ELSA MOOT COURT COMPETITION (EMC) ON WTO LAW
CASE 2017-2018

**Borginia– Measures Affecting Trade in Textile Products**
*(Complainant: Syldavia)*

by

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**INTRODUCTION**

The ELSA moot problem for the 2018 edition explores a myriad of issues surrounding the interface between trade and environment. In the present times, climate change and global warming are some of the most serious issues faced by the global commons. There has been a renewed focus on the use of trade as a tool for curbing environmental damage. While the environment has found importance within the WTO legal framework (Article XX of the GATT, for example), there is a need for greater debate on the appropriateness of multilateral rules for addressing environmental concerns that stem from climate change. With the coming into force of the Paris Agreement and the increased attention of climate-friendly production processes, how does the present multilateral legal framework aid or limit this ambition? At the same time, how can such environment–friendly practices pass the often-rigorous tests of WTO law? In this context, this moot problem seeks to discuss certain trade measures including product technical regulations, border-tax measures and subsidies, as they apply to a developing country with a fragile ecology.

The facts in this case revolve around a greenhouse gas reduction program implemented by a WTO Member, namely Borginia. The programme requires textile industry in Borginia to adopt clean production processes while manufacturing cotton fabric. According to the NESI Decision of 2015, only cotton fabrics that adhere to these processes would be eligible to be sold as ‘100% cotton fabric’ in Borginia. Such a specification raises several interesting questions under the Agreement on Technical Barriers to Trade (TBT Agreement) and the GATT 1994. First, the participants would have to address whether the prescribed process and production methods ‘relate’ to the product characteristics – a debate that remains inconclusive and is integral to the scope of the TBT Agreement. Such an analysis is key to the classification of the NESI Decision of 2015 as a ‘technical regulation’ under the TBT Agreement and the consequent application of the TBT Agreement to the moot problem. Second, participants would have to address the consistency of NESI’s Decision of 2015 with Art. 2.1 and 2.2 of the TBT Agreement. The analysis under Art. 2.1 of the TBT Agreement would require participants to evaluate the ‘likeness’ of handloom and powerloom cotton fabric and requires teams to demonstrate that less favourable treatment has been accorded to powerloom imports from Syldavia in Borginia. An evaluation under Art. 2.2 of the TBT Agreement necessitates arguments on the legitimate objectives pursued by the NESI Decision of 2015 and the trade restrictiveness of the measure. Moreover, participants would be required to analyse the measure by applying the relational and comparative test set out by the Appellate Body in *US-Tuna II (Mexico)*. An analysis under Art. 2.2 of the TBT Agreement would highlight the tension between trade rules of non-discrimination and restrictiveness and the legitimate objectives pursued by states including protection of the environment. The moot problem also sets out an international standard on ‘cotton fabric’ (ISO 14666), and teams would have to analyse the consistency of the NESI Decision of 2015 vis-à-vis this international standard. The analysis under Art. 2.4 of the TBT Agreement would require participants to address the meaning of ‘consensus’ in international standard setting bodies, especially in the light of objections by some members – a topic of discomfort for several WTO Members.

The second issue of the moot problem focuses on adoption of a tax measure that aims to incentivise clean production practices and eco-friendly technologies. Borginia has implemented the SOCA Tax measure in the form of ‘border taxes’. The legality of carbon taxes in the form of ‘Border Tax Adjustments’ on products imported from countries, which lack carbon free and eco-friendly production practices, remains largely unresolved in WTO jurisprudence. The key question is whether the SOCA Tax imposed at the border is (i) a charge...
imposed on or in connection with importation (i.e., an “import charge”) under GATT Article II: 1(b), or whether this tax is (ii) equivalent to an internal tax (i.e., an “internal tax”) in respect of the like domestic product. Syldavia would argue that the SOCA Tax is an import charge in terms of Article II:1(b) of the GATT and is above Borginia’s tariff binding on cotton fabric. In response, Borginia would argue that the SOCA Tax is not a measure falling under Article II but Article III of the GATT by virtue of Ad Article III. Alternatively, Borginia would argue that the SOCA Tax is imposed at the border and is equivalent to internal taxes imposed in respect of like domestic products within the meaning of Article II:2 (a) of the GATT, and hence is exempted from the scope of Article II:1(b). An important question in the second issue is whether the carbon emitted in the process or energy consumed in the production, upon which the taxes are levied are border adjustable or not. WTO jurisprudence suggests that inputs, which are not physically incorporated in the product, are not adjustable at the border. Some scholarly articles have argued that greenhouse gas or carbon emission during the production of a product is a by-product or externality and is not incorporated in the product and therefore such tax measures are not WTO compliant.

The final issue of the moot problem concerns a legislation adopted by Borginia to provide financial support to industries that implement clean production processes and measures to reduce emissions of greenhouse gases. The financial support is funded from the SOCA Tax collected by Borginia. This issue in the problem raises several challenging points for participants to address under the Agreement on Subsidies and Countervailing Measures (SCM Agreement). Participants would have to primarily argue whether the financial support provided by Borginia would qualify as an export subsidy under Art. 3.1(a) of the SCM Agreement. More specifically, teams would have to address whether the financial support is contingent in fact on export performance and whether the receipt of financial support is tied or conditional on export of the subsidised product. While this requires participants to engage constructively with the facts of the Moot Problem, the other claims under the SCM Agreement would require participants to confront developing country related issues under the SCM Agreement.

For an analysis of whether the financial support provided by Borginia amounts to a prohibited subsidy under Art. 3.1 (a) of the SCM Agreement, participants would have to address the special and differential treatment of developing country members under Art. 27 of the SCM Agreement. The prohibition on export subsidies does not apply to the countries set out in Annex VII (b) until their gross national product (GNP) per capita reaches US$ 1000 for three consecutive years. Even for Annex VII (b) countries, the flexibility to offer export subsidies does not exist for those products that have reached export competitiveness. Upon graduating from Annex VII (b), a Member would be governed by the provisions of Art. 27.2 of the SCM Agreement, which requires developing countries to phase out export subsidies within 8 years. The participants can utilise the drafting ambiguity in Art. 27 of the SCM Agreement – with Borginia arguing that the period of 8 years applies from the time of graduation from Annex VII (b) and Syldavia contending that such a period would apply from the date of entry into force of the WTO Agreement.

As set out above, even for countries included in Annex VII (b) of the SCM Agreement, export subsidies cannot be provided for products that have reached export competitiveness. The test for such export competitiveness is whether the developing country Members’ exports of that product have reached a share of at least 3.25% in world trade of that product for 2 consecutive calendar years (Art. 27.6, SCM Agreement). The computation of export competitiveness has raised important interpretative questions, particularly between India and the United States. Art. 27.6 of the SCM Agreement is ambiguous on whether products should be defined at the
‘section’ (group of chapters) or ‘heading’ (four-digit tariff level) and instead uses the term ‘section heading’. Participants would be required to argue on the level of the HS Nomenclature level that export competitiveness would have to be determined at. Teams would be required to focus on the differences in the French, Spanish and English texts of the SCM Agreement and utilise the interpretative tools set out in the Vienna Convention on the Law of Treaties (VCLT) to frame arguments. Further, the Complainant would have to argue that ‘product’ is defined at a six-digit level in other WTO agreements and therefore, the same should find bearing in the present case.

Syldavia’s request for the establishment of a panel to the DSB, contained the following legal claims:

- NESI’s decision in 2015 that only “100% handloom cotton fabric” can be marketed as “Cotton Fabric” in Borginia is a ‘technical regulation’ within the meaning of Annex 1.1 to the TBT Agreement 1994 and is inconsistent with Articles 2.1, 2.2 and 2.4 of the TBT Agreement 1994, as well as with Article III:4 of the GATT 1994;
- The tax levied on the imported cotton fabric in excess of other applicable custom duties is inconsistent with Articles II:1 (a) and (b), II: 2(a) and III:2 of the GATT 1994; and
- The allocation of funds from the Textile Technology Upgrade Fund Scheme to the textile units situated in the TEPZs in Borginia is inconsistent with Borginia’s obligations under Articles 3.1(a), 27.4 and 27.5 of the SCM Agreement 1994.
**WEIGHT OF CLAIMS**

The following table is based on the score sheet for the written submissions and indicates the relative weight that the panel may wish to give to the different claims and their elements. The weight is based on the novelty and complexity of claims.

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<th>1. TBT Article 2.1</th>
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<td>• Technical Regulation – 3 points</td>
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<td>• Likeness – 1 point</td>
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<td>• Less favourable treatment – 1 point</td>
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<td>• Legitimate objective – 1 point</td>
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<td>• Not more trade restrictive than necessary</td>
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<td>i) Relative Analysis – 1 point</td>
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<td>ii) Comparative Analysis – 1 point</td>
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<th>3. TBT Article 2.4</th>
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<td>• International standard – 3 points</td>
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<td>• Relevance – 1 point</td>
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<td>• “ineffective or inappropriate means” of fulfillment of “legitimate objectives” – 1 point</td>
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<th>4. GATT Article III:4</th>
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<td>• Likeness – 1 point</td>
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<td>• Less Favourable Treatment – 1 point</td>
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<th>5. GATT Article II:1(a) and (b)</th>
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<td>• Ordinary Customs Duties – 2 points</td>
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<td>• Less Favourable Treatment – 1 point</td>
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<th>6. GATT Article II:2(a) and Article III:2</th>
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<td>• Equivalence – 1.5 points</td>
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<td>• Like products under Article III:2 – 2 points</td>
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<th>7. GATT Article XX – 2 points</th>
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<th>8. SCM Article 3.1(a)</th>
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<td>• Specific Subsidy in terms of Articles 1 and 2 of the SCM Agreement – 1.5 points</td>
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<td>• Contingency of that subsidy upon export performance – 1 point</td>
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<th>9. SCM Article 27.4 and 27.5</th>
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<td>• Annex VII and Export Competitiveness– 1.5 points</td>
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<td>• Phasing out – 1 point</td>
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LEGAL CLAIMS

Note: The written memoranda need not follow precisely the same structure as this Bench Memorandum. Teams may choose to organize their arguments in any particular order.

A. NESI’S DECISION OF 2015 THAT ONLY “100% HANDLOOM COTTON FABRIC” CAN BE MARKETED AS “COTTON FABRIC” IN BORGINIA IS A “TECHNICAL REGULATION” WITHIN THE MEANING OF ANNEX 1.1 TO THE TBT AGREEMENT 1994 AND IS INCONSISTENT WITH ARTICLES 2.1, 2.2 AND 2.4 OF THE TBT AGREEMENT 1994, AS WELL AS WITH ARTICLE III:4 OF THE GATT 1994

I. WHETHER NESI’S DECISION OF 2015 CONSTITUTES A “TECHNICAL REGULATION”?

a. LEGAL PROVISIONS

Annex 1 to the TBT Agreement provides, in relevant part:

1. Technical regulation

Document which lays down product characteristics or their related processes and production methods, including the applicable administrative provisions, with which compliance is mandatory. It may also include or deal exclusively with terminology, symbols, packaging, marking or labelling requirements as they apply to a product, process or production method.

b. RELEVANT JURISPRUDENCE

The determination of whether a measure constitutes a technical regulation “must be made in light of the characteristics of the measure at issue and the circumstances of the case” (US – Tuna II (Mexico), Appellate Body Report, ¶188). The WTO Appellate Body [hereinafter “AB”] has interpreted the definition of a “technical regulation” in EC — Asbestos (EC-Asbestos (Canada), Appellate Body Report, ¶67) and EC — Sardines (EC-Sardines (Peru), Appellate Body Report, ¶175). In these cases, the AB established a three-tier test for determining whether a measure is a “technical regulation” under the TBT Agreement:

1. First, the document must apply to an identifiable product or group of products. The identifiable product or group of products need not, however, be expressly identified in the document.
2. Second, the document must lay down one or more characteristics of the product. These product characteristics may be intrinsic, or they may be related to the product. They may be prescribed or imposed in either a positive or a negative form.
3. Third, compliance with the product characteristics must be (directly or indirectly) mandatory.

In EC — Asbestos, the AB stated that “the heart of the definition of a ‘technical regulation’ is that a ‘document’ must ‘lay down’ — that is, set forth, stipulate or provide — ‘product characteristics’”. (EC-Asbestos (Canada), Appellate Body Report, ¶68) The term “product characteristics” in Annex 1.1 of the TBT Agreement should be interpreted in accordance with its ordinary meaning:
"The word ‘characteristic’ has a number of synonyms that are helpful in understanding the ordinary meaning of that word, in this context. Thus, the ‘characteristics’ of a product include, in our view, any objectively definable ‘features’, ‘qualities’, ‘attributes’, or other ‘distinguishing mark’ of a product. Such ‘characteristics’ might relate, inter alia, to a product’s composition, size, shape, color, texture, hardness, tensile strength, flammability, conductivity, density, or viscosity. In the definition of a ‘technical regulation’ in Annex 1.1, the TBT Agreement itself gives certain examples of ‘product characteristics’ — ‘terminology, symbols, packaging, marking or labelling requirements’. These examples indicate that ‘product characteristics’ include, not only features and qualities intrinsic to the product itself, but also related ‘characteristics’, such as the means of identification, the presentation and the appearance of a product. (EC-Asbestos (Canada), Appellate Body Report, ¶¶67-69)”

In EC — Sardines, the AB emphasized that product characteristics include not only “features and qualities intrinsic to the product”, but also those that are related to it, such as means of identification (EC — Sardines (Peru), Appellate Body Report, ¶189). The AB in EC — Seal Products noted that the definition of a technical regulation also provides that a regulation may prescribe “product characteristics or their related processes and production methods” (EC — Seal Products (Norway), Appellate Body Report, ¶ 5.12). In order to determine whether a measure lays down related PPMs, a panel thus will have to examine whether the processes and production methods prescribed by the measure have a sufficient nexus to the characteristics of a product in order to be considered related to those characteristics. The AB in US — Tuna II (Mexico) held that labelling schemes depicting how tuna are harvested based on a npr-PPM criteria (i.e., dolphin-safe) fell within the definition of technical regulation under the second sentence of Annex 1.1 of the TBT Agreement. (US — Tuna II (Mexico), Appellate Body Report, ¶199). In US — COOL, the measure (imposing a requirement on retailers selling beef and pork to label the origin of such products) was held to be a technical regulation under the second sentence of Annex 1.1 of the TBT Agreement (US — COOL, Appellate Body Report, ¶268). In particular, in US—Tuna II, the United States had not appealed the Panel’s findings that the tuna (i.e., tuna caught by setting on dolphin versus tuna harvested through dolphin-friendly methods) were “like”.

While the first sentence of Annex 1.1 refers to the terms “their related” processes and production methods, these terms are conspicuous by their absence in the second sentence. While there is a view that these two sentences should be read together (Mexico’s proposal, TBT/M/40), there are contrasting views that npr-PPMs may be applicable to labelling requirements. Moreover, the AB in US-Tuna II noted that, “Article 2.1 should not be read therefore to mean that any distinctions, in particular ones that are based exclusively on particular product characteristics or on particular processes and production methods, would per se constitute “less favourable treatment” within the meaning of Article 2.1.” (US — Tuna II (Mexico), Appellate Body Report, ¶211). According to AB jurisprudence, it may be possible to argue that products can be differentiated on the basis of processes and production methods, in the context of Article 2.1 of the TBT Agreement.
c. **ARGUMENTS FOR SYLDAVIA**

Syldavia could argue that NESI’s Decision of 2015 is a “technical regulation” within the meaning of Annex 1.1 to the TBT Agreement on the following basis:

- **Document**: NESI’s Decision of 2015 is a “document”.
- **Product Characteristics**: NESI’s Decision of 2015 lays down product characteristics as it defines the conditions for a fabric to be marketed as “Cotton Fabric” in Borginia. It lays down product characteristics in the negative form.
- **Related Processes and Production Methods**: Syldavia could argue that the requirements for the manufacture of cotton fabric as set out in NESI’s Decision of 2015 are production and processes methods for the purposes of the TBT Agreement, as set out by the Appellate Body. Syldavia could also show that the processes of knitting, weaving and spinning through hand and without the use of electricity, in the entire production process from fibre to fabric, could affect the final product characteristics (for instance, the texture and finesse is of the cotton fabric varies in both handloom and powerloom production processes) and, therefore, there is a sufficient nexus between the PPMs and the final product characteristics. (See, *EC- Seal Products*, Appellate Body Report, ¶ 5.12).
- **Mandatory**: NESI’s 2015 decision is mandatory. Without meeting the criteria set out in the NESI decision, especially the requirements related to “use of power”, a domestic or foreign party cannot sell fabric as “cotton fabric”.
- **In addition**, Syldavia could also argue that the NESI decision of 2015 is a labelling requirement within the meaning of the second sentence of Annex 1.1 of the TBT Agreement. Syldavia could contend that the second sentence of Annex 1.1 incorporates a definition of technical regulation where even non-product related PPMs (npr-PPMs) could be subject to labelling requirements. The absence of the term ‘related’ in the second sentence of Annex I lends credence to this view. The inclusion of the word “also” at the beginning of the second sentence supports the view that second sentence of Annex 1.1 is “additional to the first and not merely illustrative”. (See A. Appleton, *US- Shrimp, 20 Years On, in WTO Dispute Settlement at Twenty: Insiders’ Reflections on India’s Participation*, Springer, 2016; Gracia Marin Duran, *NTBs and the WTO Agreements on Technical Barriers to Trade: The Case of PPM-Based Measures Following US- Tuna II and EC- Seal Products* in C. Hermann et al. (eds.), *European Yearbook of International Law, 2015*. pp 99-102). According to this view, labelling requirements based on both product related- PPMs and non-product PPMs are covered in Annex 1.1 of the TBT Agreement.

d. **ARGUMENTS FOR BORGINIA**

It may be difficult for Borginia to argue that the NESI’s Decision of 2015 is not a “document” and compliance is not mandatory in order to sell or market the product as “cotton fabric”. However, Borginia may wish to contest that the measure is a “technical regulation” based on the following reasoning:

- **Product characteristics and related PPMs**: Borginia could argue that the NESI’s Decision of 2015 does not lay down any “objective features, qualities or ‘characteristics’” (EC-Asbestos (Canada), Appellate Body Report, ¶72). NESI’s Decision of 2015 only defined the production processes which are not intrinsically
related to the product per se. This view is reinforced by the AB finding in EC-Seals. In other words, the process and production method (PPM) involved in this case is not “related to” or has “sufficient nexus” with the product’s “characteristics” and, therefore, would not qualify as a ‘technical regulation’ within the meaning of Annex 1.1 of the TBT Agreement. The measure could only qualify as a “non-product related process and production method”. Additionally, Borginia could argue that NESI’s Decision of 2015 is not a labelling requirement but is merely a regulation specifying the production methods to be used in order to market 100% handloom cotton fabrics as cotton fabrics in Borginia. Borginia could argue that there is nothing to state that the cotton fabric sold as “Cotton Fabric” in Borginia i.e., 100% handloom cotton fabric, must be labelled. Borginia could also attempt to differentiate the facts of this moot problem from US-Tuna II and US-COOL. Therefore, NESI’s Decision of 2015 should not be regarded as a technical regulation.

- Assuming that NESI’s decision of 2015 is a labelling requirement, Borginia could argue that it does not meet the requirements of the second sentence of Annex I.1 of the TBT Agreement. Borginia could contest the view that all labelling requirements could come within the scope of Annex I.1 of the TBT Agreement. In particular, Borginia could stress on the terms “as they apply” which appear in the second sentence. Based on this reasoning, the concerned ‘labelling’ requirement that the product should be produced “without using electricity or machines” does not provide details on the “product characteristics”. Borginia should follow an approach that requires an integrated reading of Annex 1.1, i.e., reading the second sentence as a continuation of the first sentence. The word ‘related’ should be interpreted to mean ‘having a physical impact on the end product’. This view finds support in the negotiating history of the TBT Agreement. For instance, during the Uruguay Round, Mexico introduced proposals that sought to exclude PPMs unrelated to the characteristics of a product from the coverage of the TBT Agreement. (See Note by WTO Secretariat (1995), ¶¶ 146, 147). Therefore, Borginia could argue that the measure would not qualify as a ‘technical regulation’ and that the TBT Agreement is not applicable.

II. WHETHER NESI’S DECISION OF 2015 IS INCONSISTENT WITH ARTICLES 2.1, 2.2 AND 2.4 OF THE TBT AGREEMENT?

a. LEGAL PROVISION

Article 2 of the TBT Agreement provides, in relevant part:

> Preparation, Adoption and Application of Technical Regulations by Central Government Bodies

> With respect to their central government bodies:

> 2.1 Members shall ensure that in respect of technical regulations, products imported from the territory of any Member shall be accorded treatment no less favourable than that accorded to like products of

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1 The Appellate Body noted: “We see no basis in the text of Annex 1.1, or in prior Appellate Body reports, to suggest that the identity of the hunter, the type of hunt, or the purpose of the hunt could be viewed as product characteristics.” (¶ 5.45).
national origin and to like products originating in any other country.

2.2 Members shall ensure that technical regulations are not prepared, adopted or applied with a view to or with the effect of creating unnecessary obstacles to international trade. For this purpose, technical regulations shall not be more trade-restrictive than necessary to fulfil a legitimate objective, taking account of the risks non-fulfilment would create. Such legitimate objectives are, inter alia: national security requirements; the prevention of deceptive practices; protection of human health or safety, animal or plant life or health, or the environment. In assessing such risks, relevant elements of consideration are, inter alia: available scientific and technical information, related processing technology or intended end-uses of products.

2.4 Where technical regulations are required and relevant international standards exist or their completion is imminent, Members shall use them, or the relevant parts of them, as a basis for their technical regulations except when such international standards or relevant parts would be an ineffective or inappropriate means for the fulfilment of the legitimate objectives pursued, for instance because of fundamental climatic or geographical factors or fundamental technological problems.

Annex 1.2 to the TBT Agreement defines a “standard” as follows:

2. Standard

Document approved by a recognized body, that provides, for common and repeated use, rules, guidelines or characteristics for products or related processes and production methods, with which compliance is not mandatory. It may also include or deal exclusively with terminology, symbols, packaging, marking or labelling requirements as they apply to a product, process or production method.

Explanatory note

The terms as defined in ISO/IEC Guide 2 cover products, processes and services. This Agreement deals only with technical regulations, standards and conformity assessment procedures related to products or processes and production methods. Standards as defined by ISO/IEC Guide 2 may be mandatory or voluntary. For the purpose of this Agreement standards are defined as voluntary and technical regulations as mandatory documents. Standards prepared by the international standardization community are based on consensus. This Agreement covers also documents that are not based on consensus.

b. RELEVANT JURISPRUDENCE

i. Article 2.1 of the TBT Agreement
Article 2.1 of the TBT Agreement contains a national treatment and a mostfavoured nation treatment obligation. For a violation of Article 2.1 of the TBT Agreement to be established, following three elements must be satisfied (US – Tuna II (Mexico), Appellate Body Report, ¶202): -

1. the measure must be a technical regulation;
2. the imported products must be like the domestic products and the products of other origins; and
3. the treatment accorded to imported products must be less favourable than that accorded to like domestic products and like products from other origins.

**Like Products and Relationship between Art. 2.1 of the TBT and Art. III:4 of the GATT (Please refer to GATT III analysis on Pages 24 and 34)**

The AB in *US – Clove Cigarettes* noted that the interpretation of the concept of “likeness” in Article 2.1 has to be based on the text of that provision as read in the context of the TBT Agreement and of Article III: 4 of the GATT, which also contains a similarly worded national treatment obligation that applies to laws, regulations, and requirements including technical regulations. In the light of this context and of the object and purpose of the TBT Agreement, as expressed in its preamble, the AB considered that the determination of likeness under Article 2.1 of the TBT Agreement, as well as under Article III:4 of the GATT, is a determination about the nature and extent of a competitive relationship between and among the products at issue. To the extent that they are relevant to the examination of certain “likeness” criteria and are reflected in the products’ competitive relationship, regulatory concerns underlying technical regulations may play a role in the determination of likeness. (*US-Clove Cigarettes (Indonesia)*, Appellate Body Report, ¶136)

Likeness of products is usually to be determined on the basis of four criteria, namely: (i) bearing in mind the physical characteristics of the products, (ii) their end uses, (iii) the consumer tastes and preferences in relation to the products, and (iv) their tariff classification (Report of the Working Party, Border Tax Adjustments, ¶18). However, this is not an exhaustive list. In this context, it was stated by the AB in *EC-Asbestos* that “the adoption of a particular framework to aid in the examination of evidence does not dissolve the duty or the need to examine, in each case, all of the pertinent evidence.” (*EC-Asbestos (Canada)*, Appellate Body Report, ¶102)

- **Physical Characteristics**- “Characteristics” of a product are objectively definable features, qualities, attributes or other distinguishing marks that a product encompasses (*EC-Asbestos (Canada)*, Appellate Body Report, ¶67).
- **End-Use**- Capability of performing a specific function plays a pivotal role in determining the product’s end use (*US-Clove Cigarettes (Indonesia)*, Appellate Body Report, ¶131).
- **Consumer Taste and Habits**- The consumer tastes and preferences are influenced by the risks associated with the products. (*EC-Asbestos (Canada)*, Appellate Body Report, ¶47)
- **Tariff Classification** - In this regard, it may be apposite to recall the findings of the AB in *Philippines- Distilled Spirits*：“...[T]ariff classification can be a helpful sign of similarity only if it is sufficiently detailed. We do not consider that HS heading 2208, which groups together all distilled spirits, as well as other liquors and unfavoured neutral spirits for human consumption or industrial purposes, constitutes a tariff classification that is sufficiently detailed to provide an indication of “likeness”.”
**Less Favourable Treatment**

A technical regulation is said to accord less favourable treatment to imported products if it modifies conditions of competition in the relevant market to the detriment of imported products or denies effective equality of opportunities for imported products and if it does not stem exclusively from a legitimate regulatory distinction (*US-Clove Cigarettes (Indonesia)*, Appellate Body Report, ¶¶ 166, 176, 182; *US-Tuna - II (Mexico)*, Appellate Body Report, ¶¶ 214, 298). The “design, architecture, revealing structure, operation and application” of the regulation should show that the detriment to the competitive opportunities of the imported products reflects discrimination against the imports (*US-Clove Cigarettes (Indonesia)*, Appellate Body Report, ¶ 182).

In the GATT context, a less favourable treatment of imported products contrary to Articles I and III can be justified by a responding Member under the exceptions in Article XX. In the TBT Agreement, where there is no Article XX type exception provision, the AB has determined that the existence of “less favourable treatment” is not merely based on whether there is any detrimental impact of the measure on imports, but also on whether this impact stems from “legitimate regulatory distinctions”. Accordingly, under the TBT Agreement, a detrimental impact arising from “legitimate regulatory distinctions” would not amount to “less favourable treatment” in the first place.

Instead, a panel must further analyse whether the detrimental impact on imports stems exclusively from a legitimate regulatory distinction rather than reflecting discrimination against the group of imported products.” To clarify, in *US-Clove Cigarettes* the AB also noted that “the existence of a detrimental impact on competitive opportunities for the group of imported vis-à-vis the group of domestic like products is not dispositive of less favourable treatment under Article 2.1 of TBT. (*US-Clove Cigarettes (Indonesia)*, Appellate Body Report, ¶182).

In the trilogy of cases applying TBT Article 2.1, the overall objectives that the respondent (United States) had identified for each measure were ultimately accepted as legitimate. Nonetheless, in each case, the US regulations were determined to be inconsistent with Article 2.1 of the TBT Agreement in view of the fact that their detrimental impacts did not stem exclusively from legitimate regulatory distinctions.

c. **ARGUMENTS FOR SYLDAVIA**

**Like Products:** Syldavia could argue that the cotton fabric manufactured in a powerloom does not bear any objectively definable features, which would distinguish it from a handloom cotton fabric. Further, the end use of both the powerloom fabric and handloom fabric are the same. Moreover, both powerloom and handloom are classified under the same Harmonised System subheading (Table B, page 6, Moot Problem). Syldavia could argue that the imported product competes with all other cotton fabrics in the same market, in terms of the physical characteristics, end use, consumers’ preferences and tariff classification.

Note: While Syldavia has argued, for the purposes of Article 1.1 of the TBT Agreement that PPMs would impact product characteristics, this may not be of relevance for the ‘likeness’ analysis under Article 2.1 of the TBT Agreement. Since the analysis of ‘likeness’ under Article 2.1 of the TBT Agreement involves a determination of the competitive relationship between
the products in question, Syldavia could argue that handloom and powerloom cotton have similar physical characteristics and are competing products.

**Less favourable treatment:** Syldavia can argue that the design of the NESI’s Decision of 2015 is such that it discriminates against the imported products from Syldavia, as cotton fabric in Syldavia are predominantly manufactured in powerlooms. On the other hand, the textile industry in Borginia specialises in handloom products (¶1.2, Moot Problem). The measure has a detrimental impact on the competitive opportunities of cotton fabrics manufactured in the powerlooms in Syldavia since such products cannot be marketed as ‘cotton fabrics’. Consequently, Syldavia’s cotton fabric exports to Borginia have significantly declined.

d. **ARGUMENTS FOR BORGINIA**

**Like Products:** Borginia can argue that the physical characteristics of both fabrics are different. In Borginia, handloom cotton fabric has a traditional cultural significance. The Borginian consumer taste and preferences reflect that they are concerned about the environmental risks posed by the powerloom fabric production.

Borginia can argue that the separate tariff classification provided in their domestic Goods and Services Tax (Table B in the moot problem) is indicative of the fact that handloom fabrics are different from powerloom fabrics.

In short, Borginia’s tariff classification in the Goods and Services Tax, which provides a more detailed classification of cotton fabrics, could indicate that imported and domestic fabrics are not “like” from a tariff classification perspective. But according to the AB in EC-Asbestos, the four general criteria in assessing likeness: [(i) the properties, nature and quality of the products; (ii) the end-uses of the products; (iii) consumers’ tastes and habits – more comprehensively termed consumers’ perceptions and behaviour – in respect of the products; and (iv) the tariff classification of the products] must be discussed and evaluated. (EC-Asbestos (Canada), Appellate Body Report, ¶101)

**Less favourable treatment:** Borginia may rely on the AB report in US-Clive Cigarettes wherein the AB noted that “the existence of a detrimental impact on competitive opportunities for the group of imported vis-a-vis the group of domestic like products is not dispositive of less favourable treatment under Article 2.1 of TBT.” (US-Clive Cigarettes (Indonesia), Appellate Body Report, ¶182) In the present case, Borginia could concede that there is a detrimental impact on imports of powerloom cotton from Syldavia to Borginia pursuant to the NESI Decision of 2015 (See Table A, Annex 2, Moot Problem). However, Borginia could argue that the detrimental impact on imported like products stems exclusively from “legitimate regulatory distinctions”.

The term “legitimate distinction” was interpreted as requiring an examination of whether the measure was pursued in an even-handed manner or whether it created discrimination. Under this interpretation, it seems that the specific detrimental impact, not the overall policy at its base, must be justified if the regulatory distinction is to be legitimate, i.e., designed and applied in a balanced manner.

In EC-Seals the Panel noted that:

“We recall the Appellate Body’s explanation that the "legitimacy" of the regulatory distinctions drawn by a measure must be analysed in light of the objective of the
measure and based on inter alia the particular circumstances of the dispute, including the measure’s design, architecture, structure, operation, and application of the measure. The Appellate Body further explained that where a regulatory distinction is not designed and applied in an even-handed manner — because, for example, it is designed or applied in a manner that constitutes a means of arbitrary or unjustifiable discrimination — that distinction cannot be considered "legitimate."” (EC-Seals, Panel Report, Para. 7.257)

In determining whether this discrimination is necessary, a panel may look at the importance or value of the objectives, its contribution, trade restrictiveness and the availability of reasonable alternatives, etc. The absence of a rationale explaining or justifying the regulatory distinction could play a role in finding a lack of even-handedness in how the distinction was designed and applied. (US- Clove Cigarettes (Indonesia), Appellate Body Report, ¶¶ 182, 215; US- COOL (Canada), Appellate Body Report, ¶¶271, 272). In US- Clove Cigarettes, the measure at issue pursued the legitimate public health objective of reducing youth smoking. However, the exclusion of (mainly domestic) menthol cigarettes from the scope of the measure created a discriminatory impact in favour of menthol cigarettes—a distinction between the two types of cigarettes which did not involve a legitimate policy justification.

Specifically, in this case, it needs to be examined whether the distinction between ‘powerloom’ cotton fabric (cannot be marketed as ‘cotton fabric’) and ‘handloom’ cotton fabric (may be marketed as ‘cotton fabric’) is arbitrary or not rationally connected to the objectives of the LFN Action Plan (which relate to the promotion of environment-friendly production practices in various industries in Borginia); at the same time, it could be argued that such a regulatory distinction could encourage carbon neutral production means in an important industrial sector.

ii. Article 2.2 of the TBT Agreement

To be consistent with Article 2.2 of the TBT Agreement, a technical regulation must:

(i) pursue a ‘legitimate objective’; and
(ii) not be more trade-restrictive than ‘necessary’ to fulfil that legitimate objective (taking into account the risks non-fulfilment would create).

a. RELEVANT JURISPRUDENCE

• Burden of Proof

In order to establish that the technical regulation is inconsistent with Article 2.2 of the TBT, Syldavia must establish that the measure creates unnecessary barriers to trade. Syldavia must also present evidence and arguments sufficient to establish that the challenged measure is more trade restrictive than necessary to achieve the legitimate objective taking into account the risks non-fulfilment would create. In making its prima facie case, Syldavia may also seek to identify a possible alternative measure that is less trade restrictive, makes an equivalent contribution to the relevant objective, and is reasonably available.

It is then for Borginia to rebut Syldavia’s prima facie case, by presenting evidence and arguments showing that the challenged measure is not more trade restrictive than necessary to achieve the contribution it makes toward the realisation of the objective pursued and by establishing, for example, that the alternative measure identified by Syldavia is not reasonably available, is not less trade restrictive or makes an equivalent contribution.
The first step in examining the legitimacy of the objective is the identification of the objective of the measure at issue. The objective of any measure can be determined by considering the text of the statute, legislative history, and other evidence regarding the structure and operation of the measure (US-Tuna (Mexico), Appellate Body Report, ¶314). Moreover, the respondent member’s characterisation of the objective can be taken into account, although the Panel is not bound by it. A legitimate objective “refers to — an aim or target that is lawful, justifiable, or proper” (US- COOL (Canada), Appellate Body Report, ¶370).

The definition of “necessary” that appears in Article 2.2 of the TBT Agreement is derived from GATT cases interpreting Article XX, which set forth the “less trade-restrictive measure” test. In determining whether or not a measure is “more trade-restrictive than necessary to fulfil a legitimate objective”, the degree of contribution made by the measure to the legitimate objective at issue must be considered. According to the AB, the precise inquiry in this respect is as to what degree the challenged technical regulation, as written and applied, is capable of contributing and/or actually contributes to the achievement of the legitimate objective pursued by the Member (US- COOL (Canada), Appellate Body Report, ¶373).

However, it is generally acknowledged that assessing the contribution of a measure addressing climate change concerns is particularly difficult. Even the AB found that it may be difficult to isolate the contribution of a single measure that forms part of a more comprehensive policy, and because the results obtained from climate change related measures may only be evaluated “with the benefit of time.” (Brazil –Retreaded Tyres, Appellate Body Report, ¶151; Gabrielle Marceau, The Interface Between the Trade Rules and Climate Change Actions in Legal Issues on Climate Change and International Trade Law (ed. Deok-Young Park) on p.18).

The Panel in US — Tuna II (Mexico) considered that the “risks of non-fulfilment” language in Article 2.2 required consideration of the “likelihood and the gravity of potential risks”. In assessing such risks, relevant elements of consideration are, inter alia: available scientific and technical information, related processing technology or intended end-uses of products (US — Tuna II (Mexico), Appellate Body Report, ¶321). In this regard, the AB has held in US — Cool:

“A proposed alternative may be reasonably available even if it involves "some change or administrative cost". Thus, in the first instance, cost estimates may be relevant for the assessment of whether a proposed alternative measure is reasonably available. However, considering that proposed alternative measures serve as "conceptual tool[s]", and taking into account that the specific details of implementation may depend on the capacity and particular circumstances of the implementing Member in question, it would appear incongruous to expect a complainant, under Article 2.2 of the TBT Agreement, to provide detailed information on how a proposed alternative would be implemented by the respondent in practice, and precise and comprehensive estimates of the cost that such implementation would entail. Rather, once a complainant has established prima facie that the proposed alternative is reasonably available to the respondent, it would be for the respondent to adduce specific evidence showing that associated costs would be prohibitive, or that technical
difficulties would be so substantial that implementation of such an alternative would entail an undue burden for the Member in question.”
(US — Cool 21.5, Appellate Body Report, ¶5.338)

In US— Tuna II (Mexico), the Appellate Body found that an analysis of whether a technical regulation is ‘not trade-restrictive than necessary taking account of the risks non-fulfilment would create’ involves a ‘relational analysis’ and a ‘comparative analysis’. In respect of the ‘relational analysis’, a panel should begin by considering factors including: (i) the degree of contribution made by the measure to the legitimate objective at issue; (ii) the trade-restrictiveness of the measure; and (iii) the nature of the risks at issue and the gravity of consequences that would arise from non-fulfilment of the objectives pursued by the Member through the measure (US — Tuna II (Mexico), Appellate Body Report, ¶322).

In addition to the ‘relational analysis’, a ‘comparative analysis’ should also be undertaken to establish whether a technical regulation is more trade restrictive than necessary under Article 2.2 of the TBT Agreement (US — Tuna II (Mexico), Appellate Body Report, ¶322). For undertaking a ‘comparative analysis’, it would be relevant to consider: (i) whether the proposed alternative measure is less trade-restrictive; (ii) whether it would make an equivalent contribution to the legitimate objective, taking into account the risks non-fulfilment would create; and (iii) whether it is reasonably available (US — Tuna II (Mexico), Appellate Body Report, ¶322). The comparison of the measure at issue with possible alternative measures should be made in light of the nature of the risks at issue and the gravity of consequences that would arise from non-fulfilment of the legitimate objective (US — Tuna II (Mexico), Appellate Body Report, ¶321). The relational analysis considers the challenged measure on its own whereas the comparative analysis considers the challenged measure against alternatives. However, it is to be noted that according to the Appellate Body in US— Tuna II (Mexico), “it is not mandatory in respect of Article 2.2 of the TBT Agreement for a panel to draw a preliminary conclusion on ‘necessity' based on the factors with respect to the technical regulation itself before engaging further in a comparison with proposed alternative measures” (US — COOL (Article 21.5 – Canada and Mexico), Appellate Body Report, ¶5.235).

b. **ARGUMENTS FOR SYLDAVIA**

**Relational Analysis:**

- **Legitimate Objective:** It may be difficult for Syldavia to argue that there is no legitimate objective behind Borginia’s implementation of NESI’s Decision of 2015, given that Article 2.2 of the TBT Agreement explicitly mentions environmental protection as a legitimate objective.
- **Degree of Contribution:** Syldavia could argue that there is no evidence to support that the NESI’s Decision of 2015 contributed materially to the reduction in carbon emissions. Admittedly, there have been some signs of reduction in carbon emissions from Borginia’s textile industry but it could very well be attributed to other measures (as mentioned in ¶2.5 of the Moot Problem) which are taken by Borginia. Therefore, it is not conclusive as to whether the NESI’s Decision of 2015 contributed to the objective.
- **Trade-Restrictiveness:** Syldavia could argue that as a result of the NESI Decision of 2015, its cotton fabrics exports to Borginia significantly dropped since powerloom cotton could not be sold as ‘100% cotton fabric’ in Borginia.
• Nature of risks from non-fulfilment: It could be difficult for Syldavia to argue that emission of greenhouse-gases by the textile industry in Borginia and the consequent degradation of the environment is not a grave concern.

Comparative analysis: This part of the analysis would require participant teams to come up with novel alternatives to NESI’s Decision of 2015. However, in considering the efficacy of such alternative measures, the judges should consider the points set out by the Appellate Body in US — Tuna II (Mexico) (see above). A suggested alternative measure is carbon-footprint labels/eco-labels or any of the labels that fall within ISO 14000 series.

c. ARGUMENTS FOR BORGINIA

Relational Analysis:

• Legitimate Objective: Borginia could argue that NESI’s Decision of 2015 was issued to protect the environment, which is recognized as a legitimate objective in Article 2.2 of the TBT.

• Degree of Contribution: Borginia could argue that NESI’s Decision of 2015 was not more trade restrictive that necessary to fulfill its legitimate objective. The Borginian government was concerned that in view of increase in demand for cotton handloom textile products in Borginia and overseas market, the textiles manufacturing unit might turn to mechanized production processes which could lead to higher carbon emissions. Additionally, Borginia could also argue that as stated in Clarification 10 of the Moot problem, during the period 2010 to 2017, there have been some signs of reduction in carbon emissions from Borginia’s textile industry. To that extent, the measure was apt to make a material contribution to the fulfillment of the stated objective.

• Trade-Restrictiveness: Borginia could admit that since the measure was aimed to achieve a legitimate objective, it did have an impact on exports from Syldavia of cotton fabrics. Since this point is comparatively weaker for Borginia, teams should focus primarily on the degree of contribution and the nature of risks and consequences of non-fulfilment of the legitimate objective.

• Nature of risks from non-fulfilment: Borginia could argue that if the NESI Decision of 2015 was not introduced, textile manufacturing units would turn to mechanised production processes. Since power in the textile industry in Borginia was sourced from coal and fossil fuels and the textile industry was considered as a significant contributor of green-house gases, non-fulfilment of meeting carbon emission targets could negatively impact the fragile environment. Borginia could argue that considering the serious environmental damage in Borginia in recent years (as mentioned in ¶1.4 of the Moot Problem), the nature of risks and gravity of consequences from non-fulfilment of objectives pursued by Borginia would be immense. Furthermore, non-adoption of NESI’s Decision of 2015 would prevent Borginia from meeting its commitment under the Paris Agreement i.e., to reduce green-house gas emissions.

Comparative Analysis: This part of the analysis would require Borginia to disapprove the alternatives advanced by Syldavia by drawing comparisons from the reasons set out by the Appellate Body in US — Tuna II (Mexico) (see above). Therefore, Borginia would have to argue that the alternatives put forth by Syldavia do not make an equivalent contribution to the legitimate objectives sought by Borginia, are not less trade-restrictive and are not reasonably available to Borginia. An alternative may not be considered as reasonably available if there the cost for the implementation of the alternate measure is prohibitive or that technical difficulties
would be so substantial that implementation of such an alternative would entail an undue burden. (*US — COOL* 21.5, Appellate Body Report, ¶5.338)

### iii. Article 2.4 of the TBT Agreement

A three-step analysis was followed by the AB in *EC-Sardines (EC-Sardines (Peru), Appellate Body Report, ¶¶217-290)*. The AB first considered whether the alleged international standard was indeed a ‘relevant international standard’ within the meaning of Article 2.4, and then they analysed whether the relevant international standard had been used ‘as a basis for’ the technical regulation; finally, the third element considered was the ‘ineffectiveness or inappropriateness’ of the relevant international standard for the fulfilment of the legitimate objectives pursued.

#### a. Legal Provisions and Relevant Jurisprudence

**International Standard**

In *US — Tuna II (Mexico) (Panel Report, ¶¶7.663–7.665)* considered that the term “international standard” should be understood to have the same meaning as in the ISO/IEC Guide 2. The Panel noted:

> “The term "international standard" is not defined in Annex 1 of the TBT Agreement, but is defined in the ISO/IEC Guide 2. In accordance with the terms of Annex 1, in the absence of a specific definition of this term in Annex 1, the term "international standard" should be understood to have the same meaning in the TBT Agreement as in the ISO/IEC Guide 2, which defines it as a "standard that is adopted by an international standardizing/standards organization and made available to the public." (*US — Tuna II (Mexico), Panel Report, ¶7.663).*

An ‘international standard’ is thus composed of three elements:

- a standard;
- adopted by an international standardizing/standards body; and
- made available to the public.

The AB in *US- Tuna II* noted that a “standardizing body” is defined as a “body that has recognized activities in standardization”, whereas a “standards body” is a “standardizing body recognized at national, regional or international level, that has as a principal function, by virtue of its statutes, the preparation, approval or adoption of standards that are made available to the public.” (*US — Tuna II (Mexico), Appellate Body Report, ¶357.* In this particular case, it is beyond doubt that the ISO is the relevant international standardization body. However, the parties are likely to contest whether the ISO 14666 is the “relevant international standard”.

In *EC — Sardines*, in the context of an analysis relating to the notion of “relevant international standard” under Article 2.4, the AB considered the relationship between the definitions under Annex 1 of the TBT Agreement and the ISO/IEC Guide:

> “According to the chapeau [of Annex 1], the terms defined in Annex 1 apply for the purposes of the TBT Agreement only if their definitions depart from those in the ISO/IEC Guide 2:1991 (the ‘ISO/IEC Guide’). This is underscored by the word ‘however’. The definition of a standard in Annex 1 to the TBT Agreement departs from that provided in the
ISO/IEC Guide precisely in respect of whether consensus is expressly required.” (EC-Sardines (Peru), Appellate Body Report, ¶224)

- Definition of ‘consensus’ in ISO

Consensus is defined in ISO/IEC Guide 2: Standardization and related activities general vocabulary as “general agreement, characterized by the absence of sustained opposition to substantial issues by any important part of the concerned interests and by a process that involves seeking to take into account the views of all parties concerned and to reconcile any conflicting arguments. [NOTE: Consensus need not imply unanimity. “Sustained oppositions” are views expressed during minuted committee, working group (WG) or task force (TF) meetings which are maintained by an important part of the concerned interest and which are incompatible with the relevant committee consensus. The notion of “concerned interest(s)” will vary depending on the dynamics of the relevant committee and must therefore be determined by the relevant committee leadership on a case by case basis.]

It is important to note that the term ‘consensus’ is understood differently within the context of the WTO and the ISO. In the context of the WTO, ‘consensus’ means a ‘unanimous’ decision. Footnote 1 to Article IX:1 of the Marrakesh Agreement as well as Footnote 1 to Article 2.4 of the DSU define consensus as being achieved if no WTO Member, present at the meeting when the decision is taken, formally objects to the proposed decision. On the other hand, ISO Supplement defines consensus as general agreement, characterized by the absence of sustained opposition to substantial issues by any important part of the concerned interests and by a process that involves seeking to take into account the views of all parties concerned and to reconcile any conflicting views. ISO’s standard-setting process requires at least 2/3rd of participating members to vote in favour and not more than one-quarter of the total number of votes cast are negative. As indicated above, the note to the definition clarifies that consensus does not imply unanimity in the ISO standard setting process.

The AB in EC — Sardines upheld the Panel’s conclusion that even if not adopted by consensus, an international standard can constitute a “relevant international standard”. The AB agreed with the following interpretation by the Panel of the last two sentences of the Explanatory note to the definition of the term “standard”, as contained in Annex 1 paragraph 2:

“The first sentence reiterates the norm of the international standardization community that standards are prepared on the basis of consensus. The following sentence, however, acknowledges that consensus may not always be achieved and that international standards that were not adopted by consensus are within the scope of the TBT Agreement. This provision therefore confirms that even if not adopted by consensus, an international standard can constitute a relevant international standard.” (EC-Sardines (Peru), Appellate Body Report, ¶222)

An important issue is whether a standard which is not adopted by ‘unanimity’ could still be considered as a “relevant international standard”. Although EC- Sardines has by and large clarified this position, the parties could still contest this definition. In particular, the penultimate line of the Explanatory Note to Annex 1.2 clearly indicates that “[s]tandards prepared by the international standardization community are based on consensus”. It is also true that the last line of the Explanatory Note notes that [t]his Agreement also covers documents that are not
based on consensus.” However, this line does not refer to a ‘standard’ but a ‘document’. In any case, the Appellate Body’s statement in EC- Sardines that the “omission of a consensus requirement in the definition of a “standard” in Annex 1.2 was a deliberate choice on the part of the drafters of the TBT Agreement” may sound somewhat questionable. Annex 1.2 of the TBT Agreement indeed refers to ‘consensus’. It would be worthwhile to have a fresh discussion on this issue, albeit in a different setting.

- “Relevant”

In EC — Sardines, the AB agreed with the Panel’s statement that the ordinary meaning of the term “relevant” is “bearing upon or relating to the matter in hand; pertinent”. In EC — Sardines, the standard at issue in the dispute was Codex Stan 94 - Codex Standard for Canned Sardines and Sardine-type Products. The EC Regulation laid down common marketing standards for preserved sardines. Moreover, the European communities considered the terms ‘canned sardines’ and ‘preserved sardines’ as essentially identical. Additionally, various corresponding provisions of Codex Stan 94, including labelling requirement, were set out in EC Regulation. Therefore, Codex Stan 94 was considered as a relevant international standard. (EC-Sardines (Peru), Appellate Body Report, ¶217-233)

- “ineffective or inappropriate means” of fulfillment of “legitimate objectives”

In EC-Sardines, the AB held that the interpretation of the second part of Article 2.4 raises two questions:

First, the meaning of the term “ineffective or inappropriate means”; and
Second, the meaning of the term “legitimate objectives”.

The terms “ineffective or inappropriate means” refer to two aspects—the effectiveness of the measure and the appropriateness of the measure. The term “ineffective” means something which is not ‘having the function of accomplishing’, ‘having a result’, or ‘brought to bear’, whereas the term ‘inappropriate’ refers to something which is not ‘specially suitable’, ‘proper’, or ‘fitting’. The AB further noted:

Thus, in the context of Article 2.4, an ineffective means is a means which does not have the function of accomplishing the legitimate objective pursued, whereas an inappropriate means is a means which is not specially suitable for the fulfilment of the legitimate objective pursued. An inappropriate means will not necessarily be an ineffective means and vice versa. That is, whereas it may not be specially suitable for the fulfilment of the legitimate objective, an inappropriate means may nevertheless be effective in fulfilling that objective, despite its “unsuitability”. Conversely, when a relevant international standard is found to be an effective means, it does not automatically follow that it is also an appropriate means. The question of effectiveness bears upon the results of the means employed, whereas the question of appropriateness relates more to the nature of the means employed.” (EC-Sardines (Peru), Appellate Body Report, ¶285)

See also AB’s clarification in EC-Sardines, reverting the panel, that Article 2.4 of the TBT Agreement is NOT a rule-exception provision and that the complainant thus bears the full burden to make a prima facie case, including whether the use of the international standard by
the respondent is NOT ineffective or inappropriate. *(EC-Sardines (Peru), Appellate Body Report, ¶290)*

On the other hand, “legitimate objectives” referred to in Article 2.4 must be interpreted in the context of Article 2.2 of the TBT Agreement which provides an illustrative and open list of objectives considered “legitimate”. The AB in US- COOL noted that in identifying the objective pursued by a Member, a panel should take into account the Member’s articulation of its objectives. The AB, however, clarified that a panel is not bound by a Member’s characterization of such objectives *(US- COOL (Canada), Appellate Body Report, ¶371)*.

b. **Arguments for Syldavia**

Syldavia could argue that the ISO14666 is an international standard adopted by international standardizing/standards organization and is made available to the public. Furthermore, Syldavia could also argue that the standard was adopted on the basis of consensus. Syldavia could, in addition, argue that unanimity is not required to meet the requirement of ‘consensus’.

Additionally, Syldavia could argue that the legitimate objective of Borginia’s NESI’s Decision of 2015 is providing product information. The NESI’s Decision of 2015 mandates that for 100% handloom cotton fabric to be marketed as ‘Cotton fabric’ certain requirements must be met. Syldavia could argue that the specification ‘Cotton fabric’ on a product would not enable a consumer to infer whether the product was produced by employing clean production practices or not. Furthermore, Syldavia could argue that ISO 14666 is effective in accomplishing a legitimate objective since it allows the process of weaving, knitting and spinning to be undertaken by hand or by machine. Therefore, it is flexible enough to incorporate both hand and machine in the production process of cotton fabrics, and allows flexibility for Members to achieve legitimate outcomes including protection of the environment.

c. **Arguments for Borginia**

Borginia could argue that it repeatedly objected to the adoption of the draft standard at every stage of the standard setting process and that the aforesaid standard is not based on any ‘consensus’. It can be argued that Borginia objected to the standard-setting process of ISO 14666 on the following grounds:

1) ISO 14666 is based on uncertain and ambiguous science; that this standard fails to consider the environmental impact of the production of fabrics produced by machines on an industrial level.

2) Environmental concerns arising from the powerloom industry in its country. Borginia, pursuant to Paris Agreement is obligated to cut down carbon emission by 20% by 2030.

3) ISO 14666 is inconsistent with NESI’s Decision of 2015.

Despite Borginia’s repeated objection to the process, ISO 14666 was adopted. Therefore, Borginia could argue that ISO 14666 is not based on consensus as ‘sustained objection’ was maintained. Borginia could also look at the dictionary meaning of the term ‘consensus’. This is consistent with the AB statements in several cases that the “dictionary definitions are the useful starting points for discerning the meaning of a treaty term” *(EC - Chicken Cuts (Brazil), Appellate Body Report, ¶175; US - Softwood Lumber (Canada), Appellate Body Report, ¶59)*. Borginia could also rely on the TBT Committee’s Decision on Principles for the Development of International Standards, Guides and Recommendations with Relation to Article 2, 5, and Annex 3 to the Agreement [“TBT Decision”] to decipher the meaning of ‘consensus’. In US – 

Tuna II, the AB noted that the TBT Decision could qualify as a “subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions” within the meaning of Article 31.3(a) of the VCLT (US — Tuna II (Mexico), Appellate Body Report, ¶372). The decision of the TBT Committee defines consensus as “procedures... that seek to take into account the views of all parties concerned and to reconcile any conflicting arguments.”

Borginia could argue that Syldavia has not made a prima facie case that the use of the international standard is effective and inappropriate to meet Borginia’s legitimate objective. The initial burden of proof is on Syldavia to show that the use of international standard is not ineffective or inappropriate based on the observations made by the AB in EC- Sardines. Borginia could argue that the international standard is not relevant as it fails to address the environmental concerns arising from the operation of the powerloom industry. Furthermore, ISO 14666 is “ineffective or inappropriate means” of fulfilment of Borginia’s legitimate objectives. Borginia’s legitimate objective is protection of environment and sustainable standards through reduction of carbon emissions. Borginia could argue that since ISO 14666 does not distinguish cotton fabric manufactured from handloom production and powerloom production, it fails to address the specific environmental concerns of Borginia.

III. WHETHER NESI’S DECISION OF 2015 IS INCONSISTENT WITH ARTICLE III:4 OF THE GATT?

a. LEGAL PROVISIONS

Article III:4 of the GATT provides, in relevant part:

The products of the territory of any contracting party imported into the territory of any other contracting party shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use. ...

b. RELEVANT JURISPRUDENC

It is often a matter of debate whether the legal arguments and their demonstration pertaining to Article III:4 of the GATT and Article 2.1 of the TBT are the same. While Article 2.1 of the TBT Agreement applies to “technical regulations”, Article III: 4 of the GATT applies to “laws, regulations and requirements”. The AB noted in US- Tuna II (Mexico):

“[T]he Panel’s decision to exercise judicial economy rested upon the assumption that the obligations under Article 2.1 of the TBT Agreement and Article I:1 and III:4 of the GATT are substantially the same. This assumption is, in our view, incorrect.” (US — Tuna II (Mexico), Appellate Body Report, ¶405)

The AB noted that the scope and content of Article 2.1 of the TBT and Article III:4 of the GATT are not the same (US — Tuna II (Mexico), Appellate Body Report, ¶ 405).
The AB in *Canada — Periodicals*, held that the fundamental purpose of Art. III of the GATT is to ensure equality of competitive conditions between imported and like domestic products. (*Canada – Periodicals (United States)*, Appellate Body Report, p.18) The AB in *Korea-Beef* has summarized the elements that must be demonstrated to establish an inconsistency with Article III:4 as follows:

i) the measure at issue is a “law, regulation, or requirement affecting the internal sale, offering for sale, purchase, transportation, distribution, or use” of the products at issue;
ii) the imported and domestic products at issue are “like” products;
iii) the treatment accorded to imported products is “less favourable” than that accorded to like domestic products.
iv) the AB further clarified that “the word 'like' in Article III:4 is to be interpreted to apply to products that are in ... a competitive relationship”, because it is "products that are in a competitive relationship in the marketplace [that] could be affected through treatment of imports 'less favourable' than the treatment accorded to domestic products". (*Korea – Beef*, Appellate Body Report, ¶ 130-151)

i. **Likeness**

Likeness of products is determined on a case-to-case basis. In *EC-Asbestos*, the AB established that the essential test for likeness of products is a competitive relationship. (*EC-Asbestos (Canada)*, Appellate Body Report, ¶101) It further established four general criteria to determine the likeness of products namely:

i) physical properties of the products;
ii) the extent to which the products can serve the same end uses;
iii) extent to which consumers treat the products as alternatives for the satisfaction of a particular demand; and
iv) the classification of products for tariff purposes.

The 'likeness' discussion and demonstration undertaken in regard to Article 2.1 of the TBT Agreement is also relevant for Article III:4.

ii. **Less Favourable Treatment**

The AB has clarified that a measure accords less favourable treatment to imported products where it modifies the conditions of competition in the marketplace to the detriment of the group of imported products as compared to the group of like domestic products. Finally, the AB noted that, for a measure to be found to modify the conditions of competition in the marketplace to the detriment of imported products, there must be a “genuine relationship” between the measure and the detrimental impact (ibid). The AB in *Thailand-Cigarettes (Thailand-Cigarettes (Philippines)*, Appellate Body Report, ¶129) held that analysis of whether a measure has a detrimental impact on imports “need not be based on empirical evidence as to the actual effects of the measure at issue in the internal market of the Member concerned.”

### c. **Arguments for Syldavia**

In the matter, Syldavia can contend that the NESI decision of 2015 has disproportionately benefited the domestic products to the detriment of the imported products. Syldavia can use the data provided in the tables to the Annex to quantitatively establish this argument.
d. **ARGUMENTS FOR BORGINIA**

Borginia can contend that the products in question are not ‘like’. Some of the arguments, which Borginia has adopted in the case of Article 2.1 of the TBT, can also be used here especially in relation to the ‘likeness’ determination under Article III.
B. WHETHER THE SOCA TAX LEVIED ON THE IMPORTED COTTON FABRIC IN EXCESS OF OTHER APPLICABLE CUSTOM DUTIES IS INCONSISTENT WITH ARTICLES II: 1 (A) AND (B), II: 2(A) AND III:2 OF THE GATT

I. WHETHER THE SOCA TAX LEVIED ON THE IMPORTED COTTON FABRIC IN EXCESS OF OTHER APPLICABLE CUSTOM DUTIES IS INCONSISTENT WITH ARTICLES II: 1 (A) AND (B)?

a. LEGAL PROVISIONS

Article II: Schedules of Concessions

1. (a) Each contracting party shall accord to the commerce of the other contracting parties treatment no less favourable than that provided for in the appropriate Part of the appropriate Schedule annexed to this Agreement.
   
   (b) The products described in Part I of the Schedule relating to any contracting party, which are the products of territories of other contracting parties, shall, on their importation into the territory to which the Schedule relates, and subject to the terms, conditions or qualifications set forth in that Schedule, be exempt from or ordinary customs duties in excess of those set forth and provided therein. Such products shall also be exempt from all other duties or charges of any kind imposed on or in connection with the importation in excess of those imposed on the date of this Agreement or those directly and mandatorily required to be imposed thereafter by legislation in force in the importing territory on that date.

2. Nothing in this Article shall prevent any contracting party from imposing at any time on the importation of any product:
   
   (a) a charge equivalent to an internal tax imposed consistently with the provisions of paragraph 2 of Article III* in respect of the like domestic product or in respect of an article from which the imported product has been manufactured or produced in whole or in part;

Article III*: National Treatment on Internal Taxation and Regulation

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.

B. Text of Note Ad Article III

Paragraph 2

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.

b. **RELEVANT JURISPRUDENCE**

The measure at issue under this legal claim is the SOCA Tax implemented by Borginia. The tax was determined by carbon emission per square metre in the production process. In the case of cotton fabrics, SOCA Tax is applicable to both domestic and imported fabrics and, in the case of domestic fabrics, it is collected at the time of domestic sale. For imports, the tax is collected at the point of customs clearance and alongside other applicable customs duties.

The facts associated with this claim relate to the application of border duties that are also alleged to be correlated to internal taxes. The AB noted that in such a scenario, “Article II: 1(b) and Article II: 2(a) are closely related and must be interpreted together.” *(India- Additional Duties (United States), Appellate Body Report, ¶153).* Accordingly, this Bench Memo adopts the following sequence of discussion on this claim.

The Panel in *EC-Chicken Cuts* laid down a three-step test to determine if a tariff treatment is inconsistent with Article II:1(a) and Article II:1(b). First, the treatment accorded to the products at issue under a Member’s schedule is to be ascertained. Second, the treatment accorded to the products at issue under the measure at issue is to be ascertained. Third, whether the measure at issue results in less favourable treatment of the products at issue than that provided for in the Member’s schedule. In *Argentina — Textiles and Apparel*, the AB found that “Paragraph (b) prohibits a specific kind of practice that will always be inconsistent with paragraph (a): that is, the application of ordinary customs duties in excess of those provided for in the Schedule.” Also, “the application of customs duties in excess of those provided for in a Member’s Schedule inconsistent with the first sentence of Article II:1(b), constitutes ‘less favourable’ treatment under the provisions of Article II:1(a)” *(Argentina — Textiles and Apparel (United States), Appellate Body Report, ¶45).*

In *India — Additional Import Duties* the AB noted that tariffs are permissible under Article II:1(b) so long as they do not exceed a Member’s bound rates. *(India — Additional Import Duties (United States), Appellate Body Report, ¶159)* However, the AB in *Argentina-Textiles and Apparel* held that the text of Article II:1(b), first sentence, does not address whether applying a type of duty different from the type provided for in a Member’s Schedule is inconsistent, in itself, with that provision. The application of a type of duty different from the type provided for in a Member’s Schedule is inconsistent with Article II:1(b), first sentence, of the GATT to the extent that it can result in customs duties being levied in excess of those provided for in that Member’s Schedule.

The key question is whether the SOCA Tax imposed at the border is a (i) charge imposed on or in connection with importation (i.e., an “import charge”) under GATT Article II: 1(b), or whether this tax is (ii) equivalent to an internal tax (i.e., an “internal tax”) in respect of the like domestic product.

Since Syldavia is contending that the SOCA Tax is an import charge, the burden will be on Syldavia to establish this claim under Article II:1(a) and (b). If it is established as an import charge, it would be fairly easy for Syldavia to establish that the SOCA Tax imposed on fabrics is a violation of Article II: 1(b) of the GATT since the border charges are clearly above the tariff binding.
In this regard, it is instructive to examine the WTO jurisprudence on the definition of import charges. The import charge includes “ordinary customs duties” (OCD) or “other duties and charges” (ODC).

i. Definition of ‘other duties or charges’

The Panel in *Dominican Republic – Import and Sale of Cigarettes* analysed the definition of an ‘other duty or charge’. It held that any fee or charge that is in connection with importation and that is not an ordinary customs duty, nor a tax or duty as listed under Article II:2 (internal tax, antidumping duty, countervailing duty, fees or charges commensurate with the cost of services rendered) would qualify for a measure as ‘other duties or charge’ under Article II:1(b).

c. Arguments for Syldavia

Less Favourable Treatment: According to Borginia’s WTO Schedule of Concessions, the bound rate of 10% will be applicable to cotton fabrics. Since, the SOCA Tax is levied at the border upon importation, in addition to the bound rate of 10%, Borginia’s measure constitutes a less favourable treatment than what is provided in its schedule, contrary to Article II:1(a). Therefore, SOCA Tax is inconsistent with Article II:1(a) of the GATT. Regarding the ‘less favourable treatment’, the AB in *Argentina- Textiles and Apparel* noted as follows:

“Article II:1(a) is part of the context of Article II:1(b); it requires that a Member must accord to the commerce of the other Members “treatment no less favourable than that provided for” in its Schedule. It is evident to us that the application of customs duties in excess of those provided for in a Member's Schedule, inconsistent with the first sentence of Article II:1(b), constitutes “less favourable” treatment under the provisions of Article II:1(a). A basic object and purpose of the GATT 1994, as reflected in Article II, is to preserve the value of tariff concessions negotiated by a Member with its trading partners, and bound in that Member's Schedule. Once a tariff concession is agreed and bound in a Member's Schedule, a reduction in its value by the imposition of duties in excess of the bound tariff rate would upset the balance of concessions among Members.” (Argentina- Textiles and Apparel (United States), Appellate Body Report. ¶47)

**SOCA Tax constitutes an Ordinary Custom Duty:** Syldavia could argue that the SOCA Tax is collected at the point of customs clearance alongside other applicable customs duties. Since the obligation to pay SOCA Tax accrues at the time of customs clearance, it constitutes an Ordinary Custom Duty. Since SOCA Tax is in excess of the bound rate of 10% provided in Borginia’s Schedule of Concessions, Syldavia can argue that this tax is inconsistent with Borginia’s commitments under Article II: 1(a) of the GATT.

d. Arguments for Borginia

Borginia should contest that SOCA Tax is a tax not covered by Article II of the GATT. Borgina should argue that it is a tax governed by Article III only, pursuant to the *Ad Note* of Article III* and article II:2(a) and imposed after the collection of import duties. *Ad Note* to Article III specifies that when an internal charge is “collected or enforced in the case of the imported product at the time or point of importation”, such charge is nevertheless to be regarded as an “internal charge” (See *China-Auto Parts (Canada)*, Appellate Body Report, ¶162).
Borginia could argue that Syldavia has mischaracterized the SOCA Tax as an import tax within the meaning of Article II: 1(b) of the GATT. Borginia could further argue that the SOCA Tax which is imposed at the border is equivalent to internal taxes imposed in respect of like domestic products within the meaning of Article II: 1(b) of the GATT. In the light of AB’s observation in India – Additional Duties, Borginia could argue that “Article II:2 (a), subject to the conditions stated therein, exempts a charge from the coverage of Article II: 1(b).” (India – Additional Duties (United States), Appellate Body Report, ¶159). Borginia could rest their claim on the ground that the SOCA Tax imposed at the border is not triggered by importation as such, but by the sale, offering for sale, distribution or use of imported products once these products have cleared customs. (China-Auto Parts (Canada), Appellate Body Report, ¶163)

II. WHETHER THE SOCA TAX LEVIED ON THE IMPORTED COTTON FABRIC IN EXCESS OF OTHER APPLICABLE CUSTOMS DUTIES IS INCONSISTENT WITH ARTICLE II:2(A) AND III:2 OF THE GATT?

a. RELEVANT JURISPRUDENCE

i. Distinction between ‘ordinary customs duties’ and ‘internal taxes’

The Appellate Body in China — Auto Parts, spelt out the distinction between an OCD under Article II and an internal charge under Article III as follows:

“For a charge to constitute an ordinary customs duty [subject to Article II] ... the obligation to pay it must accrue at the moment and by virtue of or, in the words of Article II:1(b), “on”, importation. On the other hand, “charges falling within the scope of Article III are charges that are imposed on goods that have already been “imported”, and that the obligation to pay them is triggered by an “internal” factor, something that takes place within the customs territory.” (China – Auto Parts (Canada), Appellate Body Report, ¶¶153-158)

This view was reinforced by the AB in China – Audiovisual Services:

“This leads us, like the Panel, to the view that a key indicator of whether a charge constitutes an ‘internal charge’ within the meaning of Article III:2 of the GATT 1994 is whether the obligation to pay such charge accrues because of an internal factor (e.g., because the product was re-sold internally or because the product was used internally), in the sense that such ‘internal factor’ occurs after the importation of the product of one Member into the territory of another Member.” (China – Audiovisual Services (United States), Appellate Body Report, ¶163)

In India — Additional Import Duties, the AB observed that Article II:2(a), subject to the conditions stated therein, exempts a charge from the coverage of Article II:1(b). If a charge satisfies the conditions of Article II:2(a), it would not result in a violation of Article II:1(b). The conditions enumerated in Article II:2(a) are as follows:

i) Charge imposed at the time of importation must be equivalent to an internal tax; and
ii) It must be imposed consistently with the provisions of paragraph 2 of Article III in respect of the like domestic product or in respect of an article from which the imported product has been manufactured or produced in whole or in part.

The availability of Article II:2(a) would depend on the meaning of “imposed consistently with the provisions of paragraph 2 of Article III.” Examining the text of Article II:2(a), the AB in India-Additional Import Duties found:

“‘equivalence’ and ‘consistency with Article III:2’ — cannot be interpreted in isolation from each other; they impart meaning to each other and need to be interpreted harmoniously…. Determining whether a charge is imposed consistently with Article III:2 necessarily involves a comparison of a border charge with an internal tax in order to determine whether one is ‘in excess of’ the other…” (India- Additional Duties (United States), Appellate Body Report, ¶¶170-175)

ii. Burden of Proof in relation to Article II: 2(a)

In the interrelationship between Article II: 1(b) and II: 2(a), there is a potential issue regarding whether Article II:2(a) is an exception to a violation of Article II:1(b) and as to who should bear the burden in establishing consistency or non-consistency with II:2(a). In short, the question is whether Article II: 2(a) is an exception to any violation of Article II: 1(b) or not. The Appellate Body noted in India- Additional Import Duty as follows:

“Not every challenge under Article II: 1(b) will require a showing with respect to Article II: 2(a). In the circumstances of this dispute, however, where the potential for application of Article II:2(a) is clear from the face of the challenged measures, and in the light of our conclusions above concerning the need to read Articles II:1(b) and II:2(a) together as closely inter-related provisions, we consider that, in order to establish a prima facie case of a violation of Article II:1(b), the United States was also required to present arguments and evidence that the Additional Duty and the Extra-Additional Duty are not justified under Article II:2(a).” (India- Additional Duties (United States), Appellate Body Report, ¶190)

The AB continued in India- Additional Import Duties:

“[D]ue to the characteristics of the measures at issue or the arguments presented by the responding party, there is a reasonable basis to understand that the challenged measure may not result in a violation of Article II: 1(b) because it satisfies the requirements of Article II: 2(a), then the complaining party bears some burden in establishing that the conditions of Article II: 2(a) are not met.” (India- Additional Duties (United States), Appellate Body Report, ¶192)

Based on the above findings of the AB, Syldavia should present arguments on how the SOCA Tax is also not justified under Article II:2 (a) of the GATT in order to meet the burden of proof.

An important legal issue in the case is whether the SOCA Tax is a proper border tax adjustment or not. The imposition of SOCA Tax at the border can be regarded as a form of border tax
adjustments (BTAs) on imports. However, one of the concerns of this characterization is that this tax is not applied on a product as such but in relation to the manner in which the product is produced. The Working Party Report on Border Tax Adjustments (1970) discussed the issue of consistency of BTAs with the WTO. One of the objectives of BTA is to ensure the destination principle—a concept that products should only be taxed in the country of consumption—is enforced. The GATT Working Party was requested to pronounce on the GATT-consistency of practices by the GATT contracting parties referred to as border tax adjustments. The term border tax adjustment is explained in §4 of the final report:

“…as any fiscal measures which put into effect, in whole or in part, the destination principle (i.e. which enable exported products to be relieved of some or all of the tax charged in the exporting country in respect of similar domestic products sold to consumers on the home market and which enable imported products sold to consumers to be charged with some or all of the tax charged in the importing country in respect of similar domestic products.”

In relation to carbon taxes on imports, two questions need to be answered: (1) Is a carbon tax on imports a direct or an indirect tax? (2) Can a carbon tax which is not imposed on the good itself but on the carbon dioxide emissions generated in its production process be qualified as a BTA?

Article II:2(a) GATT allows: (i) imposing a charge equivalent to an internal tax in terms of a border tax adjustment and consistent with Article III:2 GATT on the importation of any product, and (ii) imposing charges on ‘articles from which the imported product has been manufactured or produced in whole or in part’. While the first type may refer to charges on domestic and ‘like’ imported fuels, the second type could refer to the energy inputs and fossil fuels used in the production process.

A potentially important question is whether taxes on carbon emitted in the process or energy consumed in the production are border adjustable. While BTAs are generally available for indirect taxes on inputs, such inputs are assumed to be present in the final product (Kaufmann, Christine & Weber, Rolf H, Carbon-related border tax adjustment: mitigating climate change or restricting international trade? 10 World Trade Review 4 (2011)). In the context of the facts of this moot problem, the carbon emission is an externality. Where the inputs are not physically incorporated in the final product, it becomes much more difficult to verify whether they have been actually used and in what amounts.

For instance, the GATT Panel in US–Supervfund in principle permitted the border adjustment of any ingredient physically present in the imported product. The Supervfund case is often cited as a precedent for applying input-taxes to inputs embodied in imported goods. As part of the United States’ Supervfund Amendments and Reauthorization Act of 1986, the United States levied a revenue generating tax on the use of certain feedstock chemicals used in the manufacture of chemical derivative products.

Under the Supervfund amendments, the assessment of tax for imported chemicals from abroad was according to the amount of the taxed feedstock chemicals used during their production. The tax applied to imported final chemicals varied depending on the amount of feedstock embodied in the imported chemical. In 1987, the Supervfund tax was challenged by Canada and the European Economic Community (EEC). The GATT Panel reasoned that what determines whether a tax is eligible for adjustment is whether it is levied directly on products and thus
constitutes an indirect tax. The underlying motive for the tax was deemed unimportant: “whether a sales tax is levied on a product for general revenue purposes or to encourage the rational use of environmental resources, is…not relevant for the determination of the eligibility of a tax for border tax adjustment.” (US – Superfund (Canada), Panel Report, ¶5.2.4)

There is a view that carbon should be assumed to be “embedded” in the product. While the GATT Working Party reached a consensus on the adjustability of taxes “directly levied on products” (i.e., indirect taxes), it could not reach a similar position with respect to “taxes occultes”, noting that there was divergence of views with regard to the eligibility of adjustment of certain categories of taxes, including ‘taxes occultes’ (see J J Nedumpara, Energy Security and the WTO Agreements, Springer (2013)).

While the concept of ‘embedded carbon’ is discussed in several academic journals, it is yet to find a direct application in a WTO dispute. A fairly analogous, albeit indirect example, is the Canada – Periodicals case. The measure at issue in this case was an excise tax imposed on split-run editions of periodicals. A periodical comprises of two elements, namely, the editorial content and the advertisement content. It was contended by Canada that the excise tax which differentiated between split-run edition and foreign non-split-run edition based on the value of the advertisement content is not governed by the national treatment obligations of the GATT, but could only be covered under the category of advertising services under the GATS. The AB noted as follows:

“An examination of Part V.1 of the Excise Tax Act demonstrates that it is an excise tax which is applied on a good, a split-run edition of a periodical, on a "per issue" basis. By its very structure and design, it is a tax on a periodical.” (Canada – Periodicals (United States), Appellate Body Report, p. 18)

By this reasoning, the excise tax in that case was a measure which “clearly applie[d] to goods”. (Canada – Periodicals (United States), Appellate Body Report, p. 20)

If the import border tax adjustment is not considered an internal tax on a product, (i) it would likely be considered a charge on import, and (ii) the inapplicability of Article III would also infer the unavailability of the exception under Article II:2(a).

In this regard, it is important for Syldavia to contend the prima facie inapplicability of Article II:2 (a) exception.

iii. Article III:2 of GATT

Article III:2 is especially relevant in the context of meeting the national treatment requirement of the BTA. In this case, unlike the traditional Article III:2 claims, the burden is on Borginia to argue that the SOCA Tax, which is applied at the border, is applied consistently with the requirements of Article III:2 of the GATT.

Article III:2 of the GATT provides for national treatment with respect to internal taxes. The national treatment obligation will apply depending upon whether the products are “like” or “directly competitive and substitutable”. If the imported products and the domestic products are “like”, the imported products are not to be taxed in excess of “like” domestic products, in terms of Article III:2, first sentence. In the alternative, if the two products are not “like”, but are still in a competitive relationship, it needs to be examined whether they are “directly
competitive and substitutable”. If the two categories of products are “directly competitive and substitutable”, then the imported products should be “similarly taxed”, in terms of Article III:2, second sentence.

In the context of border taxes, a major difficulty is in identifying the product for “likeness” comparison as well as the method of demonstrating that the BTA is “applied consistently with the requirements of Article III:2”. There is a view that this requirement would be met so long as the respondent Member establishes that the requirements of “Article are not violated”. (Joel Trachtman, *WTO Law Constraints on Border Tax Adjustment and Tax Credit Mechanisms to Reduce the Competitive Effects of Carbon Taxes*, RFP Discussion Paper 16-03 (2016), p7). However, it can also be argued that the respondent Member should positively establish that “like products” bear the same taxes. However, according to the facts of the problem, cotton and powerloom fabrics could attract different rates of SOCA tax based on the carbon emission. If the former line of arguments is advanced, then Borginia should argue that cotton and powerloom fabrics are not like products based on the process and production methods. However, this argument is likely to be rejected based on the prevailing non-acceptance of the PPMs under Article III of the GATT. (*US- Tuna I* (1991), noting that Article III “covers only those measures that are applied to products as such” ([¶5.81]). See also GATT Border Tax Adjustment Report, [¶ 14])

**Note:** Panellists may note that Syldavia’s argument regarding like product that PPMs are not covered under Article III:4 of the GATT may be slightly inconsistent to their arguments under Annex 1.1 of the TBT Agreement. However, on the whole, it is quite unlikely that the PPMs may have any significant bearing from the point of view of Article III of the GATT.

Therefore as an alternative, Borginia may argue that the product to be compared for “likeness” should be the imported fabric having X% of carbon with the domestic fabric having similar amount of carbon. In short, the product for comparison is neither carbon nor cotton fabric *per se* (See Low Patrick, Marceau Gabrielle, and Reinaud Julia, *Interface between the Trade and Climate Change Regimes: Scoping the Issues*, Journal of World Trade 46 (2012): 485). From the facts of the case, Borginia could argue that the SOCA Tax is based upon the amount of carbon and is applied both to imported and domestic cotton fabric, at the same rate. Further, Borginia could also argue that the carbon emitted in the production process is an integral part of the product. Syldavia could argue that SOCA Tax on carbon fabric with different carbon content is inconsistent with the requirements of Article III:2 of the GATT. Syldavia could argue that irrespective of the amount of carbon, the imported cotton fabric is a “like product” to domestic cotton fabric and that any differential taxation is a violation of Article III:2, first or second sentence.

- **Relevant factors for the determination of “likeness”**

In *Japan — Alcoholic Beverages II*, the AB held that the proper test for determination of ‘like products’ for the purposes of Article III:2, first sentence, must be construed narrowly, on a case-by-case basis, by examining relevant factors including:

i) the product’s end-uses in a given market;

ii) consumers’ tastes and habits;

iii) the product’s properties, nature and quality; and

iv) tariff classification
Relationship with Article III:4 of the GATT

In Thailand — Cigarettes (Philippines), the Panel found that the scope of “like product” is broader under Article III:4 than under the first sentence of Article III:2 and if products are “like” for purposes of Article III:2, they are automatically “like” for purposes of Article III:4. It was held by the AB in EC-Asbestos that the scope of III:2 and III:4 are however similar. (EC-Asbestos (Canada), Appellate Body Report, ¶99)

If the measure is considered to be in violation of Article II:1(b) of the GATT and is not permitted by Article II:2(a), Borginia can still use the exceptions available under Article XX of the GATT to try to justify its violation of II:1(b).

If Article II of the GATT is not applicable and the measure is an internal tax inconsistent with Article III:2, Borginia can also invoke the exceptions of GATT Article XX to justify the latter violation.
C. DEFENCE OF ARTICLE XX OF THE GATT

a. LEGAL PROVISION

The relevant provisions of the GATT are as follows:

“Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:

...

(g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption...”

b. RELEVANT JURISPRUDENCE

Article XX of GATT is meant to provide Members with the ability to regulate for reasons that are important to them, balancing between the goal of trade liberalization and upholding domestic regulatory autonomy. Accordingly, Article XX lays down a number of specific instances in which WTO members may be exempted from GATT rules.

Article XX of the GATT has a bifurcated structure. For the measure to be justified under Article XX, the measure must first, meet the requirements of one of the particular exceptions listed in paragraphs of Article XX. Second, the application of the measure must meet the requirements of the chapeau (the heading) of Article XX.

i. Article XX(g)

Article XX(g) is relevant in the context of climate change since changes in the climate lead to the depletion of other exhaustible natural resources, biodiversity, forestry, fisheries etc. Article XX(g) raises additional considerations in the context of climate change.

Firstly, for such measures to succeed under paragraph (g), they must relate to the “conservation of natural resources”. In US-Shrimp, the AB interpreted the term ‘exhaustible natural resources’ as including both living and non-living natural resources (US – Shrimp (India, Pakistan, Malaysia, Thailand), Appellate Body Report, ¶¶128-131). The AB in US – Gasoline found that clean air was an exhaustible natural resource. It could be argued that preserving the global climate is analogous to the preservation of clean air in US-Gasoline (See Condon B (2009), “Climate change and unresolved issues in WTO Law”, J. Int. Econ Law 12 (4): 896–926).

After determining that the measure is concerned with the conservation of natural resources, the next stage is to consider whether the measure “relates to” the objective pursued (US-Gasoline (Venezuela), Appellate Body Report, pp. 20-21). In order to establish this, there must be a “close and genuine relationship of ends and means” and an examination of “the relationship between the general structure and design of the measure...and the policy goal it purports to
serve.” (US-Gasoline (Venezuela), Appellate Body Report, pp. 20-21) In US-Gasoline, the AB examined whether “the means (the challenged regulations) are, in principle, reasonably related to the ends” and whether “such measures are made effective in conjunction with restrictions on domestic production or consumption” “... a requirement of even-handedness in the imposition of restrictions”. Article XX(g) thus permits trade measures relating to the conservation of exhaustible natural resources when such trade measures work together with restrictions on domestic production or consumption, which operate so as to conserve an exhaustible natural resource. (See China-Rare Earth (United States), Appellate Body Report, ¶¶359-361)

ii. Chapeau

The chapeau of article XX, with regard to measures provisionally justified under one of the paragraphs of Article XX, imposes, “the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade” (US – Shrimp (India, Pakistan, Malaysia, Thailand), Appellate Body Report, ¶150). In EC-Seal products, the AB noted that the analysis under the chapeau of Article XX of the GATT 1994 entails an assessment of whether the “conditions” prevailing in the countries between which the measure allegedly discriminates are “the same”. In conducting this assessment, the subparagraph under which a measure has been provisionally justified, as well as the provision of the GATT with which a measure has been found to be inconsistent, provide important context. (EC-Seal Products (Norway), Appellate Body Report, ¶ 5.3.17)

The AB in US — Shrimp provided an overview regarding the three constitutive elements of the concept of “arbitrary or unjustifiable discrimination between countries where the same conditions prevail”. First, the application of the measure must not result in discrimination. Second, the discrimination must not be arbitrary or unjustifiable in character. Third, this discrimination must not occur between countries where the same conditions prevail. “Arbitrary discrimination”, “unjustifiable discrimination” and “disguised restriction” on international trade may, accordingly, be read side by side; they impart meaning to one another (US-Gasoline (Venezuela), Appellate Body Report, p. 25). A measure may constitute arbitrary or unjustifiable discrimination if it is applied in a rigid and inflexible manner and without any regard for the difference in conditions between countries. In this regard, prior negotiations with an affected country could make the measure satisfy the elements of the chapeau.

c. Arguments for Syldavia

Syldavia could contest that the NESI’s Decision of 2015 and SOCA Tax are not rationally related to any climate change objectives, but a disguised restriction on trade. In Brazil — Retreaded Tyres, the Appellate Body held that “the analysis of whether the application of a measure results in arbitrary or unjustifiable discrimination should focus on the cause of the discrimination, or the rationale put forward to explain its existence.” (Brazil – Retreaded Tyres (European Communities), Appellate Body Report, ¶226). Syldavia could argue that the measure has coercive effects on the textile industry in Syldavia and elsewhere, and does not take into account any advancement, which Syldavia might have adopted in its climate mitigation efforts. Specifically in the case of Borginia’s defence under Article XX of the GATT for the NESI Decision of 2015, Syldavia can argue that even powerloom industries powered with renewable energy in Syldavia are not entitled to sell their product as ‘cotton fabric’ in Borgina. Therefore, Syldavia can argue that Borginia’s measure was applied in a rigid and inflexible manner could fail the requirements of the chapeau.
d. **ARGUMENTS FOR BORGINIA**

**Objective:** The policy objectives of the NESI’s Decision of 2015 and SOCA Tax are to ensure the regulation of carbon emissions from powerloom textiles industries; to encourage carbon mitigation steps initiated by various industries and to meet Borginia’s obligation pursuant to its Nationally Determined Contributions (NDCs) under the Paris Agreement to reduce greenhouse gas emissions by 20% by 2030. Therefore, the objective falls within the scope of conservation of exhaustible natural resources.

**“Related to” Test:** Borginia could argue that to satisfy “related to” requirement, due consideration is to be given to whether there is an observably close and real relationship between the measure and the ends (US – Shrimp (India, Pakistan, Malaysia, Thailand), Appellate Body Report, ¶141). The objectives of NESI’s Decision of 2015 and SOCA Tax are primarily aimed at reduction of carbon emissions.

**Even-handedness:** The measures adopted by Borginia are also applicable on domestic handloom and powerloom textile units. Therefore, the measures are applied in an even-handed manner.

**Application of Chapeau:** Borginia could argue that its measures were not arbitrary or unjustifiably discriminatory for the following reasons:

- Before implementing NESI’s Decision of 2015, Borginia’s governmental agency NESI took various domestic measures to phase out coal based power plants and promote clean production processes in various industries.

- Additionally, Borginia hosted a meet of Environmental Ministers of the small island states in the Indian Ocean. Syldavia was also invited for the meeting. In the meeting, states agreed to take measures including the introduction of carbon taxes, labels on greenhouse gases.

- After NESI’s Decision of 2015, Borginia undertook various activities such as textile fairs, exhibitions and interactive sessions with the powerloom producers in other countries including several cities in Syldavia. It also arranged fully sponsored visits to various handloom operators in other countries including Syldavia to familiarize producers with handloom production and acquire the requisite technology.

- Furthermore, Syldavia is a signatory to the Paris Agreement. Pursuant to Article 18 of the VCLT, Syldavia is obligated not to take measures, which could defeat the object and purpose of the Paris Agreement i.e., reduction of greenhouses gases emissions.

In light of AB report in *US-Shrimp 21.5*, Borginia could argue that that its measure were designed in such a manner that there is sufficient flexibility to take into account the specific conditions prevailing in any exporting country. It took series of measures in good faith to ensure that powerloom textile manufacturers of Syldavia are not adversely affected by its measures.
I. WHETHER THE ALLOCATION OF FUNDS FROM THE TEXTILE TECHNOLOGY UPGRADE FUND SCHEME (TTUFS) TO THE TEXTILE UNITS SITUATED IN THE TEPZS IN BORGINIA CONSTITUTES A SPECIFIC SUBSIDY WITHIN THE MEANING OF ARTICLES 1 AND 2 OF THE SCM AGREEMENT?

a. LEGAL PROVISIONS

Article 1: Definition of a Subsidy

1.1 For the purpose of this Agreement, a subsidy shall be deemed to exist if:

(a)(1) there is a financial contribution by a government or any public body within the territory of a Member (referred to in this Agreement as "government"), i.e. where:

(i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e.g. loan guarantees);

...........

and

(b) a benefit is thereby conferred.

Article 2.3: Specificity

2.3 Any subsidy falling under the provisions of Article 3 shall be deemed to be specific.

b. RELEVANT JURISPRUDENCE

According to Article 1:1 of the SCM Agreement, a “subsidy” within the meaning of this agreement is deemed to exist: (i) if there is a financial contribution by a government or public body or any form of income or price support (in the sense of Article XVI of GATT 1994); and (ii) a benefit conferred. In short, subsidy comprises of a “financial contribution” and “benefit”.

“The concept of subsidy defined in Article 1 of the SCM Agreement captures situations in which something of economic value is transferred by a government to the advantage of a recipient. A subsidy is deemed to exist where two distinct elements are present. First, there must be a financial contribution by a government, or income or price support. Secondly, any financial contribution, or income or price support, must confer a benefit.”(US- Softwood Lumber IV (Canada), Appellate Body Report, ¶51)
In the facts of this case, the alleged subsidy is the case allocation of funds to textile units located in the TEPZs.

c. ARGUMENTS FOR SYLDAVIA

Syldavia needs to argue that the TTUFS measure is a financial contribution in the form of a direct transfer of funds or money (Japan- DRAMS (Korea), Appellate Body Report, ¶¶250-252); that the Ministry of Textiles is a government agency, and that the allocation of funds confers a benefit on the textile units located on the TEPZs. As a WTO panel noted, “financial contributions in the form of "grants" under Article 1.1(a)(1)(i) of the SCM Agreement have been found to confer benefits, "as they place the recipient in a better position than the recipient otherwise would have been in the marketplace", given that no entity acting pursuant to commercial considerations would make such unremunerated payments” (US- Tax Incentives (European Union), Panel Report, ¶7.163) Syldavia should further argue that the subsidy is a specific subsidy within the meaning of Article 2.3 of the SCM Agreement. Article 2.3 speaks to specificity and states that any subsidy falling under the provisions of Article 3 shall be deemed to be specific. To establish that the subsidies are specific subsidies, Syldavia should contend that subsidies, which are contingent, in law or fact, upon export performance, are prohibited under Article 3.1 (a) of the SCM Agreement and are deemed to be specific pursuant to Article 2.3 of the SCM Agreement. According to Article 3.2 of the SCM Agreement, a Member shall not grant nor maintain prohibited subsidies.

d. ARGUMENTS FOR BORGINIA

Borginia will have difficulty contesting these points, and may choose not to contest that the measures are subsidies. They could argue however that the measures are not specific because they are not export contingent subsidies falling under the provisions of Article 3 of the SCM Agreement.

II. WHETHER THE ALLOCATION OF FUNDS FROM THE TEXTILE TECHNOLOGY UPGRADE FUND SCHEME TO THE TEXTILE UNITS SITUATED IN THE TEPZS IN BORGINIA ARE EXPORT-CONTINGENT SUBSIDIES WITHIN THE MEANING OF ARTICLES 3.1(a) OF THE SCM AGREEMENT?

a. LEGAL PROVISIONS

Article 3: Prohibition

3.1 Except as provided in the Agreement on Agriculture, the following subsidies, within the meaning of Article 1, shall be prohibited:
(a) subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I5;

Footnote 4: The standard is met when the facts demonstrate that the granting of a subsidy, without having been made legally contingent upon export performance, is in fact tied to actual or anticipated exportation or export earnings. The mere fact that the subsidy is granted to enterprises, which export shall not for that reason alone be considered to be an export subsidy within the meaning of this provision.
Footnote 5: Measures referred to in Annex I as not constituting export subsidies shall not be prohibited under this or any other provision of this Agreement.

b. **RELEVANT JURISPRUDENCE**

For a subsidy to be “contingent… in fact”, it should be “conditioned” upon export performance. The AB made this aspect very clear in *EC – Aircraft*:

“...The Appellate Body explained in Canada – Aircraft that the word “contingent” means “conditional” or "dependent for its existence on something else", and that the legal standard for export contingency expressed in Article 3.1(a) is the same for both de jure and de facto contingency. With regard to the standard for de facto export contingency set out in footnote, the Appellate Body noted that the ordinary meaning of the word “tie” in the first sentence of the footnote is to “limit or restrict as to ... conditions”. The Appellate Body thus found that to satisfy the standard for de facto export contingency “a relationship of conditionality or dependence” must be demonstrated between the subsidy and “actual or anticipated exportation or export earnings”. The Appellate Body further observed that the meaning of the word "anticipated" under footnote 4 is “expected”, and that “{w}hether exports were anticipated or 'expected' is to be gleaned from an examination of objective evidence.” The Appellate Body stressed, however, that the use of this word does not transform the standard for “contingent ... in fact” into a standard that is satisfied by merely ascertaining "expectations" of exports on the part of the granting authority. The Appellate Body explained that, although a subsidy “may well be granted in the knowledge, or with the anticipation, that exports will result”, “that alone is not sufficient, because that alone is not proof that the granting of the subsidy is tied to the anticipation of exportation.””  

(EC – Aircrafts (United States), Appellate Body Report, ¶ 1037)

In *US- Carbon Steel*, the AB observed:

“Proving de facto ... contingency is a much more difficult task. There is no single legal document which will demonstrate, on its face, that a subsidy is “contingent ... in fact...”. Instead, the existence of this relationship of contingency, between the subsidy and ... performance, must be inferred from the total configuration of the facts constituting and surrounding the granting of the subsidy, none of which on its own is likely to be decisive in any given case.”  

(US – Carbon Steel (European Communities), Appellate Body Report, ¶ 7.209)

In *Canada – Auto Parts*, the AB observed that:

A subsidy is contingent ‘in law’ upon export performance when the existence of that condition can be demonstrated on the basis of the very words of the relevant legislation, regulation or

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2Appellate Body Report, *Canada – Aircraft*, ¶171. Similarly, in *Canada – Autos*, the Appellate Body noted that footnote 4 to Article 3.1(a) uses the words “tied to” as a synonym for “contingent” or "conditional" and that, consequently, a "tie", amounting to the relationship of contingency, between the granting of the subsidy and actual or anticipated exportation meets the legal standard of "contingent" in Article 3.1(a) of the *SCM Agreement*.  
(Appellate Body Report, *Canada – Autos*, ¶107)
other legal instrument constituting the measure (Canada- Auto (Japan), Appellate Body Report, ¶100). Regarding the interpretation of the term “contingent … in fact”, the Panel in Australia — Automotive Leather II established a standard of “close connection” between the grant or maintenance of a subsidy and export performance.

In EC — Aircraft, the AB established the following test for determining whether a subsidy is de facto contingent on export performance:

“The existence of de facto export contingency, as set out above, "must be inferred from the total configuration of the facts constituting and surrounding the granting of the subsidy", which may include the following factors: (i) the design and structure of the measure granting the subsidy; (ii) the modalities of operation set out in such a measure; and (iii) the relevant factual circumstances surrounding the granting of the subsidy that provide the context for understanding the measure's design, structure, and modalities of operation.” (EC – Aircrafts (United States), Appellate Body Report, ¶ 1046)

c. ARGUMENTS FOR SYLDAVIA

Syldavia may want to concede that the allocation of funds from the TTUFS to textile units in TEPZs is not contingent in law upon export performance, and instead argue that it is contingent in fact upon export performance. In order to meet the standards of de facto contingency, Syldavia may have to argue that the subsidies provide an incentive to the textile units in TEPZs to export in a manner which is not reflective of the conditions of supply and demand in the domestic and export markets. The strength of this argument will depend on the evidence presented by Syldavia. Syldavia may highlight the following facts:

- TEPZ are deemed export zones and the TEPZs’ textile units are major recipients of export earnings for Borginia. For textile units to continue their presence in TTUFS, the textiles units have to export 80% of the output. Non-compliance could lead to "adverse consequences" including suspension of export license, as has been clarified in the moot problem.
- Only textile units in TEPZs can receive the subsidies, and textile units operating in TEPZs are required to export 80% of their production, a requirement which is strictly enforced. The requirement to export is not merely an expectation but a necessity. Thus, the subsidies are “conditional”, “dependent” on, or “tied to” actual or anticipated exportation or export earnings.

d. ARGUMENTS FOR BORGINIA

Borginia could argue that the allocation of funds is not contingent in law upon export performance because nothing in the words of the legislation itself ties that allocation to export performance.

Regarding contingency in fact, Borginia could argue that the mere fact that a subsidy is granted to enterprises that export, or that the granting authority anticipated exportation, is not sufficient to establish export contingency; rather, the subsidy must be “geared to induce the promotion of future export performance by the recipient”. Borginia could rely upon the finding of the AB in EC- Large Civil Aircraft which reads as follows: “…the conditional relationship between the granting of the subsidy and export performance must be objectively observable on the basis of such evidence in order for the subsidy to be geared to induce the promotion of future export performance by the recipient. The standard for de facto contingency is therefore not satisfied
by the subjective motivation of the granting government.” (EC – Large Civil Aircraft (United States), Appellate Body Report, ¶1050). Thus, the fact that textile units in the TEPZs export, and that the Ministry was aware of that fact, is not sufficient to demonstrate export contingency.

To that extent, Borginia could argue that the contingency is not satisfied by the subjective motivation of the granting government to promote the future export performance (EC – Large Civil Aircraft (United States), Appellate Body Report, ¶1050). Accordingly, Borginia’s Textile Ministry’s intention is rather irrelevant in examining whether the measure qualifies as an export subsidy under the SCM Agreement.

As for the indication that textile units in the TEPZs “have to sell” more than 80% of their production in export markets, Borginia could argue there was no indication that the textile units would lose access to the subsidies, or be forced to cease operation in the TEPZs, if they did not export. Borginia could contend that the reference to 80% sales is merely reflective of increasing demand for cotton textiles, especially handloom products in global markets. Sales within the TEPZs or the domestic tariff area (DTA) are an option available to the units located in the TEPZs. A failure to meet export obligations, by itself, does not lead to loss or forfeiture of TEPZ funds. Thus, Syldavia had not demonstrated that the subsidies are “dependent” upon exportation.

III. WHETHER THE ALLOCATION OF FUNDS FROM THE TEXTILE TECHNOLOGY UPGRADE FUND SCHEME TO THE TEXTILE UNITS SITUATED IN THE TEPZS IN BORGINIA IS INCONSISTENT WITH THE REQUIREMENTS OF ARTICLE 27.4 AND 27.5 AND, ACCORDINGLY, A PROHIBITED SUBSIDY UNDER ARTICLE 3.1 (A) OF THE SCM AGREEMENT?

a. LEGAL PROVISIONS

Article 27
Special and Differential Treatment of Developing Country Members
27.2 The prohibition of paragraph 1(a) of Article 3 shall not apply to:
(a) developing country Members referred to in Annex VII.
(b) other developing country Members for a period of eight years from the date of entry into force of the WTO Agreement, subject to compliance with the provisions in paragraph 4.

27.4 Any developing country Member referred to in paragraph 2(b) shall phase out its export subsidies within the eight-year period, preferably in a progressive manner. However, a developing country Member shall not increase the level of its export subsidies, and shall eliminate them within a period shorter than that provided for in this paragraph when the use of such export subsidies is inconsistent with its development needs. If a developing country Member deems it necessary to apply such subsidies beyond the 8-year period, it shall not later than one year before the expiry of this period enter into consultation with the Committee, which will determine whether an extension of this period is justified, after examining all the relevant economic, financial and development needs of the developing country Member in question. If the Committee determines that the extension is justified, the developing country Member concerned shall hold annual consultations with the Committee to determine the necessity of maintaining the subsidies. If
no such determination is made by the Committee, the developing country Member shall phase out the remaining export subsidies within two years from the end of the last authorized period.

27.5 A developing country Member which has reached export competitiveness in any given product shall phase out its export subsidies for such product(s) over a period of two years. However, for a developing country Member which is referred to in Annex VII and which has reached export competitiveness in one or more products, export subsidies on such products shall be gradually phased out over a period of eight years.

27.6 Export competitiveness in a product exists if a developing country Member’s exports of that product have reached a share of at least 3.25 per cent in world trade of that product for two consecutive calendar years. Export competitiveness shall exist either (a) on the basis of notification by the developing country Member having reached export competitiveness, or (b) on the basis of a computation undertaken by the Secretariat at the request of any Member. For the purpose of this paragraph, a product is defined as a section heading of the Harmonized System Nomenclature. The Committee shall review the operation of this provision five years from the date of the entry into force of the WTO Agreement.

Annex VII

Annex VII: Developing Country Members Referred to in Paragraph 2(A) of Article 27

The developing country Members not subject to the provisions of paragraph 1(a) of Article 3 under the terms of paragraph 2(a) of Article 27 are:

(a) Least-developed countries designated as such by the United Nations which are Members of the WTO.

(b) Each of the following developing countries which are Members of the WTO shall be subject to the provisions which are applicable to other developing country Members according to paragraph 2(b) of Article 27 when GNP per capita has reached $1,000 per annum:(68) Bolivia, Cameroon, Congo, Côte d’Ivoire, Dominican Republic, Egypt, Ghana, Guatemala, Guyana, India, Indonesia, Kenya, Morocco, Nicaragua, Nigeria, Pakistan, Philippines, Senegal, Sri Lanka and Zimbabwe.

(footnote original) 68 The inclusion of developing country Members in the list in paragraph (b) is based on the most recent data from the World Bank on GNP per capita.

b. RELEVANT JURISPRUDENCE

i. Application of the Prohibition on Export Subsidies to developing countries

By virtue of Article 27 and Annex VII of the SCM Agreement, the prohibition on export subsidies does not apply, inter alia, to the (low-income) countries listed in Annex VII(b) until
their gross national income (GNI) per capita has reached $1,000 per annum (Annex VII(b) countries). At the WTO's Ministerial Conference in Doha, Ministers decided in their Decision on Implementation-related Issues and Concerns (WT/MIN(01)17), para. 10.1, that Annex VII(b) "includes the Members that are listed therein until their GNP per capita reaches US$1000 in constant 1990 dollars for three consecutive years", and that a Member shall not leave Annex VII(b) until its GNP has reached that level "based upon the most recent data from the World Bank". In practice, the WTO Secretariat circulates the calculations it receives from the World Bank to the SCM Committee each year. The Ministers at Doha further decided (¶10.4) that a developing country Member that graduates from Annex VII(b) "shall be re-included in it when its GNP per capita falls back below US $1000."

Even for countries in Annex VII(b), however, the flexibility to offer export subsidies does not exist for products that have reached export competitiveness. In that case, those export subsidies offered by Annex VII developing countries have to be phased out within eight years. According to Article 27.6, export competitiveness in a product exists ‘if a developing country Member’s exports of that product have reached a share of at least 3.25% in world trade of that product for two consecutive calendar years’. Export competitiveness may be established based either upon a notification by the Member concerned, or on the basis of a computation by the Secretariat at the request of any Member.

With regard to Annex VII developing countries, only two such requests have been formulated so far, both made by the United States (2003, 2010) regarding India’s export competitiveness on textile and apparel exports. These computations revealed two ambiguities in the interpretation of Article 27.6. First, Article 27.6 is ambiguous as to whether products should be defined at the section or heading level of the Harmonized System (HS) Nomenclature. The uncertainty flows from the definition of a ‘product’ in Article 27.6, which refers to ‘a section heading’ of the HS Nomenclature, though the HS itself only contains ‘sections’ (group of chapters) or ‘headings’ (four-digit tariff level). Second, the text does not clarify whether the denominator for the world trade computation includes trade between EU member States (since both the EU collectively and its member States individually are WTO Members). Thus, Secretariat calculations provide calculations at both the section and heading level, and both including and excluding intra-EU trade.

On the other hand, the authentic French and Spanish texts refer to ‘positions’ and ‘partidas’ respectively, which correspond to four-digit ‘headings’ instead of ‘sections’. To resolve this, one may have to look at rules of treaty interpretation codified in the VCLT 1969. Pursuant to Article 33(3) of the VCLT, the terms of the treaty are presumed to have the same meaning in each authentic text. Accordingly, products should be defined at the four-digit heading level because this meaning, arguably “best reconciles” the three texts. There is a view that to resolve this ambiguity, recourse to preparatory work should be taken (Article 32 of the VCLT). According to Hoda and Ahuja, the level of aggregation negotiators had in mind was “sections” and not “headings” (See A. Hoda and R. Ahuja, ‘Agreement on Subsidies and Countervailing Measures: Need for Clarification and Improvement’, 39:6 Journal of World Trade 1009 (2005); Dominic Coppens, How Special is the Special and Differential Treatment under the SCM Agreement? A Legal and Normative Analysis of Subsidy Disciplines on Developing Countries, World Trade Law Review (2013)).

<table>
<thead>
<tr>
<th>Category of Developing Country Member</th>
<th>Duration of exemption</th>
<th>Period during which export subsidies have to be gradually phased out in case export competitiveness</th>
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<th>Least-developed countries designated as such by the United Nations (Article 27.2(a) in conjunction with Annex VII (a))</th>
<th>Indefinite, unless export competitiveness has been reached pursuant to Article 27.6</th>
<th>Eight years (second sentence of Article 27.5 in conjunction with Article 27.6)</th>
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<tr>
<td>Annex VII(b) countries: they are treated like least-developed countries until their GNP per capita has reached USD 1,000 per annum. Once this threshold has been reached they are treated as other developing country Members.</td>
<td>Indefinite, unless export competitiveness has been reached pursuant to Article 27.6</td>
<td>Eight years (second sentence of Article 27.5 in conjunction with Article 27.6). However, if GNP per capita has reached USD 1,000 per annum, these countries are treated like Article 27.2(b) countries, see line below</td>
</tr>
<tr>
<td>Other developing country Members (Article 27.2(b))</td>
<td>Eight years (but progressive phasing out during that period is preferable) if following conditions are met: - no increase of the level of export subsidies (second sentence of Article 27.4); - elimination within a shorter period than eight years when use of export subsidies is inconsistent with its development needs (second sentence of Article 27.4) - country did not reach export competitiveness (Article 27.5) Possibility to receive extensions of the eight-year period pursuant to Article 27.4</td>
<td>Two years (first sentence of Article 27.5 in conjunction with Article 27.6)</td>
</tr>
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The Panel in Brazil-Aircraft stated that:

"Where, as here, it is agreed that the Member in question is a developing country Member within the meaning of Article 27.2(b), it is for the Member alleging a violation of Article 3.1(a) of the SCM Agreement to demonstrate that the
substantive obligation in that provision -- the prohibition on export subsidies -- applies to the developing country Member complained against. That is, it is for the complaining Member to demonstrate that the developing country Member in question is not in compliance with at least one of the elements laid out in Article 27.4. In light of the above, we consider that, in order to determine whether Brazil has acted inconsistently with Article 3.1(a), it is for Canada to establish that Article 3.1(a), in fact, applies to Brazil at the present time. Accordingly, we find that Canada bears the burden of proving that Brazil is not in compliance with the provisions of Article 27.4." (Brazil – Aircraft (Canada), Panel Report, ¶ 7.57)

c. **ARGUMENTS FOR SYLDAVIA**

**Annex VII(b):** Syldavia could argue that as of 2014 Borginia's GNP per capita has exceeded SUS1000 per annum in constant 1990 dollars for three consecutive years and that accordingly the provisions of Article 3.1(a) of the SCM Agreement now apply to Borginia. Accordingly, Borginia is now prohibited from providing any export subsidies, irrespective of whether or not it has achieved export competitiveness in any given product. Should Borginia argue that under Article 27.2(b) it is now entitled to eight years to phase out its export subsidies, Syldavia could respond that this provision allows Members eight years from the date of entry into force of the WTO Agreement, i.e. 1995.

**Export Competitiveness:** In the alternative, and if its arguments under Annex VII(b) are rejected, Syldavia could contend that Borgia has in any event reached export competitiveness with respect to products under HS Code 5208.08, as exports of these products exceeded 3.25% of world trade for two consecutive calendar years (2014 and 2015). In order to prevail, Syldavia would need to establish that in determining export competitiveness the product should be defined at 6-digit level i.e., at the subheading level. [In this regard, Syldavia could interpret the meaning of “product” by using as context the Agreement on Textiles and Clothing, the Agreement on Rules of Origin, and the Agreement on Agriculture.] The reference to the term “products” in the Annex to the Textiles and Clothing explicitly refers to the HS Codes at the six-digit level. This could be useful and relevant context in deciphering the meaning of a particular textile and clothing product. Moreover, the World Customs Organization that has developed the Harmonized Commodity Description and Coding System (HS), identified commodities at 6-digit level in HS Codes.

**Phase-out Period for Export Competitive Products:** Because Borgia has graduated from Annex VII, it was required to phase out its export subsidies to this product within two years, i.e., by 2017. As the Panel was established in 2018, that period has now passed and Borgia's export subsidies to this product are now prohibited.

d. **ARGUMENTS FOR BORGINIA**

**Annex VII(b):** Borgia may choose not to contest that it has graduated from Annex VII(b) of the SCM Agreement. Alternatively, it might note that as the burden is upon Syldavia to show that Article 3.1(a) applies to Borgia, Syldavia must demonstrate that Borgia's GNP per capita has not fallen back below US $1000 such that it has not been re-included in Annex VII(b), and there is no data on the record on this point.

In any event, Borgia could argue that under the terms of Annex VII(b) it is now “subject to the provisions applicable to other developing country Members according to paragraph 2(b) of
Article 27…”. Since such developing country Members are entitled under Article 27.4 to an eight-year period to phase out their export subsidies, Borginia could argue that it has until at least 2022 (eight years after its Annex VII(b) graduation) to phase out its export subsidies. Until that time, Article 3.1(a) does not apply to Borginia, so long as it complies with the requirements of Article 27.4. In this respect, under Brazil-Aircraft, the burden is upon the complainant to demonstrate that Article 3.1(a) applies to a developing country Member listed in Article 27.2(b), and Syldavia has made no such showing.

**Export Competitiveness:** Borginia could argue that under Article 27.6 the term “product” refers to a “section heading”. While this term may be ambiguous, it could either refer to a “section” of the HTS (a group of chapters), or to a “heading”, but in any event there is no basis to understand it to refer to a subheading, as argued by Syldavia. Borginia could find support for this interpretation in the Spanish and French versions of the text (“positions” and “partidas”), both of which correspond to “heading”, but not to “subheading”. Borginia could also contend that if Syldavia wishes to accord the term ‘product’ a special meaning—that the product refers to a tariff line at the six-digit level - Syldavia has to establish this special meaning under Article 31(4) of the VCLT. Since there was no evidence that Syldavia had achieved export competitiveness at the section or heading level, there was no basis to contend that Article 3.1(a) applied to such products. Finally, Borginia could point out that it is unclear whether world trade includes intra-EU trade, nor whether the Secretariat's calculations include intra-EU trade. Because Syldavia has not established the proper meaning of Article 27.6 in this regard, nor established whether or not the Secretariat's calculations include such trade, it has not met its burden of proof.

**Phase-out Period for Export-competitive Products:** Finally, Borginia could argue that, even if it were found to be export competitive in certain products, as an Annex VII(b) country, it has eight years to phase out its export subsidies for such products. Since that time period has not yet passed, it cannot yet be in violation of Article 3.1(a).