



Bench Memorandum
GNLU International Moot Court Competition
(GIMC), 2010

Dispute on the differences arising between

Independent Republic of Azania

and

The Republic of Enroda

Concerning the Interpretation of the Razvana Free Trade Agreement

I. INTRODUCTION

- [1] The inspiration for the *Compromis* can be attributed to two distinct developments in the field of international trade. A power to regulate trade in many ways has become a powerful tool at the hand of nation states, to enforce their rules and ideology pertaining to the appropriate way of addressing climate change. For better or worse, there exists what could be arguably considered to be international standards today, in the shape of the United Nations Framework Convention on Climate Change, 1995 (UNFCCC) and the subsequent Kyoto Protocol, 1998. While negotiations are still underway to adopt a more aggressive approach in addressing climate change concerns, the UNFCCC represents the focal point for any legal dispute arising with respect to climate change.
- [2] More, specifically the motivation to reflect the current tussle between developed nations, and developing countries, especially the ones in a comparatively advanced stage of development arose out of media reports, which reported attempts by the European Union to place a carbon tax on imports from countries in an “*advanced stage of development*”. A copy of the report in the Economic Times, dated June 23, 2008 is attached as Annexure A to the Bench Memorandum.
- [3] With respect to the second aspect of the *Compromis*, the steps taken by the European Commission to classify a number of export incentives schemes of the Government of India as export subsidies gives rise to a need to initiate a debate on the legality of such measures.
- [4] Export incentive schemes of the Government of India, such as the Export Oriented Units (EOU) and Special Economic Zone schemes are directed at ensuring that inputs which are utilized in the manufacture of exported goods are exempted from taxes. The objective of the scheme is WTO inconsistent and explicitly recognized by Footnote 1 to Annexure 1(h) of the WTO Agreement on Subsidies and Countervailing Measures. In fact, most countries including the European Union maintain such measures through measures such as the inward remittance schemes of the Union. In dispute, is the method through which these schemes are administered by the Government of India.
- [5] While Export Oriented Units and Special Economic Zones are similar in many ways, significant differences exist. Unlike, an EOU, the SEZ is regulated by a dedicated

statute and administrative rules, i.e. the SEZ Act, 2000 and the SEZ Rules, 2006. While, the Export Oriented Unit has invited the wrath of the European Commission, the Commission has not had an occasion to examine the consistency of the SEZ scheme with the European Community Basic Regulation on Subsidies, which is basically a reflection of the WTO Subsidies Agreement. The Free Trade Zone of Enroda is similar to the Special Economic Zone of India and so is the applicable law. Of course, in the present case, the tables are turned to the extent, that the scheme is administered by a developed country and being investigated by a developing one.

- [6] To put the issue in perspective. The participants are expected to primarily argue as to whether the FTZ scheme is an export subsidy under the Razvana Agreement on Subsidies and Countervailing Measures, and whether in the presence of an international mechanism to regulate climate change, unilateral actions in violation of treaty obligations are permitted. More, specifically, whether such actions are justifiable under the General Exceptions of the Razvana Agreement on Trade in Goods, *pari materia* with the provisions of the WTO GATT. In the present case, a participant shall have to place significant reliance on his skills of interpretation rather than depend on established case laws and precedents. A participant should be therefore suitably rewarded for a novel interpretation of the applicable law.

II. Legal Issues

- [7] The legal claims of Azania and Enroda are specified in the *Compromis* and the panel shall be expected to adjudicate on the following claims raised by the Parties.

Azania

- a. The duty exemptions on import of raw materials for the steel industry is a subsidy prohibited under the Razvana Agreement on Subsidies and the imposition of a countervailing duties is consistent with the provisions of the Agreement.

- b. The imposition of a border tax on imports is in violation of the market access commitments undertaken by Enroda and is not justified by the General Exceptions to the Razvana Agreement on Trade in Goods.

Enroda

- a. The duty exemptions on import of raw materials for the steel industry is not subsidy prohibited under the Razvana Agreement on Subsidies and the imposition of countervailing duties is inconsistent with the provisions of the Agreement.
 - b. The imposition of a border tax is justified under the General Exceptions to the Razvana Agreement on Trade in Goods.
- [8] While the claims are specifically identified, the participants are permitted to interpret the provisions of the applicable treaties in their context which includes multilateral treaties to which the Appellant and the Respondent are a party, customary international law and applicable decisions of the International Court of Justice, International Tribunals and the WTO Panel and Appellate Body Reports. The rules of interpretation are laid out in Article 27 of the Agreement on the Settlement of Disputes arising out of the Razvana Free Trade Agreement.

ARTICLE 27: RULES OF INTERPRETATION

1. The RFTA shall be interpreted in accordance with the rules of treaty interpretation under public international law.

2. The decision of the WTO Panel & Appellate Body, other international tribunals and the "general principles of law recognized by civilized nations" shall serve as a subsidiary source of law in the interpretation of the provisions of the RFTA.

- [9] The position of the WTO Appellate Body in *US - Gasoline* that WTO law cannot be interpreted in clinical isolation from public international law is quite applicable to the present case.¹

¹ *United States - Standards for Reformulated and Conventional Gasoline*, Report of the Appellate Body, WT/DS2/AB/R, 1996, p. 17: Hereinafter: US-Gasoline

A. ISSUES IN DETAIL

1. *Whether the decision of the Azania Commission to impose countervailing duties on the import of steel from Enroda benefitting from the Free Trade Zone scheme is inconsistent with the provisions of the Razvana Agreement on Subsidies and Countervailing Measures?*

- [10] The bench is expected to focus its examination on whether the Free Trade Zones Act represents an export subsidy within the meaning of Article 3.1 (a) of the Razvana Free Trade Agreement². It is important to appreciate that the investigation has been initiated on the basis that the Free Trade Zone is an export subsidy. Therefore the subsidy has been “*deemed to be specific*” within the meaning of Article 2.4 of the Subsidies Agreement. There is no evidence on record to suggest that the Azanian Commission has independently examined whether the Free Trade Zone can be considered to be a specific subsidy or not. Therefore the determination of whether Free Trade Zone constitutes an export subsidy within the meaning of Article 3.1 (a) of the RASCM has a material bearing on the determination of whether the decision of the Azanian Commission is consistent with the provisions of RASCM or not.
- [11] For the purpose of the WTO Agreement on Subsidies and Countervailing Measures a subsidy is deemed to exist when the following conditions are satisfied

Article 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:

(ii) Government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits)

² Note: The provisions of the Razvana Agreement on Subsidies and Countervailing Measures are identical to the provisions of the WTO Agreement on Subsidies and Countervailing Measures. In the bench memorandum WTO SCM and RASCM are referred to interchangeably.

Footnote to Article 1.1 (a) (1) (ii): *In accordance with the provisions of Article XVI of GATT 1994 (Note to Article XVI) and the provisions of Annexes I through III of this Agreement, the exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption, or the remission of such duties or taxes in amounts not in excess of those which have accrued, shall not be deemed to be a subsidy.*

(b) A benefit is thereby conferred

[12] Annexure I (h) of the WTO SCM on the other hand identifies “*the exemption, remission or deferral of prior - stage cumulative indirect taxes on goods or services used in the production of exported products in excess of the exemption, remission or deferral of like prior - stage cumulative indirect taxes on goods or services used in the production of like products when sold for domestic consumption)*” as an export subsidy. The complete text of Annexure I (h) reads as follows:

“The exemption, remission or deferral of prior - stage cumulative indirect taxes on goods or services used in the production of exported products in excess of the exemption, remission or deferral of like prior - stage cumulative indirect taxes on goods or services used in the production of like products when sold for domestic consumption; provided, however, that prior - stage cumulative indirect taxes may be exempted, remitted or deferred on exported products even when not exempted, remitted or deferred on like products when sold for domestic consumption, if the prior - stage cumulative indirect taxes are levied on inputs that are consumed in the production of the exported product (making normal allowance for waste). This item shall be interpreted in accordance with the guidelines on consumption of inputs in the production process contained in Annex II.”

[13] The Free Trade Zone is defined by Section 2 (a) of the Enroda Free Trade Zones Act as “*an enclave of units operating in a well defined area within the geographical boundary of a country where certain economic activities are promoted by a set of policy*

measures that are not generally applicable to the rest of the country". Goods can be imported duty free into the Free Trade Zone without the payment of any duty of customs, which includes basic customs duty as well as any other applicable duty such as anti-dumping and safeguard duty.

- [14] The exemption of the above mentioned duty is subject to certain terms and conditions laid out in Section 15 and Section 16 of the FTZ Act.

Section 15: *(a) any goods removed from a Free Trade Zone to the Domestic Tariff Area shall be chargeable to duties of customs including anti-dumping, countervailing and safeguard duties under the relevant laws of Enroda, where applicable, as leviable on such goods when imported; and (b) the rate of duty and tariff valuation, if any, applicable to goods removed from a Free Trade Zone shall be at the rate and tariff valuation in force as on the date of such removal, and where such date is not ascertainable, on the date of payment of duty.*

Section 16: *The grant of exemption on import duties on imports of raw material and inputs utilized in the manufacturing process by a manufacturing unit in the Free Trade Zone shall be subject to the following conditions*

(a) The Unit shall execute a Bond-cum-Legal Undertaking in Form H, with regard to its obligations regarding proper utilization and accountal of goods, including capital goods, spares, raw materials, components and consumables including fuels, imported or procured duty free and regarding achievement of positive net foreign exchange earnings;

(b) Every Unit and Developer shall maintain proper accounts, financial year wise, and such accounts which should clearly indicate in value terms the goods imported or procured from the domestic market of Enroda, consumption or utilization of goods, production of goods, including by-products, waste or scrap or remnants, disposal of goods manufactured or produced, by way of exports, sales or supplies in the domestic tariff area or transfer to Free Trade Zone.

(c) In the event of a theft of duty exempted raw materials and inputs on its way to the free trade zones or under any other circumstances which may so arise, the manufacturing unit shall within a period of one month of such theft pay to the Government of Enroda through the Free Trade Zones officers so designated a sum commiserate to the duty exemption availed by it. Where manufacturing unit does not utilize the goods or services on which exemptions, drawbacks, cess and concessions have been availed for the authorized operations or unable to duly account for the same, the entrepreneur or the Developer, as the case may be, shall refund an amount equal to the benefits of exemptions, drawback, cess and concessions availed by it.

(d) The unit should be able to account for the entire quantity of each category of homogenous goods imported / procured duty free, by way of exports, sales/supplies in DTA or transfer to other units in the FTZ and balance in stock. However, at no point of time the units shall be required to

co-relate every import consignment with its exports, transfer to other units in the FTZ, sales in the DTA and balance in stock.

[15] The provisions are expected to be interpreted against the touchstone of the abovementioned applicable provisions of the WTO SCM/RASCM. Annexure II and III of the WTO SCM are annexed as Annexure B to the Bench Memorandum. The relevant question before the panel is whether the Free Trade Zone is a permissible scheme within the meaning of Footnote to Article 1.1 (a) (1) (ii) or whether it is an export subsidy within the meaning of Article 3.1 (a) of the RASCM or/and Annexure I(h) of the RASCM.

Arguments on behalf of the competing parties

Azania

- a. Azania is expected to argue that Enroda cannot benefit from the provisions of Footnote to Article 1.1 (a) (1) (ii) as the exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption, or the remission of such duties or taxes in amounts is allowed only to the extent the remission is not in ***excess of the duty which have accrued.***
- b. The FTZ scheme results in the Government of Azania foregoing revenue otherwise due within the meaning of Article 1.1(a) (1) (ii) of the RASCM. The foregoing of revenue provides a benefit to the beneficiaries of the FTZ scheme within the meaning of Article 1.1(b) of the RASCM.
- c. Benefits of the FTZ are applicable to exports, as the duty exemption is on the inputs utilized in the manufacture of end goods bound for export markets and is therefore a subsidy contingent on export performance.
- d. Azania can further argue that the FTZ scheme is an export subsidy within the meaning of Annexure I (h) of the RASCM as it exempts inputs from duties from otherwise due without being able to guarantee that the inputs on which duty is exempted is used in the production of the exported product.

- e. Duty exemption on inputs used in the manufacture of exported goods is subjected to the strict guidelines of Annexure II of the RASCM. Annexure II (II) of the RASCM lays down the method in which the investigating authority should proceed. It states that *“where it is alleged that an indirect tax rebate scheme, or a drawback scheme, conveys a subsidy by reason of over - rebate or excess drawback of indirect taxes or import charges on inputs consumed in the production of the exported product, the investigating authorities should first determine whether the government of the exporting Member has in place and applies a system or procedure to confirm which inputs are consumed in the production of the exported product and in what amounts.”* . It furthermore adds that *“Where such a system or procedure is determined to be applied, the investigating authorities should then examine the system or procedure to see whether it is reasonable, effective for the purpose intended, and based on generally accepted commercial practices in the country of export.”* Azania should argue that Annexure II (II) (1) lays down two requirements. First, the investigating authority has to determine whether there exporting member has in place and applies a system or procedure to confirm which inputs are consumed in the production of exported product and in what amount. Only **“where such a system or procedure is determined to be applied”** does the second part of the provision, i.e. the requirement that *“investigating authorities examine the system or procedure to see whether the system in question is reasonable, effective for the purpose intended and based on generally accepted commercial practices in the country of export”* become applicable.
- f. Participants should take a cue from Section 16(d) of the Enroda Free Trade Zones Act which states in categorical terms that the units shall not, at any point in time, be required to co-relate every import consignment with its exports, transfer to other units in the FTZ, sales in the DTA and balance in stock. Furthermore, the Enroda Trade Minister himself acknowledges that there exists no mechanism for the absolute correlation of inputs with end products.³ This should be argued to mean that Enroda does not have in place or apply a system or procedures to confirm which inputs are consumed in the production of the exported product and in what

³ *Compromis*, ¶23

amounts. Since the first requirement of the provision is not satisfied there is no question of examining the second prong of Annexure II (II) (1) on the part of the Azanian Commission.

- g. In any event, even the requirements of the second prong are not satisfied, as the scheme is expected to be effective for the purpose intended. In this case the purpose intended is to ensure that duty-exempt inputs are used in the production of exported products. In the absence of a mechanism which can correlate the inputs with the end products, the FTZ scheme can be hardly considered effective in fulfilling the purpose intended.
- h. The failure to put in place a system or procedure to determine which inputs are consumed in the production of the exported product and in what amounts, means the guidelines laid out in Annexure II of the RASCM are not being adhered to. Therefore the FTZ scheme is an export subsidy within the meaning of Annexure I (h) of the RASCM and also within the meaning of Article 3.1 (a) of the Agreement.

[16] Therefore the determination of the Azanian Commission that the Free Trade Zone was an export subsidy was consistent with the provisions of the RASCM. When such subsidized imports caused injury the imposition of countervailing duties was justified.

Enroda

- a. Enroda is expected to argue that the duty exemption on inputs such as iron ore used in the manufacture of steel is explicitly permitted under the RASCM vide Footnote 1 to Article 1.1 (a) (1) (ii). The Free Trade Zone is not an export subsidy within the meaning of Annexure II (h) of the Razvana Subsidies Agreement and is administered in complete conformity with Annexure II of the Agreement. Furthermore, the Free Trade Zone does not constitute an export subsidy within the meaning of Article 3.1 (a) of the RASCM.
- b. Annexure I (h) states that the provision is to be interpreted in accordance with the provisions of Annexure II of the Subsidies Agreement. A successful defence of the Free Trade Zone scheme shall depend on whether Enroda can establish that the provisions of Annexure II are not being violated by it.

- c. Annexure II (II) (1) requires that the investigating authorities should first determine whether the government of the exporting Member has in place and applies a system or procedure to confirm which inputs are consumed in the production of the exported product and in what amounts. Enroda can argue that the requirement under the provision is quite straight forward. Under the first prong of the provision, the investigating agency is only expected to determine whether a system or procedure within the meaning of Annexure II (II) (1) exists or not. A detailed analysis of the duty exemption scheme can only be carried out under the second prong to determine the effectiveness of the scheme in question wherein it is stated *“Where such a system or procedure is determined to be applied, the investigating authorities should then examine the system or procedure to see whether it is reasonable, effective for the purpose intended, and based on generally accepted commercial practices in the country of export”*.
- d. Firstly, Enroda should argue that Section 16 (a) – (d) puts in place a system or procedure to ensure that goods on which duty is exempted is used in the manufacture of the exported product. Azania cannot summarily come to a conclusion that the examination under the second prong is not required as the Free Trade Zone does not put in place a system or procedure to correlate duty exempted on inputs with the finished goods exported. Once it is shown that a system or procedure is in place, or being applied the investigating authorities have to examine the reasonableness and effectiveness of the scheme.
- e. Participants are expected to take a hint from the Press Statement of the Enroda Trade Minister that *“the Free Trade Zones Act ensures that the importers respect the commitment for exports not only because they are required to do so, but as they are left by the Act with no other choice”*. It can be argued that once a manufacturer imports duty free inputs into the Free Trade Zone, the following options are available:
- The manufacturer could use it for goods destined for exports as it is supposed to do.
 - He could sell it in the DTA either as part of the final product or directly.

- Sell it within the FTZ.
- Keep it idle or alternatively
- It could be stolen and in such way defeat the purpose of the exemption.

The Free Trade Zone Act, Section 15 and Section 16 (a) – (d) completely addresses all these concerns.

- In the event of sale or removal of goods from the FTZ to the DTA, Section 15 (a) of the FTZ Act provides that complete customs duty and additional duty as applicable on the end product shall have to be paid by the manufacturer based in the Free Trade Zone. Since duty on the finished product is applicable on sales to the DTA the benefits accruing as a result of exemption on inputs is taken away. It could be argued that since the duties on the end product are usually higher than that applicable on inputs, the benefits of duty free inputs are much more than taken away.
- A sale within a FTZ is illogical and impractical as all units within the FTZ are entitled to same type of benefits.
- When the inputs are stolen or kept idle, Section 16 (c) requires that a sum equivalent to the duty exemption availed on such inputs be paid to the Government of Enroda. This removes the possibility of any excess remission.

In addition to the above, Section 16 (a) and (b) require the proper maintenance of accounts on goods imported or procured from the Domestic Tariff Area as well as their consumption and utilization.

- f. The second prong of Annexure II (II) (1) is satisfied because the FTZ scheme is reasonable and in light of the above, completely effective for the purpose intended, i.e. ensuring that inputs exempt from duty are used in the manufacture of finished goods bound for exports. Furthermore, it is based on the generally accepted commercial practices of Enroda.
- g. Structure of the duty rebate scheme is a sovereign decision of the Government of Enroda. Enroda is free to structure its scheme as it deems fit.

[17] The investigation of the Azanian Commission centres on the premise that the FTZ is an export subsidy within the meaning of Article 3.1 (a) of the Razvana Subsidies Agreement. Article 1.2 of the Subsidies Agreement provides that a “*subsidy as defined in paragraph 1 shall be subject to the provisions of Part II or shall be subject to the provisions of Part III or V only if such a subsidy is specific in accordance with the provisions of Article 2.*” Part V lays down the procedure and applicable law pertaining to countervailing duty investigations and therefore is attracted only when it can be established that a subsidy is specific. Article 2.3 of the Subsidies Agreement further specifies that any subsidy within the meaning of Article 3 is deemed to be specific. Since it has been established that the FTZ is not an export subsidy within the meaning of Article 3.1(a) of the Subsidies Agreement and there is no alternative examination by the Azanian Commission pertaining to the specificity of the FTZ scheme, the entire investigation of the Azanian Commission is inconsistent with the provisions of the RASCM.

B. Whether the imposition of a border tax on imports is in violation of the market access commitments undertaken by Enroda and could be justified by the General Exceptions to the Razvana Agreement on Trade in Goods?

[18] The United Nations Framework Convention on Climate Change, 1995 came into existence as a result of multilateral efforts to address concerns arising out of the increased level of greenhouse gases in the atmosphere as a result of human activities. UNFCCC adopts the principle of common but differentiated responsibility as a guiding factor in determination of the responsibility of Member States in addressing the concern. In fact, the preamble of the UNFCCC acknowledges that “*largest share of historical and current global emissions of greenhouse gases has originated in developed countries, that per capita emissions in developing countries are still relatively low and that the share of global emissions originating in developing countries will grow to meet their social and development needs*”. In short, the Convention adopts a balancing approach, balancing the development needs of developing countries with the requirement to take steps to address global greenhouse

gas emissions. Article 3.5 of the Convention requires that *“measures taken to combat climate change, including unilateral ones, should not constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade”*.

- [19] The commitments undertaken by parties to the UNFCCC are encapsulated in Article 4. The commitments under Article 4 can be broadly divided into commitments undertaken by all parties [Article 4.1 (a) – (j)] and commitments applicable to developed parties and others parties included in Annexure I of the treaty [Article 4.2 (a) – (d)]. It is Article 4.2 (a) for instance which requires that Annexure I parties of the Convention *“adopt national policies and take corresponding measures on the mitigation of climate change, by limiting its anthropogenic emissions of greenhouse gases and protecting and enhancing its greenhouse gas sinks and reservoirs”*. The provision goes on to state that *“these policies and measures will demonstrate that developed countries are taking the lead in modifying longer-term trends in anthropogenic emissions consistent with the objective of the Convention”*.
- [20] The facts on record confirm that Azania is a non Annexure I party to the Convention and a developing nation. The subsequent Kyoto Protocol to the UNFCCC provides for specific commitments applicable to Annexure I parties of the Framework Convention. Enroda through the Carbon Tax Regulation Act (CTRA) authorizes the imposition of a border tax equivalent to the level of tax that would be charged to the domestic industry of the like goods. This measure is restricted to countries included in Annexure A of the CTRA. Annexure A includes developing countries in an advanced stage of development. Azania is considered to be a developing country in an advanced stage of development by Enroda and included in Annexure A.
- [21] The court is expected to determine, whether the decision of Enroda to subject imports from Azania to a border tax is justified in light of the fact that the UNFCCC or the Kyoto Protocol, do not impose any direct mitigation or reduction commitments on Azania. This question has to be addressed at two levels. Firstly, the judges are requested to take note that the *Compromis* quite clearly states that application of the border tax shall result in the application of a tax at the border which is above the bound rate commitment undertaken by Enroda. Therefore there cannot be any argument that the tax applied at the border is within the bound rate commitments. The first point of analysis is whether the action of Enroda is justified by Article 3 (2) (a)

which states that Member states are free to impose on imports, a “charge equivalent to an internal tax imposed consistently with the provisions of paragraph 2 of Article 4 of the RFTA 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;”.

Secondly, if the measures are in violation of the bound rate commitments undertaken by Enroda, recourse must be made to the General Exceptions under the Razvana Agreement on Goods in particular, Article XX(b) and (g) thereof.

[22] The Appellate Body Report in *Shrimp Turtle [Recourse to Article 21.5]*⁴ and the WTO panel decision in *EC- Biotech*⁵ are important cases the bench should bear in mind in this regard.

[23] Another key issue to be determined is with reference to the determination of ‘like’ products. The national treatment obligation in Article III prohibits a country from imposing taxes that discriminate in favor of its domestic producers at the expense of foreign producers. BTAs will fall foul of its requirements where an imported product is taxed “in excess’ of a “like’ domestic product. The key issue to be assessed is whether the imported and domestic products are ‘like’. To make this determination, panel looks at a non-exhaustive list of characteristics including (i) the properties, nature, and quality of the products, (ii) the end-uses of the products, (iii) consumers’ tastes and habits; and (iv) the tariff classification of the products. This “likeness’ determination is particularly likely to cause contention in the climate change context where products are alike with respect to these criteria, but differ in their PPMs (Processes and Production Methods). The question for determination is whether two products are ‘like’ if one consumes higher amount of energy during its production process.

⁴ *United States—Import Prohibition of Certain Shrimp and Shrimp Products—Recourse to Article 21.5 of the DSU by Malaysia*, WT/DS58/AB/RW, Report of the Appellate Body, 2001: Hereinafter: US-Shrimp.

⁵ *European Communities – Measures affecting the approval and marketing of Biotech products*, Report of the Panel, WT/DS291/R, 2006. Hereinafter: EC-Biotech.

Argument on behalf of the Parties

Azania

- a. Article 31(1) of the Vienna Convention on the Law of Treaties requires that a treaty be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in light of its object and purpose. Article 31(3) (c) requires that there shall be taken into account, together with the context, “any relevant rules of international law applicable in the relation between parties”. In this regard the WTO panel in *EC – Biotech* opined as follows

“In considering the provisions of Article 31 (3) (c), we note, initially, that it refers to ‘rules of international law’. Textually, this reference seems sufficiently broad to encompass all generally accepted sources of public international law, that is to say, (i) international conventions (treaties), (ii) international custom (customary international law), and (iii) the recognized general principles of law. In our view, there can be no doubt that treaties and customary rules of international law are “rules of international law” within the meaning of Article 31(3)(c).”⁶

Azania should argue that the UNFCCC and the Kyoto Protocol are applicable in the relations between the parties and therefore the ICJ should duly take it into account in interpreting the provisions of the Razvana Agreement on Trade in Goods (RATG).

- b. Azania should emphasize that the UNFCCC and the Kyoto Protocol are *lex specialis* as far as climate change is concerned and also represent multilateral efforts at arriving an appropriate way of addressing climate change concerns. The border tax implemented by Enroda results in the applied tax rate surpassing the bound rate commitments undertaken by Enroda in violation of Article 3.1(b) of the RATG. An escape route is provided under Article 3.2(a) which provides that nothing in “this Article” which includes Article 3.1(b), shall prevent any Member state from imposing at any time on the importation of a good a “charge equivalent to an

⁶ *EC-Biotech*, *Supra* note 5 , ¶ 6.67

internal tax imposed consistently with the provisions of paragraph 2 of Article 4 of the RFTA 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". Therefore the requirement is that the border tax applied by Enroda be consistent with Article 3.1(b).

- c. The participants are not expected to get into an extensive interpretation of the text of Article 3.2 (b). The WTO Appellate Body Report in *India – Additional and Extra-additional Duties on Imports from the United States* [has laid down in sufficient detail, the meaning of the term “equivalent” and “consistently with the provisions of paragraph 2 of Article III”.⁷ In substance, the Appellate Body Report requires that a determination of whether the border tax is equivalent to the internal tax requires an examination that is both qualitative and quantitative in nature. A quantitative examination includes consideration of effect and value.⁸ The facts on record in this regard state that a border tax is applied on import of goods which is equivalent to the level of tax charges to the domestic industry or producers of the like product.⁹ Taxes charged are therefore to be considered to be equivalent within the meaning of Article 3.2(b).
- d. The issue in question is whether a classification of Azania as a “*developing country in an advanced stage of development*” and subjecting it to such border tax is permissible. As discussed above, Article 31 (3) (c) would require that the concessions and obligation under UNFCCC and the Kyoto Protocol are to be duly taken into account. Furthermore, it can be argued by Azania that the UNFCCC and Kyoto Protocol are *lex speciali*. Since no specific commitments are undertaken by Azania under the Convention, the measures undertaken by Enroda are tantamount to forcing upon Azania, commitments to which it had never conceded.
- e. Azania is a non Annexure I party of the Convention and a developing country. The connotation “*developing country in an advanced stage of development*” is a creation of the Government of Enroda and has no basis in the Climate Change Convention or other applicable law. In fact, by treating Azania differently from

⁷ *India – Additional and Extra-additional Duties on Imports from the United States*, Report of the Appellate Body, WT/DS360/R, ¶ 175

⁸ *Ibid*

⁹ *Compromis*, ¶ 24

developing countries which are supposedly not in an advanced stage of development, the Most Favoured Nation treatment is being violated. In this regard, it is relevant to note that the parties have requested the Court to decide this matter on the basis of the provisions of the Razvana Free Trade Agreement, rules and principles of general international law and all applicable treaties which includes provisions pertaining to MFN.¹⁰

- f. Furthermore, the Climate Change Convention provides sufficient discretion to parties as to how it should address climate change concerns. Azania is taking concrete steps to address climate change concerns though it is not legally required to do so. Article 3.2(a) of the RATG cannot come to an aid of the importing state when a border tax is not payable by developing countries such as Azania in the first place.
- g. A carbon tax is a tax on inputs not incorporated into the final product—in other words, a tax on the production process alone. Azania may assert that under existing GATT rules and jurisprudence, "product" taxes and charges can be adjusted at the border, but "process" taxes and charges by and large cannot. For example, a domestic tax on fuel can be applied perfectly legitimately to imported fuel, but a tax on the energy consumed in producing a ton of steel cannot be applied to imported steel.¹¹ Dispute panels *United States – Tuna Dolphin*¹² case of 1991 and subsequent case of *Tuna Dolphin II*¹³ in 1996 ruled that countries cannot discriminate against products based on the way they are produced.

¹⁰ *Compromis*, Article II (a)

¹¹ Marrakesh Declaration - Item 3(a), World Trade Organization, "Taxes for Environmental Purposes" , available at http://www.wto.org/english/tratop_e/envir_e/envir_backgrnd_e/c3s3_e.htm; Available at http://www.wto.org/english/tratop_e/edis04_e.htm, (visited Jan 15,2009)

¹² GATT, United States - Restrictions on Imports of Tuna (DS21/R), Report of the Panel, Sept. 3, 199. It should be noted that the panel report was circulated in 1991, but not adopted, so it does not have the status of a legal interpretation of GATT law.

¹³ GATT, United States - Restrictions on Imports of Tuna (DS29/R), Report of the Panel, June 1994.

Defence under Article XX

Article XX (b) & Article XX (g)

- h. Article XX (b) can be invoked under WTO law when the measure undertaken is a measure to protect human life or health, and secondly, it must be necessary.¹⁴ In the facts of the present case the question to be examined is whether the measure undertaken by Enroda is a measure to protect human life or health. Azania could argue that a blanket imposition of border tax on imports based solely on the relevant amount of tax applied to the domestic industry, fails to take into consideration the steps taken by either the exporting producer or the exporting country in addressing climate change and by extension concerns of human life and health. Therefore the measure is actually directed at nullifying the tax burden borne by the domestic industry. Therefore the first requirement under Article XX (b) is not satisfied.
- i. A necessity test has evolved into a weighing and balancing of three factors (1) whether and the degree to which the common interests protected by the measure are vital and important; (2) whether alternative measures are “reasonably available” to accomplish the shared objective; (3) whether alternative measures are less consistent with the Member’s obligations.¹⁵ The participants can make arguments based on the facts that less trade restrictive alternatives were available with Enroda. Participants are free to determine what they consider to be less trade restrictive alternatives. They should be duly credited if they can provide illustration of such less trade restrictive alternatives which are practical and workable.
- j. While there is little basis to argue that climate cannot be brought within the realm of exhaustible natural resources, Azania could argue that the measures taken by Enroda do not fall within the scope of measures “*relating to the conservation of exhaustible natural resources*” of Article XX(g). The Appellate Body Reports in *US – Gasoline* and *Shrimp Turtle* are relevant in this regard. There are

¹⁴ *US - Gasoline*, *Supra* note 1 , p. 16; See generally *European Communities – Measures Affecting Asbestos and Products Containing Asbestos*, WT/DS135/AB/R, Report of the Appellate Body, 2001

¹⁵ *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, Report of Appellate Body, WT/DS161/AB/R, 2001, ¶¶ 162-166.

two relevant related tests emanating from *US – Gasoline* and *Shrimp Turtle*. The Appellate Body in *US – Gasoline* examined the ‘relating to’ requirement in Article XX (g) by examining whether the measure was primarily aimed at conservation of exhaustible natural resources. The application of this test by the Appellate Body is accompanied by a caveat that *“All the participants and the third participants in this appeal accept the propriety and applicability of the view of the Herring and Salmon report and the Panel Report that a measure must be ‘primarily aimed at’ the conservation of exhaustible natural resources in order to fall within the scope of Article XX (g). Accordingly, we see no need to examine this point further, save, perhaps, to note that the phrase “primarily aimed at” is not itself treaty language and was not designed as a simple litmus test for inclusion or exclusion from Article XX (g).”*¹⁶(The primary effects test nevertheless remains relevant in the interpretation of “relating to”. In paragraph the Appellate Body stated that “In a particular case, should it become clear that realistically, a specific measure cannot in any possible situation have any positive effect on conservation goals, it would very probably be because that measure was not designed as a conservation regulation to begin with. In other words, it would not have been “primarily aimed at” conservation of natural resources at all.

- k. The Appellate Body in *Shrimp Turtle* on the other hand adopted a means - end test stating with regard to the facts of the case *“In the present case, we must examine the relationship between the general structure and design of the measure here at stake, Section 609, and the policy goal it purports to serve, that is, the conservation of sea turtles”* ¹⁷The Appellate Body finally concluded that *“the means are, in principle, reasonably related to the ends. The means and ends relationship between Section 609 and the legitimate policy of conserving an exhaustible, and, in fact, endangered species, is observably a close and real one, a relationship that is every bit as substantial as that which we found in United States - Gasoline between*

¹⁶ *US-Gasoline*, *Supra* note 1, p. 18, 19

¹⁷ *United States—Importation Prohibition of Certain Shrimp and Shrimp Products*, Report of the Appellate Body, WT/DS58/AB/R, 1998, ¶ 137

*the EPA baseline establishment rules and the conservation of clean air in the United States.*¹⁸

- I. Azania could argue that even if the end that is pursued is legitimate, excessive means have been used by Enroda. The Appellate Body in *Shrimp Turtle* had opined that “*Focusing on the design of the measure here at stake, it appears to us that Section 609, cum implementing guidelines, is not disproportionately wide in its scope and reach in relation to the policy objective of protection and conservation of sea turtle species*”. The present measure however is disproportionately wide compared to the policy objective it seeks to address. The Framework Convention gives sufficient discretion to countries as to the modalities it prefers to adopt in addressing climate change concerns. Though Azania is a developing country with no positive commitments under the UNFCCC or Kyoto, it has taken proactive steps in mitigating greenhouse gas emissions. Enroda however has failed to duly take this into consideration and has pursued a blanket border tax adjustment policy.

Defence under the Chapeau of Article XX & Article 3.5 of the UNFCCC

- m. The chapeau of Article XX of GATT 1994, Article 3.5 of the UNFCCC and Article 2.3 of the Kyoto Protocol presents a common concern that trade restrictive measures undertaken in pursuance of legitimate policy objective should not result in arbitrary or unjustifiable discrimination or a disguised restriction on international trade. The chapeau of Article XX requires that

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:

Article 3.5 using slightly different language than Article XX states

¹⁸ *Ibid*, ¶ 141

Measures taken to combat climate change, including unilateral ones, should not constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade.

- n. The WTO Appellate Body in *Shrimp Turtle* laid down three prerequisites which need to be examined to establish a violation of the chapeau. First, the application of the measure must result in discrimination. Second, the discrimination must be unjustifiable or arbitrary in character. Third, the discrimination must occur between countries where the same conditions prevail.¹⁹
- o. The appellant must argue that Enroda discriminates against imports from Azania as compared to imports from other developing countries. It must be argued that similar conditions prevail in the developing countries. Enroda has divided developing countries into two groups i.e. developing countries in an advanced stage of development and other developing countries. This distinction is a classification made by the Government of Enroda and does not have support or basis in international law. The chapeau refers to countries in which similar conditions prevail and not identical conditions. Similar condition, Azania must argue should be understood in the context of relevant factors such as the financial and economic capability of the countries in question to take up onerous commitments to combat climate change as also the historical contribution towards greenhouse gas emissions. The preamble of the UNFCCC recognizes that developing countries have historically contributed towards greenhouse gas emissions. Azania has been classified as a non Annexure 1 country under the UNFCCC, which means like other developing countries to which the Enroda measures do not apply, specific commitments are not required to be undertaken by it. Under such conditions the discrimination is with countries where similar conditions prevail.
- p. Azania could cite the Appellate Body Report in *US – Shrimp* wherein the Appellate Body provided illustrations of what constituted arbitrary and unjustifiable discrimination. Noting the “*intended and actual coercive effect on other*

¹⁹ *US-Shrimp*, *Supra* note 4, ¶ 150

governments” to “adopt essentially the same policy” as the United States),²⁰ the Appellate Body concluded that “discrimination exists”, inter alia, “when the application of the measure at issue does not allow for any inquiry into the appropriateness of the regulatory programme for the conditions prevailing in those exporting countries”. In addition the requirement of due process was introduced in the chapeau by the Appellate Body through its determination that procedures under which United States authorities were granting the certification which foreign countries were required to obtain in order for their nationals to import shrimps into the United States were “informal” and “casual” and not “transparent” and “predictable.”²¹

[24] In light of the above, Azania must conclude that the imposition of a border tax by Enroda results in a violation of the Scheduled commitments undertaken by Enroda under Article 3.1(b) of the RATG. There is no basis for the applicability of the General Exception provisions under Article XX of RATG

Enroda

- a. Enroda must argue that the “*relevant rules of international law applicable in the relation between parties*” within the meaning of Article 31.3(c) of the VCLT includes principles of customary international law in addition to treaty law. In this regard, Enroda could build a case on the applicability of international principles such as the precautionary principle. Under this approach, the obligation on Enroda would be twofold. First, it must be able to establish that principles cited by it, such as the precautionary principle have attained the status of customary international law. Second, it must argue as to why and how such customary international law principles should be taken into consideration by the panel in interpreting the treaty text. In this regard it is relevant to note, that while WTO jurisprudence has adopted a certain approach towards the applicability of principles, such as the precautionary principle, the present dispute is before the International Court of Justice. The scope and mandate before the ICJ is broader than that available to a

²⁰ *US-Shrimp*, *Supra* note 4, ¶161

²¹ *Supra* note 4, ¶¶ 180-181.

WTO panel or Appellate Body. Under Article 27.2 of the *Agreement on Settlement of Disputes arising out of the RFTA*, WTO panel and Appellate Body Reports shall serve as a subsidiary source of law in interpretation.

- b. The right to take unilateral action to combat climate change is recognized in Article 3.5 of the UNFCCC. The only obligation imposed on a Member state is that the measure in question must not be an arbitrary or unjustifiable discrimination or a disguised restriction on trade. To the extent there exists a conflict, the principle of "*lex posterior*" shall be applicable, with the RFTA of 1995 taking precedence over the UNFCCC, 1995.
- c. Enroda must state that the imposition of a border tax squarely falls within the scope of "*a charge equivalent to an internal tax imposed consistently with the provisions of paragraph 2 of Article 4 of the RFTA*". The charge is equivalent to the internal carbon tax imposed on the domestic industries based in Enroda. Enroda has the right to take unilateral measures, which include measures against developing countries to ensure that the environmental regulation put in place by it is both even-handed and effective.
- d. It may be further submitted by Enroda, that the steps taken by Azania are inadequate in light of its present contribution towards green house gas emissions. Therefore Enroda was not required to make concessions or allowances for the steps taken by Azania.
- e. Enroda shall argue that process based BTAs is legal and non-discriminatory. *Shrimp/Turtle* case of 1998 indicates that the strictness of the WTO's "product-process" distinction has subsided since it first appeared in the 1991 *Tuna/Dolphin* case and that discrimination based on process and production methods may be permitted. In addition ICJ is not bound by strict WTO rules and it shall be reasonable to allow carbon taxes bases on inputs used in production process to achieve environmental goals and also to ensure that domestic goods and imported goods be treated equally.

Defence under Article XX

Article XX (b) & Article XX (g)

- f. Article XX (b) can be invoked under WTO law when the measure undertaken is a measure to protect human life or health, and is necessary.²² In the facts of the present case the question to be examined is whether the measure undertaken by Enroda is a measure to protect human life or health. Enroda could argue that the relevant measure undertaken by it is the Carbon Tax Regulation Act. The primary purpose of the Act is to lay down effective steps to mitigate factors that contribute towards climate change. The linkage of the adverse effect of climate change on human life and health is beyond the realm of dispute. Relevant scientific evidence could be cited by the Respondent to substantiate the claim. Therefore the Act including Section 17 thereof is a measure designed to protect human life or health.
- g. The necessity test requires a search for less trade restrictive alternate measures which are reasonably available. The decision of Enroda to impose a border tax is quite necessary to ensure the effectiveness of the measure undertaken by it. If no border tax is imposed, the imports on which no equivalent tax is imposed shall successfully undercut the domestic industry sales, which shall discourage domestic production. Under such circumstances, the sole effect of the domestic carbon tax shall be to reduce domestic production and increase production in exporting countries without any check on the GHG emissions of such exporters. Since GHG emissions effect global climate rather than a restricted region, public health and life in Enroda shall also be significantly affected. There are no alternative measures reasonably available and comparable in effectiveness which Enroda could take recourse to, to successfully regulate emissions.
- h. The Appellate Body in *Korea-Beef* has acknowledged that contribution of the alternative method in realization of the end pursued is extremely relevant²³ adding that *'the more vital or important the common interests or values' pursued, the easier it would be to accept as 'necessary' measures designed to achieve those*

²² *US-Gasoline*, *Supra* note 1, p. 30–31

²³ *Korea – Beef*, *Supra* note 14, ¶¶ 163 & 166

ends”²⁴. Therefore an examination of Article XX (b) should suitably examine the importance of the common interests which are being pursued.

- i. Global climate is an exhaustible natural resource within the meaning of Article XX (g) of the RATG. The relevant question is whether the measure undertaken by Enroda is relating to the conservation of the exhaustible natural resource and is made effective in conjunction with restriction on domestic production. The answer to both the questions is in the affirmative.
- j. The “primarily aimed at” test of *US – Gasoline* as well as the “means – end “ test of *US – Shrimp* sufficiently show that the measure undertaken by Enroda is relating to the conservation of an exhaustible natural resource. In this regard, it must be argued by Enroda that the relevant measure is the Carbon Tax Regulation Act taken a whole rather than the trade restrictive provision of the Act i.e. Section 17, taken in isolation. The observation of the Appellate Body in *US – Gasoline* is relevant wherein in the facts of the case it was opined that

*“[The] problem with the reasoning in that paragraph is that the Panel asked itself whether the ‘less favourable treatment’ of imported gasoline was ‘primarily aimed at’ the conservation of natural resources, rather than whether the ‘measure’, i.e. the baseline establishment rules, were ‘primarily aimed at’ conservation of clean air. In our view, the Panel here was in error in referring to its legal conclusion on Article III:4 instead of the measure in issue. The result of this analysis is to turn Article XX on its head. Obviously, there had to be a finding that the measure provided ‘less favourable treatment’ under Article III:4 before the Panel examined the ‘General Exceptions’ contained in Article XX. That, however, is a conclusion of law. The chapeau of Article XX makes it clear that it is the ‘measures’ which are to be examined under Article XX (g), and not the legal finding of ‘less favourable treatment.’”*²⁵

- k. Since the Carbon Tax Regulation Act is primarily aimed at the conservation of exhaustible natural resource and is the necessary means towards the end - preservation of the climate i.e. the measure is justified under Article XX (g).

²⁴ *Ibid*, ¶ 163

²⁵ *US-Gasoline*, *Supra* note 1, p.16

Application of the measure is even handed and the domestic producers and exporters are treated on a level footing and subject to the same level of treatment.

Defence under the Chapeau of Article XX & Article 3.5 of the UNFCCC

- l. Enroda must contend that it reserves the right to take unilateral measures to combat climate change. Article 3.5 does not in any way preclude action against developing countries.
- m. The threefold requirement imposed by the chapeau as elucidated in the Appellate Body Report in *Shrimp Turtle* is as follows
 1. The application of the measure must result in discrimination.
 2. The discrimination must be unjustifiable or arbitrary in character.
 3. Discrimination must occur between countries where the same conditions prevail.
- n. The Respondent could very well argue that similar conditions cannot be deemed to prevail in developing countries like Azania which are in an advanced stage of economic development and other developing countries. Classification of Azania into a separate group distinguishable from other developing countries is justifiable. In fact treating relatively prosperous developing countries like Azania at par with developing countries which are yet to attain such levels of prosperity would be unjustified.
- o. Furthermore, the discrimination is not unjustifiable or arbitrary. Developing countries have made serious effort good faith efforts at negotiation at a multilateral level under the aegis of the Framework Convention to request developing countries which are in an advanced stage of development to take up meaningful responsibility in combating climate change. The Convention and the Kyoto Protocol address the question of specific commitments to be undertaken by the Member State. At no point of time does it require that measures to combat climate change be limited to developed or Annex I countries. If such was the intention of the drafter, specific reference would have been made to this effect in Article 3.5 of UNFCCC. Any alternative interpretation would abrogate the right of

nations like Enroda to take appropriate measures to combat climate change and result in an interpretation of the text in a manner which was never intended by the drafters.

[25] Enroda can therefore conclude that the measures it undertakes are in full conformity with Article 3.2(a) of the RATG and are justified under the General Exceptions of the Agreement.