it conflicts with the provisions of this Agreement ....

(Para. 10.41, emphasis added by Panel) The Panel considered that, under this provision, a complaining party must demonstrate the following three elements: "(1) application of a measure by a WTO Member; (2) a benefit accruing under the relevant agreement; and (3) nullification or impairment of the benefit as the result of the application of the measure." (Para. 10.41) Before applying these elements to the facts in this case, the Panel considered the proper interpretation of each of these elements in the abstract.

Application of a Measure

In light of the fact that the "measures" challenged by the United States included laws, regulations, policy statements and governmental actions authorizing private activities, the Panel first considered the scope of the term "measure" under GATT Article XXIII:1(b). At the outset, it noted that the ordinary meaning of the term "measure" both encompasses and is broader than "laws and regulations." The issue, therefore, was the following: to what extent does "administrative guidance" given by the Government of Japan rise to the level of a government "measure." The Panel pointed to the GATT panel report in *Japan - Semi-Conductors* for the proposition that, "where administrative guidance creates incentives or disincentives largely dependent upon governmental action for private parties to act in a particular manner, it may be

considered a governmental measure." The Panel noted that another GATT panel, in *Japan - Agricultural Products*, found administrative guidance by the Government of Japan to be a "measure," "because it emanated from the government and was effective in the Japanese context." While these cases dealt with the term "restriction" under GATT Article XI, governing quantitative restrictions, the Panel considered that these principles are applicable to the term "measure" in Article XXIII:1(b) as well. (Paras. 10.43-46)

In the case at hand, under GATT Article XXIII:1(b), the Panel decided upon a "broad definition of the term *measure* ... which considers whether or not a non-binding government action has an effect similar to a binding one." In this regard, it considered that, while the more narrow test stated in *Japan - Semi-Conductors* is certainly applicable under Article XXIII, it should not be the *exclusive* test. Rather, it found that a broader test is supported by the purpose of Article XXIII:1(b), which is to protect the balance of concessions under the GATT. It considered that if the term "measure" is not given a broad scope, then there is a risk that cases of nullification or impairment will not be "redressable." (Paras. 10.47-50)

As to whether *private actions* fall within the scope of a government measure, the Panel noted past GATT practice, which holds that a private action may be deemed governmental "if there is sufficient government involvement with it." The Panel said that it is difficult to establish bright-line rules in this regard and that it would need to examine the actions at issue here on a case-by-case basis. (Paras. 10.52-56)

Finally, the Panel observed that Article XXIII:1(b) is written in the present tense, meaning that the non-violation remedy is limited to "measures that are currently being applied." It distinguished the few GATT cases that had examined measures that had been repealed or withdrawn on the basis that those measures "typically had been applied in the very recent past." It noted the parties' agreement that it is only the *measures being applied,* and not the market structure that might or might not result from the application of those measures, that may form the basis of a non-violation complaint. While Japan argued that many of the measures were no longer in effect, the United States argued that only a couple of the measures had been formally repealed and that, in any event, all of them were being continued through "administrative guidance." In this regard, the Panel noted that the United States bears the burden of demonstrating the existence of such guidance and that the guidance is currently nullifying or impairing benefits. (Paras. 10.57-59)

Benefit Accruing under the GATT

The second element that a complaining party must demonstrate in a non-violation case is the existence of a "benefit accruing." The Panel explained that under past GATT precedent, in all but one case, "the claimed benefit has been that of legitimate expectations of improved market-access opportunities arising out of relevant tariff concessions." Under that precedent, for expectations to be legitimate, "they must take into account all measures of the party making the concession that could have been reasonably anticipated at the time of the concession." (Para. 10.61)

In the case at hand, the Panel noted that this element is complicated by the fact that the United States raised claims with respect to concessions on four different products (black and white film and paper, and color film and paper), stemming from three different rounds of tariff concessions. This added complication raised two additional questions the Panel felt compelled to examine in the context of "benefit accruing": 1) May legitimately expected benefits derive from successive rounds of tariff negotiations? 2) What factors should be considered to determine if a member should have reasonably anticipated measures that allegedly caused nullification or impairment of benefits? (Para. 10.62)

As to the first question, the Panel agreed with the United States that reasonable expectations may continue to exist in successive rounds of GATT Article XXVIII*bis* tariff negotiations. Therefore, it rejected Japan's argument that the most recent tariff concessions replace the older ones. In making this finding, the

Panel first examined the GATT 1994 incorporation clause, which, it explained, "suggests that all protocols relating to tariff concessions, both those predating the Uruguay Round and the Marrakesh Protocol to GATT 1994, are incorporated into GATT 1994 and continue to have legal existence under the WTO Agreement." It considered that, under Article 30 of the Vienna Convention of the Law on Treaties ("VCLT"), only if there were a *conflict* between the earlier protocols and the concessions annexed to the Marrakesh Protocol would the more recent concessions supersede those in earlier rounds. Here, the Panel could find no conflict because the subsequent concessions had progressively improved the expectations of market access; it considered that a conflict would only arise if the subsequent concessions were less favorable than the earlier ones. In this way, expectations of improved market access from each protocol "can be read in harmony." It found support for this approach in past panel reports, including *EEC - Canned Fruit* and *EEC - Oilseeds*, where panels found that reasonable expectations could derive from tariff concessions that had been made prior to the most recent tariff negotiation round. (Paras. 10.63-69)

As to the second question, concerning the factors that determine whether legitimate expectations of a benefit exist, the Panel again turned to past GATT precedent. Based on several GATT cases, the Panel concluded that the United States could only claim impairment of benefits if "the United States could not have reasonably anticipated that such benefits would be offset by the subsequent application of a measure by the Government of Japan." (Paras. 10.72-77) As a starting point, the Panel explained that it would examine each measure to determine whether it was adopted before or after the conclusion of the relevant round of tariff negotiations. If the measure is shown by the United States to have been introduced subsequent to the conclusion of the relevant round of tariff negotiations, then the Panel would consider the United States to have raised a "presumption that it should not be held to have anticipated these measures." Japan could then rebut that presumption, for example, by demonstrating a "clear connection" between that measure and an earlier measure that pre-dates the relevant tariff round. In this regard, the Panel opined that Members should not be held to have reasonably anticipated all GATT-consistent measures, or all measures that are similar to measures in other Member's markets. Rather, reasonable anticipation, according to the Panel, must be assessed on a case-by-case basis. (Paras. 10.78-79)

On the other hand, the Panel explained that if Japan demonstrates that certain measures were introduced prior to the conclusion of the tariff negotiations, then the opposite presumption would arise, namely "that the United States should be held to have anticipated those measures ... ." Recognizing that the knowledge of a measure may not mean knowledge of the specific effect that a measure will have on a particular product, the Panel explained that to overcome the presumption, the United States would have to "clearly demonstrate why initially it could not have reasonably anticipated the effect of an existing measure on the film or paper market and when it did realize the effect." (Para. 10.80)

Finally, the Panel noted the relevant ending dates for each of the tariff negotiation rounds at issue, which it would use in carrying out its analysis of "reasonable anticipation." (Para. 10.81)

Nullification or Impairment of Benefit: Causality

The Panel defined the standard for the third element of a non-violation case, nullification or impairment of the benefit, as follows: "it must be demonstrated that the competitive position of the imported products subject to and benefiting from a relevant market access (tariff) concession is being *upset by* ('nullified or impaired ... as the result of') the application of a measure not reasonably anticipated." It pointed to past GATT precedent as support for this "upsetting the competitive relationship" standard. It later elaborated that the question is not whether *equality* of competitive conditions exists, but rather, "whether the relative conditions of competition which existed between domestic and foreign products as a consequence of the relevant tariff concessions have been upset." (Para. 10.82)

The Panel commented on several other factors affecting its causation analysis. First, as for the degree of causation required between the measure and the upsetting of the competitive relationship, the Panel explained that it would examine whether the measure "has made more than a *de minimis* contribution to nullification or impairment." Next, in response to an argument by Japan that all of the measures are "origin-neutral," the Panel recognized that the concept of *de facto* discrimination is well-developed in GATT/WTO case law and that the United States may show under GATT Article XXIII:1(b) that the measures have a "disparate impact on imports." In addition, the Panel noted that while a showing of intent to cause nullification or impairment is not necessary, nor determinative, it may be a relevant factor. Finally, the Panel did not reject the possibility that the measures may impact on U.S. benefits *in combination* as well as *individually*, but it noted the potential for abuse in the context of causation when measures are examined in this way, and therefore stated that such an analysis "must be approached with caution." (Paras. 10.83-88)

Examination of the Alleged "Measures"

With these standards in mind, the Panel turned to examine the Japanese measures challenged by the United States. The Panel explained that it would examine each alleged measure "in light of each of the three elements of a non-violation claim." For the sake of a complete analysis, the Panel decided to examine each measure under *all* three elements, even if it were to find that a challenged measure fails to meet the requirements of one of the elements. (Para. 10.89)

Distribution "Measures"

The Panel began with the eight distribution "measures" challenged by the United States. In short, the United States argued that these measures were designed to create, and did in fact create, a market structure in which imports are excluded from traditional distribution channels, particularly through vertical integration and single-brand distribution. The measures challenged by the United States were a 1967 Cabinet Decision, a JFTC Notification, and various reports/surveys/manuals or guidelines/plans connected to MITI. (Paras. 10.90-93)

The Panel rejected all of the U.S. challenges against the distribution "measures." The following summary of the Panel's findings covers paragraphs 10.95 through 10.207 of the Panel Report.

With respect to the first element of a non-violation claim, "application of a measure," the Panel concluded that four of the eight "measures" challenged do not constitute "measures" under GATT Article XXIII:1(b). The Panel considered those items, specifically two reports, one survey and one manual, to contain general policy recommendations, often directed at the government rather than trade operators, and lacking in the provision of incentives, disincentives or exhortations. In addition, while the Panel questioned whether many of the eight measures were still in effect given their age, if there had been no formal withdrawal of the "measure" by Japan, the Panel concluded that these measures "*may* still be in effect."

As to the second element, "benefit accruing," because all of the challenged "measures" were imposed or published during the period 1967-1975, for all eight measures, the Panel presumed that the United States *should have reasonably anticipated* those measures with respect to the Tokyo and Uruguay Round tariff concessions, both of which concluded after 1975. While the Panel recognized that the *existence* of a measure does not necessarily entail a full understanding of the potential impact of the measure on a specific product market, the Panel considered that the United States provided no evidence to overcome the Panel's presumption that the United States should be charged with knowledge of those early measures. It found simple assertions by the United States that the measures were "too vague" to understand their full consequences at the time they were imposed insufficient to overcome the presumption. Therefore, the Panel concluded that the United States had no legitimate expectation of a benefit with respect to concessions made during the Tokyo and Uruguay Rounds.

For those measures that were published after, or within days of the conclusion of, the Kennedy Round, the Panel presumed that the United States could *not* have reasonably anticipated these measures. In this regard, it rejected Japan's rebuttal that those later measures were natural outgrowths of Japan's earlier distribution policies. However, because Japan's tariff concessions in the Kennedy Round concerned only black and white film, the Panel concluded that the United States' lack of reasonable anticipation similarly could pertain only to black and white film, a product that is relatively insignificant in the current Japanese market and, based on statistics submitted by Japan and largely unrebutted by the United States, a product for which foreign market share in the Japanese market increased steadily from 1965-1975, the period of concern in the U.S. claims.

With respect to the third element, "impairment and causality," for all eight measures, the Panel concluded that the United States failed to demonstrate nullification or impairment, because it failed to prove a causal link between the measures and the single-brand nature of the distribution system for film and paper in the Japanese market, or between the measures and any alleged upsetting of conditions of competition. In particular, the Panel observed a timing problem in the U.S. claims. Specifically, it observed that the single-brand distribution system being challenged by the United States had evolved in the Japanese market *before*, and independently of, any of the challenged measures. Moreover, the Panel considered that the United States failed to prove that the measures are "directed at promoting vertical integration or single-brand distribution," in light of the fact that the measures were either broad policy statements often directed at the government itself, rather than private operators, or they were general recommendations for the systemization and modernization of the distribution and film sectors in the Japanese economy. The Panel also noted the origin-neutral nature of these measures. Finally, the Panel observed that none of the measures challenged by the United States even mention photographic paper. (Para. 10.208)

For these reasons, the Panel concluded that the United States failed to demonstrate that, under GATT Article XXIII:1(b), the distribution "measures" nullify or impair benefits accruing to the United States.

Restrictions on Large Retail Stores

The Panel next turned to examine the U.S. claims regarding Japan's restrictions on large retail stores, in light of the three required elements under the non-violation remedy. In short, the United States argued that the measures "restricted the growth of an alternative distribution channel for imported film ... ." In this regard, the United States argued that large stores in Japan carry imported products, including film, more frequently than small stores. Moreover, it argued that restrictions on large stores empower oligopolistic distribution structures because large stores can resist manufacturers' attempts to control the manufacturer-wholesale distribution chain. (Paras. 10.209, 212, 222)

In addressing this claim, the Panel examined each element under the non-violation provision in turn. As to the first element, "application of a measure," both parties agreed that the Large Stores Law of 1974 and its 1979 Amendment are measures. They also agreed that the Large Stores Law, as amended, is currently in effect. (Para. 10.214) With respect to the second element, "benefit accruing," the Panel found that the United States could not have reasonably anticipated the Large Stores Law and its amendments as of the conclusion of the Kennedy Round in 1967. In this regard, the Panel rejected Japan's argument that the Large Stores Law was simply a continuation of the policy underlying its earlier Department Store Law of 1956. The Panel rejected such a broad notion of reasonable anticipation and asserted that "it is not sufficient to claim that a *specific* measure should have been anticipated because it is a continuation of a past *general* government policy." The Panel noted, however, that Japan's Kennedy Round concessions are limited to black and white film and paper. (Paras. 10.215-217)

On the other hand, with respect to the Tokyo Round, the Panel concluded that the United States should be "charged with knowledge" of the Large Stores Law and its Amendment. It observed that the United States - Japan bilateral negotiations in the context of the Tokyo Round ended in December 1978, while the Large Stores Law was passed in 1974, and the relevant 1979 Amendment was actually passed in November 1978. Moreover, the overall Tokyo Round negotiations did not end until April 12, 1979. While the Panel recalled its consideration that knowledge of a measure's existence is not necessarily the equivalent of understanding the full potential impact of that measure on a specific product market, the Panel considered insufficient mere assertions by the United States that the Large Stores Law and its Amendment were "opaque" and "informal," such that their potential impact could not be assessed at the time they were imposed. (Paras. 218-219)

Similarly, the Panel concluded that the United States should have reasonably anticipated the measures and their potential impact as of the conclusion of the Uruguay Round. It based this conclusion on the fact that the Large Stores Law and its Amendment predate the conclusion of the Uruguay Round, and the fact that those measures had been the subject of U.S. publications and bilateral discussions with Japan for several years leading up to the Uruguay Round. (Para. 10.220)

The Panel then turned to the third element, "impairment and causality," and found that the United States failed to prove that the Large Stores Law and its amendments and regulations nullified or impaired benefits accruing to the United States under GATT Article XXIII:1(b). At the outset, the Panel made several observations regarding the Japanese measures. First, they are origin-neutral. Second, the objective behind the Large Stores Law is similar to that found in many other countries' laws -- the protection of small stores. Next, the Panel found survey evidence regarding whether large stores are more likely to carry imported film to be inconclusive. Moreover, it noted its "unease" at finding that a law impairs benefits under GATT Article XXIII:1(b) simply because it impacts upon a certain type of store that happens to sell more imported products than other stores. (Paras. 10.225-228)

The Panel also examined the evolution of the Japanese regulation of large stores in order to evaluate whether restrictions on large stores are more hurdensome today than they were in 1967 under the Department Store Law. While certain administrative aspects of the Large Stores Law appeared to the Panel to be tighter than those in 1967, such as notification and explanation requirements, the Panel also noted aspects of the regulation that seemed more liberal, including extended closing times and fewer required store holidays. It also noted that the share of large stores had increased since 1982. Similarly, the Panel observed that the regulation of large stores had been further liberalized since the conclusions of the Tokyo and Uruguay Rounds. (Paras. 10.228-230)

Finally, the United States had argued that the share of large stores would have been even larger, and, therefore, the position of foreign film even better, if it were not for the large store regulations. In response, the Panel questioned whether a Member could have a reasonable expectation of a particular "market evolution." And, even assuming that such a claim could be made under GATT Article XXIII:1(b), the Panel concluded that the United States had not established that it had any such expectation at the end of any of the relevant tariff negotiations.

On this basis, the Panel concluded that the United States failed to demonstrate that the large store regulations nullify or impair benefits accruing to the United States under GATT Article XXIII:1(b).

Promotion "Measures"

The United States challenged eight promotion "measures" that it claimed nullified or impaired benefits accruing to the United States under Article XXIII:1(b). Specifically, the United States argued that

restrictions on sales promotions disadvantaged foreign manufacturers of film and paper who rely on innovative inducements or advertising campaigns to compete. (Paras. 10.234-235) It argued that these measures were taken specifically as "countermeasures" against the expected influx of foreign enterprises due to liberalization of restrictions on foreign investment in Japan. (Para. 10.242)

Again, the Panel examined each measure in light of the three required elements of a non-violation claim. The following paragraphs provide a brief summary of the Panel's findings in Paragraphs 10.239 through 10.348.

As to the first element, "application of a measure," the Panel found that all eight of the challenged "measures" constitute "measures" within the meaning of GATT Article XXIII:1(b). For certain of the older measures, however, the Panel found that they were no longer in effect, or it questioned their current significance in light of later developments. In addition, four of the measures were implemented through guidance or regulations developed by "councils" composed of private actors. Because these councils were established with the approval of government agencies, such as the JFTC, the Panel found that these groups have enough of a connection to the government to render their actions "governmental measures." In addition, it found that the "guidance" given by these councils rose to the level of a "measure" under GATT Article XXIII:1(b) because there was a sufficient likelihood that private parties would act in conformity with them.

With respect to the second element, "benefit accruing," the Panel followed the standards and presumptions developed above with respect to the relative timing of the measures as compared to the end of the relevant rounds of tariff negotiations. Because all eight of the measures were imposed prior to the *Uruguay Round*, the Panel found that the United States could not have any reasonable anticipation of benefits accruing pursuant to tariff concessions given by Japan during that round. The Panel did find, however, that the United States could be presumed to have legitimate expectations with respect to the *Tokyo and/or Kennedy Rounds* for certain of the measures that came into effect after the conclusion of those rounds, or in the case of one of the measures, which was imposed only 9 days before the conclusion of the relevant tariff round.

Finally, the Panel found that all eight "measures" failed to meet the third element of a non-violation claim, "impairment and causality." In short, the Panel found that the measures were tailored to specific forms of promotional activity, such as the overall value of certain premiums, or the dispatch of employees, and therefore left open to all manufacturers a wide variety of alternative forms of promotional activity. Indeed, the evidence showed that when Kodak increased its general advertising expenditures, an activity not regulated by the measures at issue, its market share increased. The Panel also considered that many of the measures were targeted at consumer protection and not at restricting the influx of foreign enterprises, and it noted that the measures were origin-neutral. Moreover, it questioned whether several of the challenged measures even applied to the film and/or paper sectors, given Japan's arguments to the contrary and the fact that the texts of the measures suggested that they were most relevant to the *camera* industry. Across the board, the Panel found that the United States failed to provide any evidence demonstrating how the measures impacted on Kodak or foreign film, or how they upset the conditions of competition.

For these reasons, the Panel concluded that the United States failed to "demonstrate that the promotion measures upset the competitive relationship between imported and domestic film and paper in the Japanese market," and therefore the measures do not nullify or impair benefits under Article XXIII:1(b). (Para. 10.349)

Combined Effects

Finally, the Panel examined the U.S. argument that the three categories of measures -- distribution "measures," restrictions on large stores, and promotion "measures" -- acting "in combination" nullify or impair benefits accruing to the United States under GATT Article XXIII:1(b).

The Panel rejected the U.S. claim. At the outset, the Panel made clear that it considered it possible that individual measures, which do not impair benefits when considered in isolation, could potentially impair those benefits when examined collectively. However, it emphasized that the United States would have to "adduce relevant specific evidence and provide a detailed justification how this evidence supports the theory." With respect to the U.S. evidence, it recalled its findings above that the measures were introduced over several decades and that several of the measures are no longer in effect. It also recalled that the single-brand distribution market structure appeared in the Japanese market for film and paper prior to the introduction of the measures under challenge.

In examining the U.S. claim, the Panel found that the United States failed to offer any persuasive evidence in addition to that already considered by the Panel in the context of examining the measures individually. In particular, the United States failed to explain how each group of measures -- distribution, large store restrictions, promotion -- "operating as a set" adversely impacted the distribution of imported film and paper in Japan, or how all of the measures worked "in concert to upset US market-access expectations." (Paras. 10.353-366)

For these reasons, the Panel considered that the United States failed "to make a detailed showing of the relevance" of how the combined effects of the measures nullified or impaired benefits under Article XXIII:1(b). (Para. 10.366)

GATT Article III:4

The United States also challenged the eight distribution "measures" examined above under GATT Article III:4. (Para. 10.368)

The Panel rejected the U.S. claims. It began by quoting Article III:4:

> The products of the territory of a Member imported into the territory of any other Member 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.

(Para. 10.369) Based on GATT/WTO precedent, the Panel noted that, under this provision, the United States is required to demonstrate the existence of the following elements: "(a) a law, regulation or requirement affecting the internal sale, offering for sale or distribution of imported film or paper; and (b) treatment accorded in respect of the law, regulation or requirement that is less favourable to the imported film or paper than to like products of national origin." Moreover, it noted that Article III:4 must be interpreted taking into account the general principle set forth in GATT Article III:1, although recent Appellate Body precedent makes clear that Article III:4 does *not* require a separate consideration of the "so as to afford protection" standard of Article III:1. Finally, again citing recent Appellate Body precedent, the Panel stated that the mandate of Article III is the following: "Article III obliges Members of the WTO to provide equality of competitive conditions for imported products in relation to domestic products." (Para. 10.370-371)

The Panel first examined whether the "measures" challenged are "laws, regulations or requirements" within the meaning of Article III:4. It recalled its broad construction of the term "measure" in the non-violation context and also noted that past GATT panels had given a similarly broad construction to the phrase "laws, regulations or requirements" under Article III:4. The Panel conceded that "[a] literal reading" of the phrase "could suggest that ["laws, regulations or requirements"] may have a *narrower scope* than the word *measure* in Article XXIII:1(b)." (emphasis added) However, for purposes of its analysis in the case at hand, the Panel decided to "assume ... that they should be interpreted as encompassing a similarly broad range of government action and action by private parties that may be assimilated to government action." In this way, the Panel recalled its findings under Article XXIII:1(b) that only three of the distribution measures cited by the United States -- the 1967 Cabinet Decision, the 1970 Guidelines and the 1971 Basic Plan -- qualified as "measures," such that the Panel would assume that they also constitute "laws, regulations, [or] requirements" under Article III:4. Moreover, "for the sake of completeness of [its] analysis," the Panel also assumed that the other five distribution "measures" under challenge are also "laws, regulations, [or] requirements" under Article III:4. (Para. 10.373-377)

As to the "no less favourable treatment" element, the Panel recalled its findings under GATT Article XXIII:1(b) that the United States had failed to demonstrate that any of the eight distribution "measures" discriminate against imported products. Moreover, the Panel considered that the standard used under Article XXIII:1(b), namely "upsetting the competitive relationship," is not significantly different from the Article III:4 "upsetting effective equality of competitive opportunities." The only real difference is that Article III:4 examines treatment for imported products in general, "whereas the Article XXIII:1(b) standard calls for a comparison of the competitive relationship between foreign and domestic products at two specific points in time," *i.e.*, the time at which the concession was granted and the present time. In the case at hand, the Panel noted that the measures are generally origin-neutral and do not have a "disparate impact" on imported film or paper. Furthermore, it observed that the vertical distribution structure pointed to by the United States was in place prior to the time the challenged "measures" came into effect, and is a common structure around the world. (Para. 10.378-381)

For these reasons, the Panel found that the United States had not proved that the distribution measures are inconsistent with Article III:4. (Para. 10.382)

GATT Article X:1 - Publication

The United States argued that Japan failed, as required by GATT Article X:1, to publish 1) certain enforcement actions by the JFTC and the fair trade councils, and 2) guidance through which MITI officials and other authorities force large store applicants to coordinate their plans with local competitors before submitting a notification, and through which they continue to impose a "prior explanation" requirement. (Para. 10.383)

The Panel rejected the U.S. claim. It first examined the text of Article X:1, which reads:

> Laws, regulations, judicial decisions and *administrative rulings of general application*, made effective by any Member, 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 transfers of payments therefore, 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.*

(Para. 10.384, emphasis added by Panel)

The primary issue for the Panel was whether the administrative rulings challenged by the United States constitute administrative rulings "of general application." The Panel agreed with the panel in *U.S. - Underwear* that the publication requirement in Article X:1 does not extend to "administrative rulings addressed to specific individuals or entities." On the other hand, the Panel considered that the publication requirements extend to "administrative rulings in individual cases where such rulings establish or revise principles or criteria applicable in future cases." (Paras. 10.384-388)

Applying this legal standard to the facts here, the Panel first examined the U.S. claim regarding the JFTC and the fair trade council's enforcement actions. Japan argued that all of the enforcement actions taken by these officials were pursuant to, and consistent with, already published policies. Because the United States was unable to cite any example of a specific unpublished enforcement action that resulted in a policy change, the Panel found that the United States failed to demonstrate the existence of any actions that could be viewed as a violation of Article X:1. (Para. 10.390-393)

Next, the Panel examined actions taken by various fair trade councils under the "Fair Competition Codes." Again, the Panel considered that the United States failed to provide any evidence "as to the nature of any alleged unpublished enforcement actions effecting changes to JFTC or code enforcement criteria." Therefore, the Panel rejected the U.S. claim under Article X:1 with respect to these alleged actions by the fair trade councils.

As to the "measures" taken in the context of the large stores law, the Panel considered that at the national level, the Japanese Government had published a directive formally abolishing the "prior explanation" requirement under the Large Stores Law. While the Panel recognized the existence of anecdotal evidence that such practices were continuing at the sub-national level, the Panel found that the United States failed to show that these actions amount to rules of "general application." That is, the Panel considered that the United States failed to demonstrate that the anecdotal evidence of guidance "amounts to ... rulings which establish or modify criteria applicable in future cases, or is otherwise in the nature of administrative rulings of 'general application.'" (Paras. 10.397-401)

On this basis, the Panel found that the United States failed to prove a violation of Article X:1.

COMMENTARY

For further reading on this case, see:

Sara Dillon, *Fuji-Kodak, the World Trade Organization and the Death of Domestic Political Constituencies*, 8:2 Minnesota Journal of Global Trade 197 (1999).

James Durling, *Anatomy of a Trade Dispute: A Documentary History of the Kodak - Fuji Film Dispute* (Cameron May) (2001).

John Linarelli, *The Role of Dispute Settlement in World Trade Law: Some Lessons from the Kodak-Fuji Dispute*, 31 Law and Policy in Int. Bus. 2 (2000).

Norio Komuro, *Kodak - Fuji Film Dispute and the WTO Panel Ruling*, 32 Journal of World Trade 5, pp. 161-217 (1998).

DSU Article 6.2 - Identification of Measures

The Panel was called upon to decide whether a measure that was not identified in the panel request could still be considered to fall within the Panel's terms of reference. Specifically, in its first submission and in its responses to the Panel's first set of questions, the United States raised claims concerning several measures that it had not identified by name in its panel request.

In determining whether the measures could be considered to fall within its terms of reference despite the fact that they were not specifically mentioned in the panel request, the Panel considered the scope of the DSU Article 6.2 requirement to "identify the specific measures at issue." The Panel focused on two key elements: the concepts of a "close relationship" between the non-identified measure and an identified measure, and "adequate notice." In this way, the Panel examined the connection between an identified measure and the non-identified measure, and considered whether the relationship was close enough so as not to cause prejudice to Japan or third parties. A similar issue arose in *U.S. - Certain EC Products*. *See DSC for U.S. - Certain EC Products (AB)*.

This notion of "prejudice" has evolved over time, and it has become an essential element of an analysis under DSU Article 6.2 when considering whether a Member should have been more detailed in its reference to the measure at issue or the legal claims. For a more detailed discussion of the "prejudice" standard, see *DSC for Korea - Dairy Safeguards (AB)*.

GATT Article X - "Administrative Rulings of General Application"

The Panel elaborated on the approach to the interpretation of the phrase "general application" in GATT Article X endorsed by the Appellate Body in *U.S. - Underwear*. There, the panel and Appellate Body held that the phrase "measure of general application" in Article X:2 does not apply to administrative rulings addressed to specific individuals or specific entities. Later, in *EC - Poultry*, the Appellate Body explained that this standard also applies to the phrase "administrative rulings of general application" contained in Article X:1 (incorporated into Article X:3 by reference). Examining Article X:1 in this case, the Panel clarified this standard, holding that, in its view, Article X:1 *does* apply to administrative rulings in individual matters where these rulings "establish or revise principles applicable in future cases." *See DSC for U.S. - Underwear (AB)* and *DSC for EC - Poultry (AB)*.

GATT Article XXIII:1(b) - Non-Violation Nullification or Impairment

The Panel's assertions that the non-violation remedy should be "approached with caution" and that it is an "exceptional remedy" have been referred to with agreement by subsequent panels and the Appellate Body. In those later cases, *Korea - Government Procurement* and *EC - Asbestos*, the panels and/or Appellate Body similarly rejected the complainant's claims of non-violation nullification or impairment.

The Panel's ultimate decision with respect to the U.S. claims under the non-violation nullification or impairment remedy turned mostly on the facts. In large part, the Panel's findings were based on its conclusion that the United States simply had not proved that the Japanese government measures at issue caused the single-brand distribution system about which the United States complained.

Despite the importance of the specific facts in this case, the Panel's interpretation and explanation of the legal standards for non-violation claims are of relevance for future cases. Although a

comprehensive examination of this remedy is beyond the scope of this analysis, we review below four specific aspects of the Panel's findings.

The first aspect is the burden of proof in non-violation cases. In setting out the burden of proof, the Panel referred to DSU Article 26.1, which requires that parties making non-violation claims must present a "detailed justification" in support of their claims. In its findings, the Panel quoted this language, and referred to GATT cases that had relied on similar standards. During the interim review process, the United States argued that the Panel "misconstrued" this requirement as imposing a "heightened evidentiary standard" in non-violation cases. In fact, the United States argued, it is simply a "pleading requirement," and does not require a "quantum of proof" that is higher than the one applied in violation complaints. In response, the Panel said that it had not applied the "detailed justification" requirement as a "heightened evidentiary standard." It then recalled that the standard it used to determine whether nullification or impairment had occurred was whether the measures made "more than a *de minimis* contribution to nullification or impairment." (Para. 9.5)

In making these statements, the Panel appears to have confused the "detailed justification" standard with the standard of causation. It is true that the causation standard applied by the Panel in the context of determining whether nullification or impairment had occurred was whether the measure made "more than a *de minimis* contribution to nullification or impairment." But the standard of causation to be applied is a different issue than whether the complainant has provided a detailed justification. In fact, these two standards should be applied in combination. Thus, the issue the Panel should have examined is whether the United States provided a *detailed justification* for its claim that the measures caused nullification or impairment *under the appropriate causation standard*. In addition, the U.S. argument that the detailed justification requirement is just a "pleading requirement" appears to be contradicted by other provisions of the DSU. The pleading requirements are clearly laid out in DSU Articles 4 and 6, which establish requirements for consultation and panel requests. Furthermore, GATT negotiating history shows that at least one of the drafters expressed the view that there was, in fact, a heightened evidentiary standard for non-violation cases, that is, a higher burden of proof was required for such cases.

Second, as noted, the causation standard used by the Panel to determine whether nullification or impairment had occurred was whether the measures made "more than a *de minimis* contribution to nullification or impairment." This standard appears to be quite low, especially considering the "exceptional" nature of this remedy, and when compared with other causation standards applied under the WTO Agreement. For instance, in *U.S. - Wheat Gluten Safeguards*, the Appellate Body ruled that the standard of causation to be applied by WTO Member governments in safeguard investigations is whether there is a "genuine and substantial relationship of cause and effect between increased imports and injury." Furthermore, the low standard of causation set by the Panel here is arguably inconsistent with the text of Article XXIII:1(b), which requires that nullification or impairment be "the result of" the measure at issue.

Third, the Panel relied on certain "presumptions" in determining whether particular measures should have been anticipated by the United States. In particular, if measures were introduced *prior* to the end of a negotiating round, the Panel presumed that the United States anticipated these measures as of the time of the concessions made during that round. By contrast, if measures were introduced *subsequent* to the end of a negotiating round, the Panel presumed that the United States could not have anticipated these measures as of the time of the concessions made during that round. It should he noted, however, that the panel in *EC - Asbestos* found that such presumptions were not applicable in the context of that case. (See paragraph 8.291).

Finally, the Panel interpreted "nullification or impairment" in a way that is almost identical to the discrimination standard for "less favourable treatment" under GATT Article III:4. Under Article III:4, "less favourable treatment" exists if a measure "upsets the competitive conditions" between imported and

domestic products. Under Article XXIII:1(b), the Panel found that "nullification or impairment" exists if the "relative conditions of competition which existed between domestic and foreign products as a consequence of the relevant tariff concessions have been upset." Thus, under the Panel's approach, the standard for "nullification or impairment" focuses on anti-discrimination, just as Article III:4 does, and measures causing nullification or impairment under Article XXIII:1(b) would likely be inconsistent with Article III:4 as well.

In its decision in *EC - Asbestos*, the Appellate Body made certain statements, in *obiter dicta*, relating to the non-violation remedy that may be relevant to this issue. In particular, in paragraph 190 of the *Asbestos* report, the Appellate Body twice refers to the concept of "market access" in its discussion of the non-violation remedy. In its ordinary meaning, market access is a broader notion than anti-discrimination, addressing *all barriers* to imports, even if they are not *discriminatory*. For example, a ban on the sale of a product might apply equally to domestic and imported products, and therefore would not be discriminatory, but it nevertheless impedes market access for imports. It is not clear whether the Appellate Body's statements actually express a particular view on this issue. However, an approach to the non-violation remedy based on market access would provide the non-violation remedy with a more logical scope, given that a non-discrimination standard already exists in GATT Article III:4. On the other hand, such an approach might be unacceptably broad in terms of the resulting intrusion into Members' ability to make domestic policy. *See DSC for EC - Asbestos (AB).*

For further reading on this issue, see:

Sung-joon Cho, *GATT Non-Violation Issues in the WTO Framework: Are They the Achilles' Heel of the Dispute Settlement Process?*, 39 Harvard Int. L. J. 2 (1998).

Adrian Chua, *Reasonable Expectations and Non-Violation Complaints in GATT/WTO Jurisprudence*, 32 Journal of World Trade 2 (1998).

Thomas Cottier and Krista Nadakavukaren Schefer, "Non-Violation Complaints in WTO/GATT Dispute Settlement: Past, Present and Future," in *International Trade Law and the GATT/WTO Dispute Settlement System* (Ernst-Ulrich Petersmann, ed.), at 148 (1997).

James P. Durling and Simon N. Lester, *Original Meanings and the Film Dispute: The Drafting History, Textual Evolution, and Application of the Non-Violation Nullification or Impairment Remedy*, 32 The George Washington J. of Int'l L. and Economics 2 (1999).

Ernst-Ulrich Petersmann, *Violation Complaints and Non-Violation Complaints in Public International Trade Law*, 34 German Y.B. Int.'l L. 175 (1991).

Frieder Roessler, "The Concept of Nullification and Impairment in the Legal System of the World Trade Organization," in *International Trade Law and the GATT/WTO Dispute Settlement System* (Ernst-Ulrich Petersmann, ed.), at 125 (1997).

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GATT Article III:4 - Scope of the Term "Requirement"

For ease of analysis, the Panel relied on an assumption that all of the actions which constituted a "measure" for purposes of Article XXIII:1(b) also constituted "laws, regulations or requirements" under GATT Article III. The Panel did note, however, that the ordinary meaning of the terms might suggest that the phrase "laws, regulations or requirements" is actually *narrower* than the term "measure."

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