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WTO Appellate Body upholds Panel's ruling in *US – Measures Affecting the Production and Sale of Clove Cigarettes*

On 4 April 2012, the WTO Appellate Body issued its final report upholding, albeit for different reasons, the Panel's finding that Section 907(a)(1)(A) of the 2009 *Family Smoking Prevention and Tobacco Control Act* amending the *Federal Food, Drug, and Cosmetic Act* (hereinafter, FFDCA) was in contravention of, *inter alia*, Article 2.1 of the WTO Agreement on Technical Barriers to Trade (hereinafter, TBT Agreement). Before the Panel, Indonesia alleged that Section 907(a)(1)(A) of the FFDCA prohibiting, *inter alia*, the production or sale in the US of cigarettes containing certain constituents or additives, including cloves, but permitting the production and sale of cigarettes containing menthol, discriminated against Indonesian clove cigarettes in favour of '*like'* domestic menthol cigarettes, in a manner which was inconsistent with, *inter alia*, Article 2.1 of the TBT Agreement.

The Panel had concluded that Section 907(a)(1)(A) of the FFDCA violated, *inter alia*, Article 2.1 of the TBT Agreement. The Panel based its determination on whether the products were '*like*' within Article 2.1 of the TBT Agreement in terms of the regulatory objectives pursued by the law. Specifically, the Panel found that clove and menthol-flavoured cigarettes are '*like products*' within Article 2.1 of the TBT Agreement, based in part on factual findings that both cigarette types are flavoured and similarly appealing to youth (for additional background on the Panel decision, see Trade Perspectives, Issue No. 16 of 9 September 2011).

The Appellate Body, while upholding the Panel's finding that clove cigarettes and menthol cigarettes are '*like products*' within Article 2.1 of the TBT Agreement, rejected the Panel's approach in determining '*likeness*', which focused on assessing the objective risks posed by the particular products (*i.e.*, clove cigarettes and menthol cigarettes) in light of the regulatory objective pursued. The Appellate Body instead adopted an interpretative approach based on both the TBT Agreement and Article III:4 of the General Agreement on Tariffs and Trade 1994 (hereinafter, GATT), stressing that '*likeness*' under Article 2.1 of the TBT Agreement is a determination of the '*nature and extent of a competitive relationship*' between the two products at issue. Citing *EC – Measures Affecting Asbestos and Asbestos-Containing Products*, the Appellate Body reasoned that conflicting risks posed by the products in question (*i.e.*, clove and menthol cigarettes) are relevant only in determining the competitiveness of product categories (namely, physical characteristics, end-uses, consumer tastes and habits, and tariff classification), but are not in and of themselves sufficient to establish that competitive products are not alike. Therefore, the regulatory concerns underlying a measure, such as the health risks associated with clove and menthol cigarettes, may only be relevant in determining '*likeness*' to the extent that they have an impact on the competitive relationship between the products.

In examining the '*treatment no less favourable*' element of Article 2.1 of the TBT Agreement, the Appellate Body noted that, as seen in the preamble, the object and purpose of the TBT Agreement is to strike a balance between the recognition of a country's right to regulate and the desire to avoid unnecessary obstacles to international trade. As such, the Appellate Body stated that Article 2.1 of the TBT Agreement should not be interpreted as prohibiting any detrimental impact on competitive opportunities for imports where such detrimental impact on imports '*stems exclusively from legitimate regulatory distinctions*'. The Appellate Body was also mindful to consider previous Appellate Body findings in the context of Article III:4 of the GATT as instructive in assessing the meaning of '*treatment no less favourable*'. Accordingly, a panel should seek to ascertain whether the regulation modifies the conditions of competition in the market of the regulating Member to the detriment of imported products, in comparison to like domestic products. The Appellate Body further contemplated unintentional discrimination in considering the extent to which imported and domestic cigarettes compete. To do so, a panel must carefully scrutinize the particular circumstances of the specific case at issue, including the '*design, architecture, revealing structure, operation, and application of the technical regulation at issue, and, in particular, whether that technical regulation is even-handed'*. After careful scrutiny of Section 907(a)(1)(A) of the FFDCA, the Appellate Body relied on the Panel's findings that flavouring in cigarettes are appealing for young people to mask the harshness of tobacco, thus making them more pleasant to begin smoking with. To the extent that both menthol and clove mask the harshness of tobacco, they have the same product characteristic in light of the stated objective of the US law, which justified the prohibition of clove cigarettes. Based upon the fact that the US failed to provide proper justification for differentiation between menthol and clove cigarettes, Section 907(a)(1)(A) provided less favourable treatment to like products (*i.e.*, clove cigarettes) imported from Indonesia.

Importantly, the Appellate Body Report appears to calm concerns regarding the prohibition of inadvertent discrimination by Article 2.1 of the TBT Agreement. In theory, there is no such risk as long as the detrimental impact on imports from any such prohibition stems exclusively from a legitimate regulatory distinction. Under the Panel's approach, existence of a legitimate regulatory distinction could end the analysis of potential violation at the '*likeness'* stage, while the Appellate Body additionally requires that detrimental effects on imports stems '*exclusively*' from the legitimate regulatory distinction. Consequently, it is important to carefully monitor the interpretation of the Appellate Body's findings in future disputes brought under Article 2.1 of the TBT Agreement. These findings could soon be tested in various areas of regulation, as countries increasingly enact measures in fields such as public health (*e.g.,* alcohol, unhealthy foods), the environment and consumer protection. Any future WTO challenge concerning technical regulations should be carefully monitored to assess how future panels weigh the delicate balance found in the preamble and Article 2.1 of the TBT Agreement, along with previous Appellate Body findings in the context of Article III:4 of the GATT.

Which remedies against Argentina's nationalisation of Repsol's assets?

On 16 April 2012, the Argentinean Government announced its decision to expropriate 51% of Repsol's stakes in Yacimientos Petroliferos Fiscales (hereinafter, YPF). YPF is an oil company whose 57.4% of shares are owned by the Spanish company Repsol. The rest of YPF's shares are partly owned by Argentina's Petersen (25.5%), the Argentinean Government (0.02%) and publicly traded (17%). Argentina's move would leave Repsol with a 6.4% stake in YPF, while the expropriated shares would be distributed among the Argentinean Government and provincial governors.

Argentina's announcement has met widespread criticism, including from the EU, EU Members States (Spain and the UK) and other countries (e.g., the US and Mexico). The EU Commission has expressed deep disappointment with Argentina's possible nationalisation of Spain's assets and, together with Spanish authorities, is considering possible remedies.

Investment relations between Spain and Argentina are regulated by a bilateral investment treaty (hereinafter, BIT or Treaty) concluded in 1991. As it is the case for other investment treaties, the definition of investment in the BIT covers shares and other means of control in the other Party's companies. The BIT provides for specific obligations in case of nationalisation and expropriation of investments. In particular, according to the Treaty, nationalisation and expropriation can only take place for public purposes in compliance with national legislation, and cannot be discriminatory. In any event, the Treaty requires the Party nationalising investments to provide to the investor, or its right-holder, an 'adequate' compensation. Repsol reportedly estimates such compensation to amount to, at least, USD 10 billion. However, Argentina appears to have not yet given indications whether, and to what amount, it will compensate Repsol.

The BIT provides for dispute settlement mechanisms that can be triggered in case of alleged violations. These include a state-to-state arbitration mechanism, permitting Spain to challenge Argentina for the nationalisation of a Spanish company's investments, and an investor-to-state arbitration, which would allow Repsol to lodge a direct complaint against the Argentinean Government. The rules governing this latter mechanism provide that a possible complaint can only be lodged before an international arbitration mechanism provided that, either (i) both parties to the dispute agree to that effect; or (ii) a complaint is first lodged before Argentinean courts and a decision on the merits has not been reached within 18 months or where the parties are displeased with such decision. In any event, to allow parties to the dispute to reach an amicable solution, recourse to Argentinean courts cannot be sought before six months from the date in which the complaint is formally raised by Repsol.

The remedies included in the BIT are available to, respectively, the Spanish Government or Repsol. However, a certain degree of uncertainty may derive from the new allocation of competences established by the Lisbon Treaty. The Lisbon Treaty has conferred exclusive competences to EU institutions in deciding on EU Member States' international investment policies, and it implies that, as it is the case for competences in the field of trade, it would be the EU Commission's task to launch a dispute relating to investment agreements with third countries. However, a mechanism to establish transitional arrangements for the BITs negotiated and individually concluded by EU Member States with third countries before the entry into force of the Lisbon Treaty has not yet been agreed upon (see Trade Perspectives, Issue No. 14 of 16 July 2010). This may have implications as to the competence to currently decide on, and handle, investment disputes arising in the context of such agreements.

The WTO dispute settlement system may also play a role. A WTO complaint could arguably be based on a possible violation of Argentina's commitments under the General Agreement on Trade in Services (hereinafter, the GATS), which regulates, to some extent, foreign direct investment in services trade. In particular, under its Schedule of Specific Commitments, Argentina committed to grant market access and national treatment to foreign operators established in its territory to deliver 'services incidental to mining'. The UN Central Product Classification, on which the WTO services classification is based, defines such services as '*services rendered on a fee or contract basis at oil and gas fields, e.g., drilling services, derrick building, repair and dismantling services, oil and gas well casing cementing services*'. A legal basis for challenging the nationalisation could also arguably be found within Argentina's commitments in the distribution sector, inasmuch as they may cover wholesale and retail trade of fuels. Therefore, the possibility of invoking WTO dispute settlement will depend on whether or not the services affected by expropriation may fall under the definition and scope of 'services incidental to mining' and/or distribution services.

In the context of a WTO dispute, the EU could argue that Argentina's nationalisation constitutes a measure affecting Repsol's ability to supply such services in Argentina's territory, and which results in less favourable treatment granted to Spain's services supplier, in violation of Articles XVI and XVII of the GATS and Argentina's specific commitments. In particular, a violation of Article XVI of the GATS can be argued inasmuch as Argentina's nationalisation may result in either a limitation of the number of services suppliers (letter (a) of Article XVI), a limitation on the total value of services transactions or assets (letter (b) of Article XVI), or a limitation on the participation of foreign capital (letter (f) of Article XVI). In addition, a violation of Article XVII of the GATS could be argued inasmuch as Argentina's nationalisation results in discrimination of the Spanish supplier *vis-à-vis* domestic like services suppliers. Argentina's nationalisation may also affect the country's obligations under Article VI of the GATS, which require, *inter alia*, Argentina to ensure that all measures of general application affecting trade in services are administered in a reasonable, objective and impartial manner.

Both WTO and BIT remedies would provide the parties to the dispute with a binding decision. In terms of timing, it would take between six and eleven months to establish an arbitral tribunal within the BIT state-to-state arbitration mechanism. The investor-to-state mechanism would require Repsol to first try to reach a mutually agreed solution (within six months) and to resort, at least for a period of eighteen months, to Argentina's domestic courts, before being able to invoke international arbitration. A decision of a WTO panel takes, on average, a little less than fourteen months from the establishment of a panel, following a period of mandatory consultations. Another factor to be considered is the result that can be obtained through the awards provided under the two remedies. Arbitration awards under the BIT may entitle Repsol to obtain financial compensation, although they would not protect it against a possible failure of Argentina's Government to pay (see, in this regard, Trade Perspectives, Issue No. 7 of 5 April 2012). A WTO dispute settlement decision would not lead to pecuniary compensation in favour of Repsol. It may find that Argentina's nationalisation violates WTO rules and would require Argentina to bring its legislation into conformity with the WTO. However, it is not clear what the potential consequence of such finding and recommendation would be, in particular, whether it could possibly imply a restoration of the '*status quo ante*'.

The EU Commission and EU Member States are reportedly going to discuss available options against Argentina's move next week. A decision on possible remedies, which are not restricted to dispute settlement under either the BIT or the WTO but also include diplomatic avenues, will ultimately depend on a number of factors, including, notably, on whether Argentina is going to compensate Repsol for the nationalisation of its stakes and, if so, in what amount.

'Sin taxes' **on food and beverages in the EU Member States – A Model for the EU?**

There is an ongoing debate in Europe (but also elsewhere, such as in Australia) on whether taxing fattening foods and/or sugary beverages, with the aim of decreasing consumption of foods linked to obesity and other health-related risks, should be established by all EU Member States and at EU level. The term *'fat-tax'* is predominately used in this context, although one can also refer to a *'sin tax'* on food and beverages. *'Sin taxes'* amount to excise or '*per unit*' taxes that are mainly designed to reduce specific behaviours thought to be harmful to society. They are levied on certain goods, which are generally socially proscribed (or whose abuse is), such as alcohol, tobacco, sweets, soft drinks, fatty foods, and coffee, and services like gambling. A number of EU Member States have adopted taxes on fatty foods (in the case of Denmark and Hungary) or carbonated drinks (in the case of France) (see Trade Perspectives, Issue No. 18 of 7 October 2011 and Issue No. 1 of 13 January 2012). In the context of the current economic crisis, EU Member States (such as France with the *'Soda tax'*) may use such fiscal measures not only to fight obesity and bad health in general, but also to generate higher governmental revenues, as often done in the past with the taxation of alcohol and tobacco.

The EU Commission has reportedly declared that it currently has no intention of pursuing harmonisation of *'fat taxes',* but there are indications that measures could be introduced should current EU Member State taxes prove successful in changing consumer habits (*i.e.*, if there is evidence that such excise taxes affect health and not only primarily raise revenues) and if there were to a *'critical mass'* of EU Member States supporting these measures. The EU Commission is said to be *'looking at the legal perspective'* of *'fat taxes'*.

What are the legal implications of adopting *'fat taxes'* in the EU and under international trade law? Firstly, EU Member State measures have to comply with EU internal market rules. Non-harmonised internal taxes of EU Member States must comply with the Treaty on the Functioning of the European Union (hereinafter, TFEU), in particular with Article 110 thereof, which prohibits internal discriminatory taxation, direct or indirect, on products from other Member States, in excess of that imposed on *'similar domestic products'*. Article 110 TFEU also prevents Member States from imposing any internal taxation on products from other Member States *'of such a nature so as to afford indirect protection to other products'*. In other words, if goods are similar (Article 110(1)), or if they are dissimilar, but in competition with each other (Article 110(2)), this provision prohibits EU Member States from discriminating against imported products by means of imposing higher taxes on them than what is being imposed on goods of national origin. Member States are, therefore, not precluded from introducing *'fat taxes'* on certain foods, but, in so doing, they must ensure an identical tax on similar foodstuffs and foodstuffs that are in competition, so as to avoid any claim of discrimination or protectionism. Therefore, national *'fat tax'* schemes need to be examined in their practical application and effects in order to determine whether they may create a higher tax burden on products from another EU Member State.

Secondly, EU Member States' *'fat taxes'* and, if introduced, any harmonised EU *'fat tax'*, must also comply with international trade law obligations (from a '*most-favourite-nation treatment*' (MFN) and 'national treatment (NT)' perspective). The tax schemes introduced so far by certain EU Member States appear to be origin-neutral (*i.e.*, the same tax burdens appear to apply to domestic and imported goods). However, it must be closely examined whether there is, in practice, a higher tax burden on the imported products subject to these taxes. In fact, possible (*de facto*) discrimination against third country products could become an issue with the implementation of such taxes. Article III:2 of the GATT prevents WTO Members from applying internal taxes to imported products in excess of those applied to domestic products so as to afford protection to domestic production. As stated above, the taxes introduced so far appear to be origin-neutral, but instances of discrimination relevant to WTO obligations may nevertheless occur where the taxes *de facto* favour domestic production of like or *'directly competitive or substitutable'* products, which must be examined on a case-by-case basis.

In order to justify this new trend of taxing certain foods for purposes of health protection, regulators should collect credible science that additional taxes on food products encourage consumers to have a more balanced diet and lead a healthy lifestyle. The food industry has been calling for such a (scientific) link between taxes and health, as it believes there is no such justification (see Trade Perspectives, Issue No. 1 of 13 January 2012). Before considering adopting a harmonised EU *'sin tax'* on food and beverages, the EU should therefore carry out a thorough and critical legal review of its envisaged measures to ensure that they are in compliance with its obligations under the GATT, and in particular that they do not give cause to trade discrimination *vis-à-vis* products imported from third countries.

India may challenge US measures raising visa fees

It appears that India may file a request for WTO consultations with the US concerning the latter's measures to increase visa fees. These measures were imposed by the US already in August 2010. India considers that they may directly affect Indian companies operating in the technology sector, which employ thousands of Indian workers in their US offices, such as Wipro, Tata, Infosys and Satyam.

Indeed, in August 2010 the US Congress passed the Public Law 111-230, aimed at strengthening security controls at the US south-western border. In order to improve the security system, and hence to cover the costs of security personnel, equipment, infrastructures and other resources in that area, the fees for H-1B and L-1 visa petition were raised by USD 2,000 and USD 2,250 each, for companies meeting certain requirements. These kinds of visa constitute temporary working permits for skilled workers within the US. As a matter of fact, the increase in fees only affects companies that employ more than 50 workers in the US, at least half of which must be H-1B or L-1 visa holders. The fee is to be cleared by the company when filing a petition for a visa on behalf of a foreign worker, or in the event of filing a petition to allow a H-1B or L-1 worker to change employers. The relevant legislation initially envisaged the fees hike to apply until 30 September 2014, but subsequent legislation has extended their application until 2015.

The measure is intended to respond to budgetary needs (apparently connected to costs relating to improved security at the US-Mexico border). Nonetheless, during floor deliberations of the Bill, it was stated that the visa fee hike was a necessary measure to restrict availability of the two aforementioned kinds of visa. Allegedly, those are often the subject of abuse by companies that outsource technology jobs to lower wage, temporary immigrant workers from different countries.

These measures are relevant to the provisions of the GATS, which provides for a number of general obligations and specific commitments affecting trade in services supplied through one of the four established modes of supply. In the case at issue, Mode 3 (regarding commercial presence) and Mode 4 (concerning presence of natural persons), are of relevance. The GATS includes also an Annex on *Movement of Natural Persons Supplying Services under the Agreement*. According to paragraph 4 thereof, WTO Members may enact measures to regulate the flow of natural persons in their territories, *provided that such measures are not applied in such a manner as to nullify or impair the benefits accruing to any Member under the terms of a specific commitment*. Inasmuch as the requirements triggering the visa fees increases (*i.e.*, companies with more than 50 employees in the US, at least half of which holding a H-1B or L-1 visa) appear to particularly affect subsidiaries and branches of Indian companies, India argued that the US measures impair the benefits of temporary access to the US enjoyed by Indian skilled workers under the US Mode 4 commitments (see in this regard, Trade Perspectives, Issue No. 1 of 14 January 2011). Moreover, GATS Article VI(1) states that in respect of domestic regulation, '*in sectors where specific commitments are undertaken, each Member shall ensure that all measures of general application affecting trade in services are administered in a reasonable, objective and impartial manner*'. A WTO panel may find that the US contentious measure does not meet the requirements of reasonable, objective and impartial administration. In January 2011, a report by the National Foundation for American Policy already found the measure as '*likely to violate the US commitments under the GATS*'.

India is reportedly going to file its request for consultations within the coming weeks. Should that occur, this will not be the only ongoing WTO dispute between the two countries. In March 2012, the US filed a request for consultations concerning the Indian decision to ban various agricultural products of US origin. Only a few weeks later, India filed a request for consultations regarding the US imposition of countervailing duties on certain hot rolled carbon steel flat products from India. This controversy may have important implications for businesses active in the US, as well as for prospective investors, which may be affected by the increase in visa fees. Businesses using H-1B, L-1, or other visas to enable their employees to provide services in the US or another WTO Member should monitor visa fee increases and follow these developments closely. Such increases may result in a violation of WTO Members' commitments under the GATS and constitute valid grounds to seek a legal challenge under WTO rules.

Recently Adopted EU Legislation

Trade Remedies

- *Council Implementing Regulation (EU) No. 325/2012 of 12 April 2012 imposing a definitive anti-dumping duty and collecting definitively the provisional duty imposed on imports of oxalic acid originating in India and the People's Republic of China*

- *Council Implementing Regulation (EU) No. 332/2012 of 13 April 2012 amending Regulation (EC) No. 130/2006 imposing a definitive anti-dumping duty and collecting definitively the provisional duty imposed on imports of tartaric acid originating in the People's Republic of China, and excluding company Hangzhou Bioking Biochemical Engineering Co., Ltd from the definitive measures*

Customs Law

- *Commission Delegated Regulation (EU) No 312/2012 of 9 January 2012 amending Council Regulation (EU) No 973/2010 temporarily suspending autonomous Common Customs Tariff duties on imports of certain industrial products into the autonomous regions of the Azores and Madeira*

- *Commission Implementing Decision of 4 April 2012 amending Decisions 2008/603/EC, 2008/691/EC and 2008/751/EC as regards the temporary derogations from the rules of origin laid down in Annex II to Council Regulation (EC) No. 1528/2007 to take account of the special situation of Mauritius, Seychelles and Madagascar with regard to preserved tuna and tuna loins (notified under document C(2012) 2321)*

- *Commission Implementing Regulation (EU) No. 308/2012 of 11 April 2012 amending the rate of additional duty for products listed in Annex I to Council Regulation (EC) No. 673/2005 establishing additional customs duties on imports of certain products originating in the United States of America*

Food and Agricultural Law

- *Council Decision of 26 March 2012 on the conclusion of the International Cocoa Agreement 2010*

- *Commission Implementing Regulation (EU) No. 307/2012 of 11 April 2012 establishing implementing rules for the application of Article 8 of Regulation*

(EC) No. 1925/2006 of the European Parliament and of the Council on the addition of vitamins and minerals and of certain other substances to foods

- *Commission Implementing Decision of 10 April 2012 allowing Member States to extend provisional authorisations granted for the new active substances amisulbrom, chlorantraniliprole, meptyldinocap, pinoxaden, silver thiosulphate and tembotrione (notified under document C(2012) 2259)*

- *Commission Implementing Regulation (EU) No. 313/2012 of 12 April 2012 amending Annexes IV and VIII to Council Regulation (EC) No. 73/2009 establishing common rules for direct support schemes for farmers under the common agricultural policy*

- *Commission Implementing Regulation (EU) No. 314/2012 of 12 April 2012 amending Commission Regulations (EC) No. 555/2008 and (EC) No. 436/2009 as regards the documents accompanying consignments of wine products and wine sector registers to be kept*

- *Commission Implementing Regulation (EU) No. 319/2012 of 13 April 2012 adding to the 2012 fishing quotas certain quantities withheld in the year 2011 pursuant to Article 4(2) of Council Regulation (EC) No. 847/96*

- *Commission Regulation (EU) No. 322/2012 of 16 April 2012 amending Annexes II and III to Regulation (EC) No. 396/2005 of the European Parliament and of the Council as regards maximum residue levels for clopyralid, dimethomorph, fenpyrazamine, folpet and pendimethalin in or on certain products*

- *Commission Implementing Regulation (EU) No. 331/2012 of 18 April 2012 on the issue of licences for the import of garlic in the subperiod from 1 June 2012 to 31 August 2012*

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