

**BEFORE THE APPELLATE BODY  
OF THE WORLD TRADE ORGANIZATION**

***PHILIPPINES – TAXES ON DISTILLED SPIRITS***  
**(AB-2011-6/DS396, DS403)**

**Third Participant Written Submission of Australia**

**14 October 2011**

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<b>Short Title</b>	<b>Full Case Title and Citation</b>
Panel Report	Panel Report, <i>Philippines – Taxes on Distilled Spirits</i> WT/DS396/R, WT/DS403/R (circulated on 15 August 2011)
<i>Brazil-Tyres</i>	Appellate Body Report, <i>Brazil-Measures Affecting Imports of Retreaded Tyres</i> , WT/DS332/AB/R, adopted 3 December 2007
<i>Chile-Alcoholic Beverages</i>	Panel Report, <i>Chile – Taxes on Alcoholic Beverages</i> , WT/DS87/R, WT/DS110/R, adopted 12 January 2000, as modified by Appellate Body Report WT/DS87/AB/R, WT/DS110/AB/R
<i>EC-Asbestos</i>	Appellate Body Report, <i>European Communities - Measures Affecting Asbestos and Asbestos-Containing Products</i> , WT/DS135/AB/R, adopted 5 April 2001
<i>Japan –Alcoholic Beverages II</i>	Appellate Body Report, <i>Japan – Taxes on Alcoholic Beverages</i> , WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996
<i>Japan –Alcoholic Beverages II</i>	Panel Report, <i>Japan – Taxes on Alcoholic Beverages</i> , WT/DS8/R, WT/DS10/R, WT/DS11/R, adopted 1 November 1996, as modified by Appellate Body Report WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R
<i>Korea-Alcoholic Beverages</i>	Appellate Body Report, <i>Korea – Taxes on Alcoholic Beverages</i> , WT/DS75/AB/R, WT/DS84/AB/R, adopted 17 February 1999
<i>Korea-Alcoholic Beverages</i>	Panel Report, <i>Korea – Taxes on Alcoholic Beverages</i> , WT/DS75/R, WT/DS84/R, adopted 17 February 1999, as modified by Appellate Body Report WT/DS75/AB/R, WT/DS84/AB/R
<i>Mexico-Taxes on Soft Drinks</i>	Panel Report, <i>Mexico – Tax Measures on Soft Drinks and Other Beverages</i> , WT/DS308/R, adopted 24 March 2006, as modified by Appellate Body Report WT/DS308/AB/R

## I. INTRODUCTION

1. The Philippines' appeal in respect of certain aspects of the panel's findings in *Philippines – Taxes on Distilled Spirits* under the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (DSU) raises systemic issues concerning the application of obligations of WTO Members under the *General Agreement on Tariffs and Trade 1994* (GATT 1994). In particular, the appeal raises systemic issues as to the proper application of the terms "like products" and "directly competitive or substitutable products" under Article III:2 and *Ad Article III* of GATT 1994. The appeal also raises systemic issues in relation to the panel's obligation to conduct "an objective assessment of the matter before it" pursuant to Article 11 of the DSU.
2. The European Union's appeal in this dispute similarly raises systemic issues, which Australia will briefly address in this submission, on the relationship between the first and second sentences of Article III:2 of GATT 1994.

## II. AUSTRALIA'S SUBMISSION ON THE PANEL'S FINDINGS

### A. ARTICLE III:2 OF GATT 1994 – "LIKE PRODUCTS"

3. The Philippines alleges that the panel erred in its finding that spirits which meet the raw materials requirement<sup>1</sup> and those that do not are "like" products for the purposes of the first sentence of Article III:2 of GATT 1994.
4. In relation to this claim, Australia refers largely to its views as expressed during the panel stage of this dispute. In its third party submission Australia referred to the body of WTO jurisprudence on this issue, and submitted that the determination of whether products are "like" for the purposes of the first sentence of Article III:2 of GATT 1994 should be undertaken on a case-by-case basis through the application of established criteria such as the product's end-uses in a given market, and its properties, nature, and quality.<sup>2</sup>
5. The Philippines asserts in its Appellant submission that "[t]he narrow scope of the category of 'like products' has meant that any significant physical difference, even those that may not be perceptible to the consumer, will be considered sufficient to

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<sup>1</sup> Section 141 of *National Internal Revenue Code of 1997* (Philippines) applies a lower rate of tax to spirits made from specified raw materials which are commercially produced in the same country where they are processed into distilled spirits. Australia refers to this requirement as the 'the raw materials requirement'.

<sup>2</sup> Appellate Body Report, *Japan-Alcoholic Beverages II* adopted the approach for interpreting 'like or similar products' under GATT 1947 as set out in the Report of the Working Party on *Border Tax Adjustments*, adopted by the CONTACTING PARTIES in 1970, which provided:

...the interpretation of the term should be examined on a case-by-case basis. This would allow a fair assessment in each case of the different elements that constitute a "similar" product. Some criteria were suggested for determining, on a case-by-case basis, whether a product is "similar": the product's end-uses in a given market; consumers' tastes and habits, which change from country to country; the product's properties, nature and quality (cited at p. 20).

The Appellate Body added that '[u]niform classification in tariff nomenclatures based on the Harmonized System (the "HS") was recognized in GATT 1947 practice as providing a useful basis for confirming "likeness" in products.' (at p. 22) ; see also Australia Third Party Submission, paras 9 and 10.

disqualify a product from being considered ‘like’ another product.”<sup>3</sup> In Australia’s view, such a statement appears to overstate the importance of the physical characteristics of a product to the like product analysis. Australia considers that while this is one element of such an analysis it is not, on its own, determinative; rather, the evidence must be examined as a whole.<sup>4</sup>

6. While Australia agrees with the Philippines’ contention in its Appellant submission that “like” products should be narrowly construed,<sup>5</sup> Australia submits that this does not extend to the conclusion that *any* physical difference, for example a difference in raw ingredients, would necessarily disqualify a product from being considered “like” another product. In Australia’s view, it is the role of a panel to determine on a case-by-case basis whether a difference between products is significant enough to disqualify them from being considered “like” products. For example, the panel in *Japan-Alcoholic Beverages II*, identified the appropriate standard in that case to be “[s]ubstantial noticeable differences in physical characteristics”.<sup>6</sup> Australia further observes that assessing the significance of differences in physical characteristics between products should not be limited to consideration of a single characteristic, but should be an assessment based on all the physical characteristics of the products at issue such as appearance, ingredients, flavour and smell.
7. In comparing the range of physical characteristics of spirits which meet the raw materials requirement and those that do not, Australia observes that the facts in this dispute appear to indicate that the raw materials used in the products do not materially alter consumer perception of the product; rather such perception appears to be affected by the appearance, taste, and smell of the product, as well as its marketing as a particular type of spirit, such as brandy, gin, etc.
8. On this point, Australia considers that the finding of the panel in *Mexico – Soft Drinks* “that beet sugar and cane sugar are ‘like products’ within the meaning of the first sentence of Article III:2, as sweeteners in the production of soft drinks and syrups”, is of particular relevance.<sup>7</sup> Of similar relevance is the panel’s conclusion in *Japan-Alcoholic Beverages II* that vodka and shochu were “like” products for the purposes of Article III:2 on the basis that they were both clean spirits; made of *similar* raw materials; and their end-uses were virtually identical.<sup>8</sup>
9. In Australia’s view, in a “like” product analysis, no one criterion is determinative; rather all the factors and evidence should be weighed and balanced. Additionally, this process should be undertaken in a flexible manner on a case-by-case basis to ensure that Article III:2 of GATT 1994 is applied in a manner that is consistent with its objectives and purpose.

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<sup>3</sup> Philippines Appellant Submission, para. 30.

<sup>4</sup> Appellate Body Report, *EC-Asbestos*, para. 109; see also Australia Third Party Submission, para 11.

<sup>5</sup> Philippines Appellant Submission, para. 27; see also Australia Third Party Submission, para 10.

<sup>6</sup> Panel Report, *Japan-Alcoholic Beverages II*, para. 6.23. Emphasis added.

<sup>7</sup> Panel Report, *Mexico – Soft Drinks*, para. 8.36.

<sup>8</sup> Panel Report, *Japan-Alcoholic Beverages II*, para. 6.23. Emphasis added. See also Australia Third Party Submission, para. 16.

**B. ARTICLE III:2 AND AD ARTICLE III OF GATT 1994 – “DIRECTLY COMPETITIVE OR SUBSTITUTABLE PRODUCTS”**

10. The Philippines argues in its Appellant submission that the panel in this dispute has erred in its reasoning in respect of the second sentence of Article III:2 of GATT 1994, including by failing to consider the “degree of proximity of the products’ competitive relationship”;<sup>9</sup> by comparing “everyday” products with “special occasion” products;<sup>10</sup> by finding that it was sufficient that products are available to consumers within a certain segment of the market;<sup>11</sup> and by relying on speculation as to potential future competitive relationships between products rather than assessing the actual competitive relationship between products.<sup>12</sup>
11. Australia considers that a useful starting point for assessing a “directly competitive or substitutable” relationship under *Ad Article III* of GATT 1994, for the purposes of a claim under the second sentence of Article III:2 of GATT 1994 is the panel report in *Korea-Alcoholic Beverages* which stated that:

[A]n assessment of whether there is a direct competitive relationship between two products or groups of products requires evidence that consumers consider or could consider the two products or groups of products as alternative ways of satisfying a particular need or taste.<sup>13</sup>
12. WTO panels have used comparable approaches to develop criteria that may be applied in determining whether such a directly competitive relationship exists. For example, in *Korea-Alcoholic Beverages* the panel considered evidence of a direct competitive relationship to include “comparisons of their physical characteristics, end-uses, channels of distribution and prices”.<sup>14</sup> In contrast to the characterisation of “like” products under the first sentence of Article III:2 of GATT 1994, the panel in *Japan-Alcoholic Beverages II* found that “the decisive criterion” in determining whether products are “directly competitive or substitutable”, “is whether they have common end uses, *inter alia*, as shown by elasticity of substitution”.<sup>15</sup>
13. In this respect it is, in Australia’s view, relevant that domestically produced and imported spirits are marketed as the same “type” of spirit (i.e., gin, whisky, etc.), often using similar packaging and branding<sup>16</sup> and that the nature and content of the products’ marketing strategies seem to indicate that they are competing for a similar market segment.<sup>17</sup>

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<sup>9</sup> Philippines Appellant Submission, para. 88.

<sup>10</sup> Philippines Appellant Submission, para. 96.

<sup>11</sup> Philippines Appellant Submission, para. 102.

<sup>12</sup> Philippines Appellant Submission, para. 107.

<sup>13</sup> Panel Report, *Korea – Alcoholic Beverages*, para. 10.40.

<sup>14</sup> Panel Report, *Korea – Alcoholic Beverages*, para. 10.43. A similar approach was taken by the panel in *Chile-Alcoholic Beverages* (Panel Report, para. 7.30). See also Australia Third Party Submission, paras 30-31.

<sup>15</sup> Panel Report, *Japan-Alcoholic Beverages II*, para. 6.22; Appellate Body Report, *Japan-Alcoholic Beverages II*, p. 25. See also Australia Third Party Submission, para. 37.

<sup>16</sup> United States First Written Submission, para. 97.

<sup>17</sup> European Union First Written Submission, para. 77.

14. The Philippines argues in its appeal that products purchased only on “special occasions” cannot directly compete with more frequently purchased “everyday” products. However, in Australia’s view there is no jurisprudence to support such a contention. Australia notes that in a similar context, the panel in *Korea-Alcoholic Beverages* distinguished alcoholic beverages as frequently purchased consumer goods, finding that even a lower income earner “can afford to purchase a bottle of a more expensive beverage at least occasionally”.<sup>18</sup> Thus, Australia observes that previous panels have found that products with different net retail prices can be “directly competitive” even if the products are not purchased with the same frequency.<sup>19</sup>
15. In relation to the Philippines’ allegations as to the “speculative” nature of the panel’s decision, Australia observes that previous panels have taken into account evidence of both the existing market competition as well as evidence of future potential market competition between products. For example, the panel in *Chile-Alcoholic Beverages* concluded that, “[t]he current actual overlap in end-uses *plus the evidence of potential overlap*, is supportive of a conclusion that pisco and the imported distilled spirits are directly competitive or substitutable”.<sup>20</sup> Indeed, in Australia’s view, there must, to a certain degree, be consideration of potential future direct competition where a product is denied equality of competition in the market due to discriminatory treatment on the basis that such treatment must have an effect on the existing competitive relationship between products.

#### **C. RELATIONSHIP BETWEEN THE FIRST AND SECOND SENTENCE OF ARTICLE III:2 OF GATT 1994**

16. The European Union, in its Other Appellant submission, makes a number of assertions in respect of the relationship between the first and second sentence of Article III:2 of GATT 1994. Australia agrees that the Appellate Body’s finding in *Korea-Alcoholic Beverages* provides a useful overview of the relationship between the term “like” for the purposes of the first sentence of Article III:2 of GATT 1994, and the term “directly competitive or substitutable”<sup>21</sup> for the purposes of applying the second sentence, stating that:

[t]he first sentence of Article III:2 also forms part of the context of the term. “Like” products are a subset of directly competitive or substitutable products: all like products are, by definition, directly competitive or substitutable products...<sup>22</sup>

17. On the basis of the Appellate Body’s reasoning, the European Union asserts that if a panel makes a finding that there has been a violation of the first sentence of Article III:2 then this would “almost automatically lead to a finding of a breach of the second sentence of the same provision” and that in such circumstances “the Panel could have

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<sup>18</sup> Panel Report, *Korea – Alcoholic Beverages*, para. 10.74.

<sup>19</sup> Panel Report, *Korea – Alcoholic Beverages*, para. 10.74; Panel Report, *Chile-Alcoholic Beverages*, para. 7.37.

<sup>20</sup> Panel Report, *Chile-Alcoholic Beverages*, para. 7.47. Emphasis added.

<sup>21</sup> See *Ad Article III* of GATT 1994.

<sup>22</sup> Appellate Body Report, *Korea – Alcoholic Beverages*, para. 118. See also Panel Report, *Japan-Alcoholic Beverages II*, para. 6.22.

immediately ruled on the second claim without a new overall assessment.”<sup>23</sup>

Australia agrees that the Appellate Body’s reasoning in *Korea-Alcoholic Beverages* provides scope to argue that a finding that products are “like” under the first sentence could lead to a panel to automatically conclude that those same products were “directly competitive or substitutable”<sup>24</sup> for the purposes of determining a claim under the second sentence.

18. However, Australia observes that the Appellate Body in *Korea-Alcoholic Beverages* also reasoned that “not all ‘directly competitive or substitutable’ products are ‘like’”.<sup>25</sup> Therefore, in some circumstances the range of products which are “directly competitive or substitutable” in a dispute may be broader than those products which are considered “like”. On this basis, Australia submits that a panel should be cautious in exercising judicial economy on this issue, as the identification of the scope of products which are “directly competitive or substitutable” (as distinct from “like” products) may be material to enabling a complete analysis of a claim under the second sentence of Article III:2 of GATT 1994.
19. In any event, Australia does not agree with the contention that a finding of a violation of the first sentence of Article III:2 of GATT 1994 means that a violation of the second sentence is automatic. In Australia’s view, the panel would still need to give full consideration to all three elements of a claim under the second sentence of Article III:2 of GATT 1994, articulated by the Appellate Body in *Japan-Alcoholic Beverages II* as follows:

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

Again, these are three separate issues. Each must be established separately by the complainant for a panel to find that a tax measure imposed by a Member of the WTO is inconsistent with Article III:2, second sentence.<sup>26</sup>

#### **D. ARTICLE 11 OF THE DSU**

20. The Philippines’ final claim in its appeal is that the panel has violated Article 11 of the DSU by failing to conduct “an objective assessment of the matter before it, including an objective assessment of the facts of the case”. Australia understands the Philippines’ allegations in respect of this claim to include that the panel disregarded expert testimony;<sup>27</sup> failed to properly interpret scientific evidence and survey data;<sup>28</sup>

<sup>23</sup> European Union Other Appellant Submission, para. 17.

<sup>24</sup> See *Ad Article III* of GATT 1994.

<sup>25</sup> Appellate Body Report, *Korea – Alcoholic Beverages*, para. 118.

<sup>26</sup> Appellate Body Report, *Japan-Alcoholic Beverages II*, p. 24. See also *Ad Article III* of GATT 1994.

<sup>27</sup> See Philippines Appellant Submission, paras. 143, 149, 152, 173 and 177.

<sup>28</sup> See Philippines Appellant Submission, paras. 143, 147, 156, and 162.

and reached conclusions in relation to facts which were unsupported by the evidence adduced by the parties to the dispute.<sup>29</sup>

21. In essence then, the Appellate Body is called upon to determine whether the panel has made an “objective assessment” of the evidence adduced by the parties. To this end, Australia considers that the general principles articulated by the Appellate Body in *Brazil-Tyres* in relation to what constitutes an “objective assessment” provide a useful starting point:

[An objective] assessment implies, among other things, that a panel must consider all the evidence presented to it, assess its credibility, determine its weight, and ensure that its factual findings have a proper basis in that evidence.

Within these parameters, it is generally “within the discretion of the panel to decide which evidence it chooses to utilise in making findings”... and the Appellate Body “will not interfere lightly with the panel’s exercise of its discretion”.<sup>30</sup>

22. Australia refrains from stating a view as to whether, in this case, the panel has “exceeded the bounds of its discretion, as the trier of facts, in its appreciation of the evidence.”<sup>31</sup> However, Australia observes that the Philippines has made five separate allegations in respect of its claim that the panel has not complied with its obligations under Article 11 of the DSU to make an “objective assessment” of the facts. In Australia’s view, claims under Article 11 should only be considered where allegations are serious in nature as such claims go to the heart of the WTO dispute panel’s primary responsibility in the resolution of disputes. From a systemic perspective, it would be of concern to Australia if claims of a frivolous nature were made under Article 11 in an attempt to “retry” the facts of a dispute and require the Appellate Body to, in effect, second-guess a panel’s conclusions.
23. Finally, Australia notes the observation of both the European Union and the United States in their Appellee submissions that a number of issues appealed by the Philippines are repeated both in relation to Article III:2 of GATT 1994 and under Article 11 of the DSU.<sup>32</sup> In Australia’s view, the repetition of arguments gives rise to uncertainty as to whether the Philippines is alleging that in relation to certain claims the panel erred in its interpretation and application of the law, or whether the panel erred in its appreciation of the facts and evidence adduced by the parties to the dispute. Australia therefore submits that the Appellate Body may wish to scrutinise the appropriateness of some aspects of the Philippines’ appeal to distinguish between questions as to the panel’s appreciation of the facts and evidence, and its alleged errors of law, in order to determine how such claims should appropriately be dealt with.

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<sup>29</sup> See Philippines Appellant Submission, paras. 173, and 185.

<sup>30</sup> Appellate Body Report, *Brazil-Tyres*, para. 185; citing Appellate Body Report, *EC-Hormones*, paras. 132 and 133; quoting Appellate Body Report, *US-Carbon Steel*, para. 142 (quoting Appellate Body Report, *EC-Hormones*, para. 135); and Appellate Body Report, *US-Wheat Gluten*, para. 151. See also Appellate Body Report, *EC-Asbestos*, paras. 161-162.

<sup>31</sup> Appellate Body Report, *EC-Asbestos*, paras. 162.

<sup>32</sup> See for example: European Union Appellee Submission, paras. 163, 185, and 191; and United States Appellee Submission para. 99.

### **III. CONCLUSION**

24. Australia considers that this appeal raises systemic issues which have broad implications for the interpretation of Member's obligations under Article III:2 of GATT 1994, as well as for the application of Article 11 of the DSU. In this submission, Australia has sought to draw attention to specific aspects of the appeal which in its view should be taken into account in analysing both Members' and the panel's obligations under these covered Agreements.