WORLD TRADE ORGANIZATION

WT/DS2/9
20 May 1996

(96-1932)

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UNITED STATES - STANDARDS FOR REFORMULATED AND CONVENTIONAL GASOLINE

Appellate Body Report and Panel Report

Action by the Dispute Settlement Body

At its meeting on 20 May 1996, the Dispute Settlement Body adopted the attached Appellate Body report on "United States - Standards for Reformulated and Conventional Gasoline" (WT/DS2/AB/R) and the attached panel report on "United States - Standards for Reformulated and Conventional Gasoline" (WT/DS2/R) as modified by the Appellate Body report. The panel report should therefore be read in conjunction with the Appellate Body report.

Both reports have been derestricted upon their adoption by the Dispute Settlement Body.

RESTRICTED

WT/DS2/AB/R

29 April 1996

(96-1597)

WORLD TRADE ORGANIZATION

Appellate Body

United States - Standards for

WORLD TRADE ORGANIZATION
APPELLATE BODY

United States - Standards for Reformulated and Conventional Gasoline	**AB-1996-1**
United States, Appellant Brazil Venezuela, Appellees European Communities Norway, Third Participants	Present: Feliciano, Presiding Member Beeby, Member Matsushita, Member

I. Introductory

The United States appeals from certain conclusions on issues of law and certain legal interpretations contained in the Panel Report, *United States - Standards for Reformulated and Conventional Gasoline*, WT/DS2/R, 29 January 1996 (the "Panel Report"). That Panel had been established to consider a dispute between the United States, on the one hand, and Venezuela,

' Environmental Protection Agency (the "EPA") pursuant to that Act, to control toxic and other pollution caused by the combustion of gasoline manufactured in or imported into the United States. This regulation is formally entitled "*Regulation of Fuels and Fuel Additives - Standards for Reformulated and Conventional Gasoline*", Part 80 of Title 40 of the Code of Federal Regulations,[1] and is commonly referred to as the Gasoline Rule.

[1]40 CFR 80, 59 Fed. Reg. 7716 (16 February 1994).

Working Procedures.

[5]Pursuant to Rule 22(1) of the *Working Procedures*.

[6]Pursuant to Rule 24 of the *Working Procedures*.

[7]Pursuant to Rule 25 of the *Working Procedures*.

[8]The oral hearing was originally scheduled for 25 March 1996 but had, for exceptional and unavoidable reasons, to be deferred to 27 and 28 March 1996.

[9]Rule 28 of the *Working Procedures*.

[10]Rule 28(1) of the *Working Procedures*.

B. The Clean Air Act and its Implementation

The CAA and its implementation by the Gasoline Rule, are described fully at paragraphs 2.1-2.13 of the Panel Report. However, it may be convenient to recall a number of the Panel's factual findings at this stage.

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The CAA established two gasoline programs[11] to ensure that pollution

gasoline

C. The Panel Report: Its Findings and Conclusions

The Panel's overall conclusions and its recommendation are set out in the following terms:

> 8.1 In the light of the findings above, the Panel concluded that the baseline establishment methods contained in Part 80 of Title 40 of the Code of Federal Regulations are not consistent with Article III:4 of the General Agreement, and cannot be justified under paragraphs (b), (d) and (g) of Article XX of the General Agreement.
>
> 8.2 The Panel *recommends* that

(iv) that the "aspect of the baseline establishment methods" found inconsistent with Article III:4 was not justified under Article XX(b) of the *General Agreement* as "necessary to protect human, animal or plant life or health";[21]

(v) that the "maintenance of discrimination between imported and domestic gasoline" contrary to Article III:4 was not justified under Article XX(d) as "necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of [the General] Agreement";[22]

(vi) that clean air was an exhaustible natural resource within the meaning of Article XX(g) of the *General Agreement*;[23]

(vii) that the baseline establishment rules found to be inconsistent with Article III:4 could not be justified under Article XX(g) as a measure "relating to" the conservation of exhaustible natural resources;[24]

(viii) that it was unnecessary, in the light of finding (vii), to determine whether the measure at issue was "made effective in conjunction with restrictions on domestic production or consumption";[25]

(ix) that it was unnecessary, in the light of finding (vii), to determine whether the measure at issue met the conditions in the introductory clause of Article XX (sometimes referred to as the chapeau of Article XX);

(x) that it was unnecessary, in view of findings (ii), (iv), (v) and (vii), to determine whether the measure at issue was inconsistent with Article XXIII:1(b) as having nullified and impaired benefits accruing under the *General Agreement*;[26] and

[21]Panel Report, para. 6.29.

[22]Panel Report, para. 6.33.

[23]Panel Report, para. 6.37.

[24]Panel Report, para. 6.40.

[25]Panel Report, para. 6.41.

[26]Panel Report, para. 6.42.

(xi) that it was unnecessary, in the light of findings (ii), (iv), (v) and (vii), to determine whether the measure at issue was inconsistent with Articles 2.1 and 2.2 of the *Agreement on Technical Barriers to Trade* (the "*TBT Agreement*").[27]

II. Issues Raised In This Appeal

A. The Claims of Error by the United States

It is important to focus upon the subject matter of this appeal. We seek to do this first by identifying the issues which have been raised by the Appellant, the United States. In what follows we highlight those same issues by listing certain other issues dealt with in the Panel proceedings but which have *not* been brought before the Appellate Body in this appeal, and which we accordingly exclude from consideration in this Appellate Report.

In its Notice of Appeal, dated 21 February 1996, and its Appellant's Submission, dated 4 March 1996, the United States claims that the Panel erred in law, firstly, in holding that the baseline establishment rules of the Gasoline Rule are not justified under Article XX(g) of the *General Agreement* and, secondly, in its interpretation of Article XX as a whole.

More specifically, the United States assigns as error the ruling of the Panel that the baseline establishment rules do not constitute a "measure" "relating to" the conservation of clean air within the meaning of Article XX(g) of the *General Agreement*. Consequently, it is also the view of the United States that the Panel erred in failing to proceed further in its interpretation and application of Article XX(g), and in not finding that the baseline establishment rules satisfy the other requirements of Article XX(g) and the introductory provisions of Article XX.

The sharply limited scope of this appeal is underscored by noting the number of findings which the Panel had made but which have not been appealed from by the United States. Very briefly, the United States does not appeal from the findings or rulings made by the Panel on, or in respect of, the consistency of the baseline establishment rules with Article I:1, Article III:1, Article III:4, and Article XXIII:1(b) of the *General Agreement* and the applicability of Article XX(b) and Article XX(d) of the *General Agreement* and of the *TBT Agreement*. Understandably, the United States has also not

[27]Panel Report, para. 6.43.

appealed from the Panel's ruling that clean air is an exhaustible natural resource within the meaning of Article XX(g) of the *General Agreement*.

B. The Claims of the Appellees and the Arguments of the Third Participants

The Appellees, Venezuela and Brazil, submit that the Appellate Body should dismiss the United States' appeal and uphold the Panel's findings and conclusions concerning Article

The third participants, the European Communities and Norway, endorse the Panel's interpretation of "relating to" and the Panel's findings under Article XX(g). They find it difficult to accept the United States' arguments that the measure at issue was "made effective in conjunction with restrictions on domestic production or consumption," as the measure in issue did not impose restrictions on clean air. With regard to the Article XX chapeau

III. The Issue of Justification Under Article XX(g)

provisions infringing Article III:4.[28] These earlier panels had not interpreted "measures" more broadly under Article XX to include provisions not themselves found inconsistent with Article III:4. In the present appeal, no one has suggested in their final submissions that the Appellate Body should examine under Article XX any portion of the Gasoline Rule other than the baseline establishment rules held to be in conflict with Article III:4. No one has urged an interpretation of "measures" which would encompass the Gasoline Rule in its totality.[29]

At the oral hearing and in its Post-Hearing Memorandum, the United States complained about the designation of the baseline establishment rules in the Panel Report and by the Appellees Venezuela and Brazil, in such terms as "the difference in treatment", "the less favourable treatment" or "the discrimination." It is, of course, true that the baseline establishment rules had been found by the Panel to be inconsistent with Article III:4 of the *General Agreement*. The frequent designation of those

'measure' with which this appeal is concerned is the baseline methodology of the Gasoline Rule, not the entire rule itself." This would suggest a position similar to that adopted by the United States. Thereafter, Brazil continued to state that "Brazil and Venezuela did not challenge all portions of the Rule; they challenged only the discriminatory methods of establishing baselines."

Venezuela stated, in its summary statement, dated 29 March 1996, that "the measure to be examined is the discriminatory measure, that is, the aspect of the Gasoline Rule that denies imported gasoline the right to use the same regulatory system of baselines applicable to U.S. gasoline, namely, the system of individual baselines."

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less favourable treatment to imported gasoline *were primarily aimed at* the conservation of natural resources" (emphasis added). The Panel did not try to clarify whether the phrase "direct connection" was being used as a synonym for "primarily aimed at" or whether a new and additional element (on top of "primarily aimed at") was being demanded.

One 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

ARTICLE 31

General rule of interpretation

> 1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.

The "general rule of interpretation" set out above has been relied upon by all of the participants and third participants, although not always in relation to the same issue. That general rule of interpretation has attained the status of a rule of customary or general international law.[34] As such, it forms part of the "customary rules of interpretation of public international law" which the Appellate Body has been directed, by Article 3(2) of the *DSU*, to apply in seeking to clarify the provisions of the *General Agreement* and the other "covered agreements" of the *Marrakesh Agreement Establishing the World Trade Organization*[35] (the "*WTO Agreement*"). That direction reflects a measure of recognition that the *General Agreement* is not to be read in clinical isolation from public international law.

Applying the basic principle of interpretation that the words of a treaty, like the *General Agreement*, are to be given their ordinary meaning, in their context and in the light of the treaty's object and purpose, the Appellate Body observes that the Panel Report failed to take adequate account of the words actually used by Article XX in its several paragraphs. In enumerating the various categories of governmental acts, laws or regulations which WTO Members may carry out or promulgate in pursuit of differing legitimate state policies or interests outside the realm of trade liberalization, Article XX uses different terms in respect of different categories:

"necessary" - in paragraphs (a), (b) and (d);	"essential" - in paragraph (j);
"relating to" - in paragraphs (c), (e) and (g);	"for the protection of" - in paragraph (f);
"in pursuance of" - in paragraph (h); and	"involving" - in paragraph (i).

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[34]

's International Law (9th ed., Jennings and Watts, eds. 1992) Vol. 1, pp. 1271-1275.

[35]Done at Marrakesh, Morocco, 15 April 1994.

It does not seem reasonable to suppose that the WTO Members intended to require, in respect of each and every category, the same kind or degree of connection or relationship between the measure under appraisal and the state interest or policy sought to be promoted or realized.

At the same time, Article XX(g) and its phrase, "relating to the conservation of exhaustible natural resources," need to be read in context and in such a manner as to give effect to the purposes and objects of the *General Agreement*. The context of Article XX(g) includes the provisions of the rest of the *General Agreement*, including in particular Articles I, III and XI; conversely, the context of Articles I and III and XI includes Article XX. Accordingly, the phrase "relating to the conservation of exhaustible natural resources" may not be read so expansively as seriously to subvert the purpose and object of Article III:4. Nor may Article III:4 be given so broad a reach as effectively to emasculate Article XX(g) and the policies and interests it embodies. The relationship between the affirmative commitments set out in, *e.g.*, Articles I, III and XI, and the policies and interests embodied in the "General Exceptions" listed in Article XX, can be given meaning within the framework of the *General Agreement* and its object and purpose by a treaty interpreter only on a

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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).

Against this background, we turn to the specific question of whether the baseline establishment rules are appropriately regarded as "primarily aimed at" the conservation of natural resources for the purposes of Article XX(g). We consider that this question must be answered in the affirmative.

The baseline establishment rules, taken as a whole (that is, the provisions relating to establishment of baselines for domestic refiners, along with the provisions relating to baselines for blenders and importers of gasoline), need to be related to the "non-degradation" requirements set out elsewhere in the Gasoline Rule. Those provisions can scarcely be understood if scrutinized strictly by themselves, totally divorced from other sections of the Gasoline Rule which certainly constitute part of the context of these provisions. The baseline establishment rules whether individual or statutory, were designed to permit scrutiny and monitoring of the level of compliance of refiners, importers and blenders with the "non-degradation" requirements. Without baselines of some kind, such scrutiny would not be po

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The claim of the United States is that the second clause of Article XX(g) requires that the burdens entailed by regulating the level of pollutants in the air emitted in the course of combustion of gasoline, must not be imposed solely on, or in respect of, imported gasoline.

On the other hand, Venezuela and Brazil refer to prior panel reports which include statements to the effect that to be deemed as "made effective in conjunction with restrictions on domestic production or consumption", a measure must be "primarily aimed at" making effective certain restrictions on domestic production or consumption.[38] Venezuela and Brazil also argue that the United States has failed to show the existence of restrictions on domestic production or consumption of a natural resource under the Gasoline Rule since clean air was not an exhaustible natural resource within the meaning of Article XX(g). Venezuela contends, finally, that the United States has not discharged its burden of showing that the baseline establishment rules make the United States' regulatory scheme "effective." The claim of Venezuela is, in effect, that to be properly regarded as "primarily aimed at" the conservation of natural resources, the baseline establishment rules must not only "reflect a conservation purpose" but also be shown to have had "some positive conservation effect."[39]

The Appellate Body considers that the basic international law rule of treaty interpretation, discussed earlier, that the terms of a treaty are to be given their ordinary meaning, in context, so as to effectuate its object and purpose, is applicable here, too. Viewed in this light, the ordinary or natural meaning of "made effective" when used in connection with a measure - a governmental act or regulation - may be seen to refer to such measure being "operative", as "in force", or as having "come into effect."[40] Similarly, the phrase "in conjunction with" may be read quite plainly as "together with" or "jointly with."[41] Taken together, the second clause of Article XX(g) appears to us to refer to governmental measures like the baseline establishment rules being promulgated or brought into effect together with restrictions on domestic production or consumption of natural resources. Put in a slightly different manner, we believe that the clause "if such measures are made effective in conjunction with restrictions on domestic product or consumption" is appropriately read as a requirement that the measures concerned impose restrictions, not just in respect of imported gasoline but also with respect to domestic gasoline.

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[38]*Canada - Measures Affecting Exports of Unprocessed Herring and Salmon*, BISD 35S/98, paras. 4.6-4.7; adopted 22 March 1988. Also, *United States - Restrictions on Imports of Tuna*, DS29/R (1994), unadopted; and *United States - Taxes on Automobiles*, DS31/R (1994), unadopted.

[39]Venezuela's Appellee's Submission, dated 18 March 1996; Venezuela's Statement at the Oral Hearing, dated 27 March 1996.

[40]The New Shorter Oxford English Dictionary on Historical Principles (L. Brown, ed., 1993), Vol. I, p. 786.

Submission.

The clause is a requirement of *even-handedness* in the imposition of restrictions, in the name of conservation, upon the production or consumption of exhaustible natural resources.

There is, of course, no textual basis for requiring identical treatment of domestic and imported products.

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.

IV. The Introductory Provisions of Article XX of the General Agreement: Applying the Chapeau of the General Exceptions

Having concluded, in the preceding section, that the baseline establishment rules of the Gasoline Rule fall within the terms of Article XX(g), we come to the question of whether those rules also meet the requirements of the chapeau of Article XX. In order that the justifying protection of Article XX may be extended to it, the measure at issue must not only come under one or another of the particular exceptions - paragraphs (a) to (j) - listed under Article XX; it must also satisfy the requirements imposed by the opening clauses of Article XX. The analysis is, in other words, two-tiered: first, provisional justification by reason of characterization of the measure under XX(g); second, further appraisal of the same measure under the introductory clauses of Article XX.

The chapeau by its express terms addresses, not so much the questioned measure or its specific contents as such, but rather the manner in which that measure is applied.[43] It is, accordingly, important to underscore that the purpose and object of the introductory clauses of Article XX is generally the prevention of "abuse of the exceptions of [what was later to become] Article [XX]."[44] This insight drawn from the drafting history of Article XX is a valuable one. The chapeau is animated by the principle that while the exceptions of Article XX may be invoked as a matter of legal right, they should not be so applied as to frustrate or defeat the legal obligations of the holder of the right under the substantive rules of the *General Agreement*. If those exceptions are not to be abused or misused, in other words, the measures falling within the particular exceptions must be applied reasonably, with due regard both to the legal duties of the party claiming the exception and the legal rights of the other parties concerned.

The burden of demonstrating that a measure provisionally justified as being within one of the exceptions set out in the individual paragraphs of Article XX does not, in its application, constitute

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[43]This was noted in the Panel Report on *United States - Imports of Certain Automotive Spring Assemblies*, BISD 30S/107, para. 56; adopted on 26 May 1983.

[44]EPCT/C.11/50, p. 7; quoted in Analytical Index: Guide to GATT Law and Practice, Volume I, p. 564 (1995).

abuse of such exception under the chapeau, rests on the party invoking the exception. That is, of necessity, a heavier task than that involved in showing that an exception, such as Article XX(g), encompasses the measure at issue.

The enterprise of applying Article XX would clearly be an unprofitable one if it involved no more than applying the standard used in finding that the baseline establishment rules were inconsistent with Article III:4. That would also be true if the finding were one of inconsistency with some other substantive rule of the *General Agreement*. The provisions of the chapeau cannot logically refer to the same standard(s) by which a violation of a substantive rule has been determined to have occurred. To proceed down that path would be both to empty the chapeau of its contents and to deprive the exceptions in paragraphs (a) to (j) of meaning. Such recourse would also confuse the question of whether inconsistency with a substantive rule existed, with the further and separate question arising under the chapeau of Article XX as to whether that inconsistency was nevertheless justified. One of the corollaries of the "general rule of interpretation" in the *Vienna Convention* is that interpretation must give meaning and effect to all the terms of a treaty. An interpreter is not free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility.[45]

The chapeau, it will be seen, prohibits such [illegible] of a measure at issue (otherwise falling within the scope of Article XX(g)) as would c[illegible]

(a) "arbitrary discrimination[illegible] countries where the same [illegible]s prevail);

(b) "unjustifiable discrimi[illegible]h the same qual028o54.48 3[illegible]F17 (a) aB0 1 194.16 453.6 T

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that phrase as referring to both the exporting countries and importing countries and as between exporting countries. It also said that the language spoke for itself, but there was no reference to third parties; while some thought that this was only between exporting countries *inter se*, there is no support in the text for that view. No such question was put to the United States concerning the field of application of the third standard - disguised restriction on international trade. But the United States put forward arguments designed to show that in the case under appeal, it had met all the standards set forth in the chapeau. In doing so, it clearly proceeded on the assumption that, whatever else they might relate to in another case, they were relevant to a case of national treatment where the Panel had found a violation of Article III:4. At no point in the appeal was that assumption challenged by Venezuela or Brazil. Venezuela argued that the United States had failed to meet all the standards contained in the chapeau. So did Norway and the European Communities as third participants. In short, the field of application of these standards was not at issue.

The assumption on which all the participants proceeded is buttressed by the fact that the chapeau says that "*nothing in this Agreement* shall be construed to prevent the adoption or enforcement by any contracting party of measures ..." The exceptions listed in Article XX thus relate to all of the obligations under the *General Agreement*: the national treatment obligation and the most-favoured-nation obligation, of course, but others as well. Effect is more easily given to the words "nothing in this Agreement", and Article XX as a whole including its chapeau more easily integrated into the remainder of the *General Agreement*, if the chapeau is taken to mean that the standards it sets forth are applicable to all of the situations in which an allegation of a violation of a substantive obligation has been made and one of the exceptions contained in Article XX has in turn been claimed.

Against this background, we see no need to decide the matter of the field of application of the standards set forth in the chapeau nor to make a ruling at variance with the common understanding of the participants.[46]

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[46]We note in this connection that two previous panels had occasion to apply the chapeau. In *United States - Imports of Certain Automotive Spring Assemblies*, BISD 30S/107; adopted on 26 May 1983, the panel had before it a ban on imports, and an exclusion order of the United States' International Trade Commission, of certain automotive spring assemblies which the Commission had found, under Section 337 of the Tariff Act of 1930, to have infringed valid United States patents. The panel there held that the exclusion order had *not* been applied in a manner which would constitute a means of "arbitrary or unjustifiable discrimination against countries where the same conditions prevail," because that order was directed against imports of infringing assemblies "from all foreign sources, and not just from Canada." At the same time, the same order was also examined and found *not* to be "a disguised restriction on international trade." Id., paras. 54-56. See also *United States - Prohibition of Imports of Tuna and Tuna Products*, BISD 29S/91, para. 4.8; adopted 22 February 1982.

It may be observed that the term "countries" in the chapeau is textually unqualified; it does not say "foreign countries", as did Article 4 of the 1927 League of Nations *International Convention for the Abolition of Import and Export Prohibitions and Restrictions*, 97 L.N.T.S. 393. Neither does the chapeau say "third countries" as did, *e.g.*, bilateral trade
(continued...)

"Arbitrary discrimination", "unjustifiable

> and tracking the refinery or origin would be very difficult because gasoline is a fungible commodity. The United States should not have to prove that it cannot verify information and enforce its regulations in every instance in order to show that the same enforcement conditions do not prevail in the United States and other countries ... The impracticability of verification and enforcement of foreign refiner baselines in this instance shows that the "discrimination" is based on serious, not arbitrary or unjustifiable, concerns stemming from different conditions between enforcement of its laws in the United States and abroad.[47]

Thus, according to the United States, imported gasoline was relegated to the more exacting statutory baseline requirement because of these difficulties of verification and enforcement. The United States stated that verification and enforcement of the Gasoline Rule's requirements for imported gasoline are "much easier when the statutory baseline is used" and that there would be a "dramatic difference" in the burden of administering requirements for imported gasoline if individual baselines were allowed.[48]

While the anticipated difficulties concerning verifice

> to US regulation. The nature of the data in this case was similar to data relied upon by the United States in other contexts, including, for example, under the application of antidumping laws. In an antidumping case, only when the information was not supplied or deemed unverifiable did the United States turn to other information. If a similar practice were to be applied in the case of the Gasoline Rule, then importers could, for instance, be permitted to use the individual baselines of foreign refiners for imported gasoline from those refiners, with the statutory baseline being applied only when the source of imported gasoline could not be determined or a baseline could not be established because of an absence of data.[50]

We agree with the finding above made in the Panel Report. There are, as the Panel Report found, established techniques for checking, verification, assessment and enforcement of data relating to imported goods, techniques which in many contexts are accepted as adequate to permit international trade - trade between territorial sovereigns - to go on and grow. The United States must have been aware that for these established techniques and procedures to work, cooperative arrangements with both foreign refiners and the foreign governments concerned would

the process by denying funding, is beside the point: the United States, of course, carries responsibility for actions of both the executive and legislative departments of government.

In its submissions, the United States also explained why the statutory baseline requirement was not imposed on domestic refiners as well. Here, the United States stressed the problems that domestic refineries would have faced had they been required to comply with the statutory baseline. The Panel Report summarized the United States' argument in the following

of the foregoing, our conclusion is that the baseline establishment rules in the Gasoline Rule, in their application, constitute "unjustifiable discrimination" and a "disguised restriction on international trade." We hold, in sum, that the baseline establishment rules, although within the terms of Article XX(g), are not entitled to the justifying protection afforded by Article XX as a whole.

V. FINDINGS AND CONCLUSIONS

For the reasons set out in the preceding sections of this report, the Appellate Body has reached the following conclusions:

(a) the Panel erred in law in its conclusion that the baseline establishment rules contained in Part 80 of Title 40 of the Code of Federal Regulations did not fall within the terms of Article XX(g) of the *General Agreement*;

(b) the Panel accordingly also erred in law in failing to decide whether the baseline establishment rules contained in Part 80 of Title 40 of the Code of Federal Regulations fell within the ambit of the chapeau of Article XX of the *General Agreement*;

(c) the baseline establishment rules contained in Part 80 of Title 40 of the Code of Federal Regulations fail to meet the requirements of the chapeau of Article XX of the *General Agreement*, and accordingly are not justified under Article XX of the *General Agreement.*

The foregoing legal conclusions modify the conclusions of the Panel as set out in paragraph 8.1 of its Report. The Appellate Body's conclusions leave intact the conclusions of the Panel that were not the subject of appeal.

The Appellate Body *recommends* that the Dispute Settlement Body request the United States to bring the baseline establishment rules contained in Part 80 of Title 40 of the Code of Federal Regulations into conformity with its obligations under the *General Agreement*.

It is of some importance that the Appellate Body point out what this does *not* mean. It does not mean, or imply, that the ability of any WTO Member to take measures to control air pollution or, more generally, to protect the environment, is at issue. That would be to ignore the fact that

Article XX of the *General Agreement* contains provi
including the protection of human health, as well as
to find expression. The provisions of Article XX w
of Multilateral Trade Negotiations. Indeed, in the pr
on Trade and Environment,[54] there is specific ackn
coordinating policies on trade and the environment.
to determine their own policies on the environme
environmental objectives and the environmental legis
the WTO, that autonomy is circumscribed only by th
Agreement and the other covered agreements.

Signed in the original at Gene

WORLD TRADE ORGANIZATION

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WT/DS2/R

29 January 1996

(96-0326)

United States - Standards for Reformulated and Conventional Gasoline

Report of the Panel

Table of Contents

I. INTRODUCTION

1.1 On 23 January 1995, the United States received a request from Venezuela to hold consultations under Article XXII:1 of the General Agreement on Tariffs and Trade 1994 ("General Agreement"), Article 14.1 of the Agreement on Technical Barriers to Trade ("TBT Agreement") and Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"), on the rule issued by the Environmental Protection Agency on 15 December 1993, entitled "Regulation of Fuels and Fuel Additives - Standards for Reformulated and Conventional Gasoline" (WT/DS2/1). The consultations between Venezuela and the United States took place on 24 February 1995. As they did not result in a satisfactory solution of the matter, Venezuela, in a communication dated 25 March 1995, requested the Dispute Settlement Body ("DSB") to establish a panel to examine the matter under Article XXIII:2 of the General Agreement and Article 6 of the DSU (WT/DS2/2). On 10 April 1995, the DSB established a panel in accordance with the request made by Venezuela. On 28 April 1995, the parties to the dispute agreed that the Panel should have standard terms of reference (DSU, Art. 7)

1.7 The Panel met with the parties to the dispute from 10 to 12 July 1995 and from 13 to 15 September 1995. It met with the interested third parties on 11 July 1995.

1.8 On 21 September 1995, the Chairman of the Panel informed the DSB that the Panel would not be able to issue its report within six months. The reasons for that delay are stated in document WT/DS2/5.

1..9 The Panel issued its interim report to the parties on 11 December 1995. Following a request made by the United States pursuant to Article 15.2 of the DSU, the Panel held a further meeting with the parties on 3 January 1996.

1.10 The Panel issued its final report to the parties to the dispute on 17 January 1996.

II. FACTUAL ASPECTS

A. The Clean Air Act

2.1 The Clean Air Act ("CAA"), originally enacted in 1963, aims at preventing and controlling air pollution in the United States. In a 1990 amendment to the CAA[1], Congress directed the Environmental Protection Agency ("EPA") to promulgate new regulations on the composition and emissions effects of gasoline in order to improve air quality in the most polluted areas of the country by reducing vehicle emissions of toxic air pollutants and ozone-forming volatile organic compounds. These new regulations apply to US refiners, blenders and importers.

2.2 Section 211(k) of the CAA divides the market for sale of gasoline in the United States into two parts. The first part, which covers approximately 30 percent of gasoline marketed in the United States, consists of the nine large metropolitan areas that experienced the worst summertime ozone pollution during the period 1987-1989, plus any areas that do not meet national ozone requirements and are added at the request of the governor of the state. These areas are referred to as ozone "nonattainment areas", and in this part of the United States only "reformulated gasoline" may be sold to consumers. In the rest of the United States, "conventional gasoline" may be sold to consumers.

2.3 Section 211(k)(2)-(3) of the CAA established certain compositional and performance specifications for reformulated gasoline. The oxygen content must not be less than 2.0 percent by weight, the benzene content must not exceed 1.0 percent by volume and the gasoline must be free of heavy metals, including lead or manganese. The performance specifications of the CAA require a 15 percent reduction in the emissions of both volatile organic compounds ("VOCs") and toxic air pollutants ("toxics") and no increase in emissions of nitrogen oxides ("NOx"). These requirements are measured by comparing the performance of reformulated gasoline in baseline vehicles (representative model year 1990 vehicles) against the performance of "baseline gasoline" in such vehicles. Section 211(k)(10) of the CAA defines the specifications of baseline gasoline sold in the summer, which is the high ozone season, and leaves the specifications of winter baseline gasoline to be determined by EPA. It provides, however, that the specifications for winter gasoline shall be those of the industry average gasoline sold in 1990. For the year 2000 and beyond, the CAA requires that new reformulated gasoline requirements be developed that require a 20-25 percent reduction in emissions of VOCs and toxics, depending on EPA's considerations of feasibility and cost.

[1] 42 U.S.C. §7545(k).

2.4 The CAA also sets requirements for conventional gasoline, which ensure that each refiner's, blender's or importer's conventional gasoline sold in the rest of the country remains as clean as it was in 1990. This programme is known as "anti-dumping rules" because it is designed to prevent refiners, blenders or importers from dumping into conventional gasoline fuel components that are restricted in reformulated gasoline and that cause environmentally harmful emissions. To accomplish this, section 211(k)(8) of the CAA provides that no refiner, blender or importer of gasoline may sell conventional gasoline that emits VOCs, toxics, NOx or carbon monoxide ("pollutants") in greater amounts than the gasoline sold in the United States by that refiner, blender or importer in 1990. In order to implement this provision, separate individual baselines must be established for refiners, blenders or importers based on the gasoline they sold in 1990. That permits determination of whether the emissions from a refiner's, blender's and importer's conventional gasoline (post-1994 gasoline) are greater than the emissions from its 1990 gasoline. If, however, EPA determines that no adequate and reliable data exist regarding the composition of such 1990 gasoline sold by a refiner, blender or importer, the statutory baseline gasoline is applied. The statutory annual baseline values are calculated using

2.8 Certain entities are, however, automatically assigned to the statutory baseline. Firstly, refineries which began operation after 1990 or were in operation for less than 6 months in 1990 are required to use the statutory baseline. Secondly, importers and blenders are assigned the statutory baseline unless they can establish

The Gasoline Rule limits ("caps") the volume of conventional gasoline that is subject to an individual baseline to the volume of gasoline produced in 1990 by that entity; all conventional gasoline produced in excess of the specific volume cap is measured against the statutory baseline.

2.12 Domestic refiners and importers of conventional gasoline, unlike those of reformulated gasoline, will still be subject to different baselines after the entry into force of the Complex Model in 1998.

C. The May 1994 Proposal

2.13 In view of the comments made by interested parties

(a) consistent with Articles I and III of the General Agreement 1994;
(b) falling within the scope of Article XX (b), (d), and (g) of GATT 1994;
(c) consistent with the Agreement on Technical Barriers to Trade.

B. The General Agreement on Tariffs and Trade

1. Article I - General Most-Favoured-Nation Treatment

3.5 Venezuela and Brazil argued that the rule allowing an importer which was also a foreign refiner to establish its individual baseline, provided that it imported into the United States at least 75 percent of the gasoline produced at that refinery in 1990 ("75 % rule"), granted an advantage

an individual baseline for its gasoline. The United States also noted that the regulatory deadline for individual baseline applications under the 75 % rule had elapsed without any company meeting the criteria. The 75 % rule had no application and could therefore not be inconsistent with any provisions of the General Agreement.

3.9 Venezuela considered that the United States interpreted too narrowly the panel report "EEC - Imports of Beef From Canada" when saying that the favoured country must be expressly identified in order for the regulation to violate Article I. A rule violated Article I when it stipulated, like the 75 % rule, that the products of only some countries could qualify.

3.10 Venezuela and Brazil considered that the fact that the 75 % rule had no application should not prevent the Panel from ruling on it. Venezuela considered that the mere existence of such a regulation might have inhibiting effects on commercial and

argued that EPA's 1994 proposed amendments to the Gasoline Rule ("1994 Proposal") acknowledged that the discriminatory treatment of imported gasoline was inconsistent with the United States' obligations under the General Agreement. Venezuela and Brazil argued that the 1994 Proposal would have partly eliminated the discrimination by providing for the establishment of individual baselines by foreign refiners of reformulated gasoline; however, the discriminatory treatment of conventional gasoline would have continued.

3.14 Venezuela noted that "Petroleos de Venezuela, S.A." ("PDVSA") had already made costly adjustments to its production in order to meet the statutory baseline requirements and had accelerated its programme of investments with a view to complying with the Complex Model requirements. These adjustments had reduced the volume and value of Venezuela's current and anticipated gasoline exports to the United States below the levels that would have prevailed if PDVSA were allowed to establish its individual baseline. These adjustments interfered with PDVSA's investment programme, obliging it to focus on production for the US gasoline market and adversely affecting other important investment projects.

3.15 Brazil stated in addition that application of the statutory baseline to foreign refiners and domestic importers was discriminatory in several respects. First, the flexibility given to domestic refiners in establishing individual baselines had the effect that many of them were allowed emissions levels higher than those permitted by the statutory baseline. Secondly, the statutory baseline was more stringent than the average of the individual baselines for refineries located in the Eastern and Gulf Coast states (where virtually all Brazilian gasoline was sold) because of the inclusion in the national average of the strict 1990 Californian standards. The Gasoline Rule also favoured imports by domestic refiners over imports by importers who were not domestic refiners. Domestic refiners whose current production was "cleaner" than their individual baseline could import gasoline with parameter levels above the statutory baseline, could blend it with their own cleaner production and sell it on the US market as long as the mixture conformed with their individual baseline. Importers who were not domestic refiners had to conform to the statutory baseline in all instances. Thus, the Gasoline Rule affected the distribution of gasoline in the United States by channelling imports to domestic refiners who had an incentive to take advantage of their privileged position by demanding lower prices from foreign refiners.

3.16 Brazil stated that the same gasoline that it used to export to the United States market as "finished" gasoline was, since the entry into force of the Gasoline Rule, considered only as "blendstock[8]", which was sold at a lower price. Thus, Brazil had not been able to export "finished" conventional gasoline to the US market since 1 January 1995. Brazilian refiners were not currently producing reformulated gasoline .

3.17 The United States replied that the Gasoline Rule did not treat imported gasoline less favourably than domestic gasoline overall. The environmental goal of the Gasoline Rule was to regulate the overall quality of the gasoline sold in the United States. Each importer had to satisfy on average the statutory baseline, which approximated average gasoline quality consumed in the US in 1990, and domestic refiners had to satisfy on average their 1990 individual baselines, which overall roughly represented 1990 US gasoline quality. Hence, overall domestically produced gasoline had to be at least as clean as foreign gasoline since roughly half of domestic gasoline would be "cleaner" and roughly half would be dirtier than gasoline using the statutory baseline. The United States supplied the Panel with data documenting the number of domestic refiners with baseline values both above and below the statutory baseline for specific parameters and emissions levels upon which compliance with the non-degradation requirements was based. This analysis

[8]Blendstock is unfinished gasoline which has to be blended in

showed that five domestic refineries had individual baselines that were below the annual statutory baseline for all fuel parameters and emissions levels, and three domestic refiners had individual baselines that were above the annual statutory baseline for all fuel parameters and emissions levels. Thus, most refiners had individual baselines with several parameters above the corresponding statutory values and several below. The United States considered that a previous panel report had recognized that "there may be cases where application of formally identical legal provisions would in practice accord less favourable treatment to imported products and a contracting party might thus have to apply different legal provisions to imported products to ensure that the treatment accorded them is in fact no less favourable"[9]. Since the majority of importers did not have the necessary data to use Methods 1, 2, or 3, they would be precluded from supplying the US market as they

gasoline and domestically produced gasoline were in the same position with regard to the flexibility for complying with their respective baselines. As various qualities of gasoline were available in the market, some above and some below the statutory baseline, an importer had complete flexibility to select gasoline from different sources and mix them in order to reach the annual average quality required by the statutory baseline. By contrast, a domestic refiner was constrained by its refinery equipment and crude oil supplies.

3.20 The United States considered that Venezuela was incorrect in its claim that the US government official's statement demonstrated that the Gasoline Rule had a protectionist purpose. The statement in question actually reflected the US government's commitment when it issued the final Gasoline Rule to continue addressing the issue of how imports were

The United States wrongly introduced the concept of "similarly situated parties" as a basis for arguing that imported gasoline and US produced gasoline were not "like product". Imported and domestic gasolines had the same tariff classification, served the same end use and the same end users and were indistinguishable from the commercial standpoint; thus, all gasoline was a like product. The concept "similarly situated parties" was new to GATT and lacked a legal basis. Moreover, Venezuela considered that these parties were not "similarly situated". Importers, who obtained finished gasoline for distribution to other wholesalers or retailers were not "similarly situated" to blenders, who produced gasoline by mixing gasoline components produced by others. It was more appropriate to compare them to "jobbers" who obtained finished gasoline for distribution to other wholesalers or retailers and who used the individual baselines associated with the gasoline they acquired. Foreign refiners were "similarly situated parties" with respect to US refiners in that the reasons given by the United States as to why US refiners can establish their own baselines apply equally to foreign refiners.

3.23 Venezuela argued that the United States did not deny the existence of differential treatment for imported gasoline. Thus, it had to assume the burden of proving that such treatment was no less favourable to the imported product. According to past panel reports, the test was not whether the rules were different but whether such differences accorded no less favourable treatment to imported products. Venezuela considered that such a demonstration had not been made. Venezuela disagreed with the interpretation given by the United States to the panel report "United States - Section 337 of the Tariff Act of 1930" and considered that panels interpreted the words "treatment no less favourable" contained in Article III:4 as calling for effective equality of opportunities for imported products. The United States' assertion that it was "incumbent upon the importer to balance the products of one or more foreign refiners with that of another" was contrary to that established understanding of Article III:4. No such equality could exist if the very ability of a producer/exporter to introduce his product into the importer's market depended on the subsequent decisions of the importer to buy additional product produced and exported by another person. The opportunity to import a like product could not be conditional upon the importer's willingness to run a risk of not finding below-statutory baseline gasoline in order to average it with above-statutory baseline gasoline. Venezuela considered that the reasoning of two previous panel reports[10] regarding the loss of competitive opportunities for imported products was applicable to this case and led to the conclusion that imported gasoline should have the same distribution opportunities available to US produced gasoline, including the ability to be sold directly into commerce with the application of an individual baseline.

3.24 Venezuela considered that the issue at stake was not averaging, a technique which was also available to domestic refiners, but the difference between the requirements imposed on imported gasoline and the requirements imposed on US gasoline. In order to regulate the average quality of gasoline in the United States, the Gasoline Rule regulated every batch of gasoline produced in or imported into the US. The fact that the very same gasoline with identical characteristics would be treated differently under the Rule if produced by a US refiner as opposed to a foreign refiner was precisely the "less favourable treatment" prohibited under Article III:4.

3.25 Venezuela rejected the United States' assertion that a foreign refiner that produced gasoline in 1990 with properties of sulphur, olefins and T-90 above the statutory baseline only had to mix "additives such as oxygenates" to upgrade its gasoline; in fact, the very composition of the foreign gasoline had to change. Venezuela denied the United States' claim that Venezuela had rejected the 1994 Proposal. Venezuela had simply explained why some means by which the EPA

[10]"United States - Measures Affecting Alcoholic and Malt Beverages", BISD 39S/206 (adopted on 19 June 1992), and

proposed to achieve certain ends were not workable from a practical standpoint, and presented alternatives to achieve the same ends in a more practical and workable manner.

3.26 Brazil argued that the alleged benefit to imports deriving from the fact that "roughly half" of the domestic gasoline must be "cleaner" than imported gasoline (which, in Brazil's view had not been demonstrated) did not overcome the less favourable treatment accorded to imports deriving from the fact that "roughly half" of the domestic gasoline was permitted to be "dirtier" than imported gasoline. This statement by the United States implicitly admitted the discrimination contained in the Gasoline Rule which required imported gasoline to be cleaner than half of the domestically produced gasoline. Brazil noted that a previous panel report had rejected any notion of balancing more favourable treatment of some imported products against less favourable treatment of other imported products[11]. The same rationale applied to any notion of balancing more favourable treatment vis-à-vis some domestic products against less favourable treatment vis-à-vis other domestic products. Similarly, another panel report[12]

3.29 Brazil agreed with the United States that Article III applied to gasoline and not to the producer of gasoline. In this particular case, the standard applied to gasoline had been determined with reference to the producer of gasoline. Brazil was not questioning this policy choice as such, but the fact that a different and less favourable standard applied to imported products. In the case of Brazil, this discrimination was illustrated by the fact that the gasoline exported by Brazil as "finished" conventional gasoline until 1 January 1995 was now considered as a mere "blendstock" because it did not meet the statutory baseline requirements. Blendstock gasoline commanded a lower price because the buyer had to mix it with "cleaner" gasoline in order to comply with the statutory baseline. In conclusion, Brazil stated that the fact that the product produced by

sensitive to various factors (US demand, exporting country's supply and demand, refinery cost structure, gasoline market conditions in other competing exporting countries, for instance), and that worldwide exports of gasoline to the United States had been following a downward trend over the last five years. It was equally difficult to know the exact role played by the Gasoline Rule with regard to the investment programme of Venezuelan refineries since any refiner operating at the world level needed a significant reformer capacity. Venezuela's investment in such a reformer unit likely reflected overall Venezuelan market strategy. Moreover, whatever production limitations PDVSA might have with respect to one particular refiner, blending of feedstock from several refineries made higher levels of statutory-quality gasoline on a per-shipment basis possible. In addition, the US government had studied refinery cost structure shortly after passage of the Clean Air Act and found that refiners whose production of reformulated gasoline was about 30% or less of their total gasoline production could produce the reformulated gasoline at little or no incremental cost (i.e. investment costs) because of their ability to select among blendstocks.

3.32 The United States argued that, with respect

3.36 Brazil argued that previous disputes[13], to which the United States had been a party, involved a violation of Article III:1.

3. Article XX - General Exceptions

3.37 The United States argued that

certain gasoline qualities would need to change the characteristics of their production to meet the standard for those qualities, and those producers whose gasoline was cleaner than the baseline could degrade down to the baseline. The result would be the same overall average for gasoline, but large segments of gasoline producers would have been required to make changes to their conventional gasoline production. Where future production exceeded their 1990 output, refiners must meet the statutory baseline. With respect to reformulated gasoline, individual baselines were used for a three year transition period and applied to three gasoline qualities -sulphur, olefin and T-90- which were required to preserve their average US 1990 levels because EPA lacked data about their precise emission effects. This approach avoided requiring large segments of producers to make changes in their gasoline in order to meet a single requirement, whereas it was not clear whether and how any such change was needed to avoid emissions increases. However, all reformulated gasoline refiners must have begun to adjust their operations in order to meet the new reformulated gasoline requirements that would be in effect in 1998 under the Complex Model. All regulated gasoline qualities would then be measured against the statutory baseline. Thus, the baseline system protected air quality in the most practical and cost-effective manner, while taking the best account of the various producers' characteristics.

3.41 The United States argued that the individual baseline approach was however not possible with all producers, in particular, refiners that were only producing during part of 1990, blenders and importers. These categories of producers were in a different situation since they lacked the data necessary to use Methods 1, 2 and 3, and requiring them to establish an individual baseline, like domestic refiners, would have had the effect of precluding them from the US market. Thus, assigning importers to the statutory baseline ensured that they would not be forced out of the market while treating similarly situated parties alike. Moreover, even if in some cases importers might be able to establish individual baselines derived from foreign refiner information, giving importers a choice as to which baseline to use would inevitably have undermined the air quality objective of the regulation since business incentives would have induced them to use the cheapest and least stringent option, which would also have been the most polluting one. Taking into account these concerns over gaming, EPA had determined that no other option was feasible without having adverse effects on trade. The United States stressed that the Gasoline Rule applied to the importer and not to the foreign refiner. Given that there had traditionally been a variety of gasoline and blendstock qualities available on the market, importers were likely to have the flexibility to import gasoline from various sources, some with levels above and others below the statutory baseline, as long as the annual average for the importer met the statutory baseline.

3.42 The United States argued that it was not feasible to give individual baselines to foreign refiners for various reasons. First, gasoline was a fungible international commodity and a shipment of gasoline arriving in a US port generally contained a mixture of gasoline that had

Section 337 of the Tariff Act of 1930" had acknowledged that a measure might need to provide apparently less favourable treatment to imports in situations where it "might be considerably more difficult to identify the source of infringing products or to prevent circumvention of orders limited to the products of named persons"[14], than for US products. The present case offered similar differences in enforcement needs and capabilities with respect to the identification of the source of gasoline.

3.43 The United States disagreed with Venezuela's assertion that the May 1994 Proposal demonstrated the feasibility of individual baselines for foreign refiners. This Proposal was a continuation of EPA's efforts to develop criteria that would protect the environment, minimize disruption to producers and treat similarly situated gasoline alike, taking into account the comments and concerns expressed by interested parties. The fact that EPA made this attempt was neither a determination that the Gasoline Rule was flawed nor a determination that the 1994 Proposal was feasible. The 1994 Proposal contained several strict conditions governing the establishment of individual baselines for foreign refiners, which showed that concerns still existed. Moreover, it applied only to reformulated gasoline because the indefinite application of individual baselines for conventional gasoline and the expectation that many more foreign refiners would supply the conventional market indicated that the environmental risk associated with allowing this option were too great to justify even its proposal. In public comments, the 1994 Proposal had been criticised as favouring a small group of importers over all the others. PDVSA and other foreign refiners had objected that the proposed conditions, *inter alia* those related to gasoline tracking, were unworkable. For these reasons, the United States rejected Venezuela's assertion that EPA would have finalized this proposal except for the action by Congress.

3.44 The United States considered that Venezuela's citation of the testimony of a US government official was inappropriate. This testimony reflected the US government's commitment when it issued the final Gasoline Rule to continue addressing the issue of how imports were treated together with the concerns that environmental protection not be compromised and that the provisions be fair to all the parties affected. Contrary to Venezuela's argument, this testimony did not show that protectionism underlay the Gasoline Rule's treatment of imports. The statement of a US government official defending the proposed use of foreign refiner baselines only illustrated that US regulators wished to obtain a mutually satisfactory solution with Venezuela. Moreover, the Rule explici 149.76 460.32 Tm/F17 /F17 11 Tf(Rule) Tj Tf(explici 149.76 460.32 (US)ua) TjETBT1 0 0 1 82.04

3.46 Venezuela considered that, contrary to the US argument, the use of a

emissions from gasoline would vary, depending on which refiners were supplying it, and as a consequence, the emissions levels could exceed the statutory baseline. Moreover, EPA had recently proposed several amendments to the Gasoline Rule, such as provisions permitting upward adjustment in baseline levels because of a US refiner's inability to acquire low sulphur content crude oil that was available in 1990, which equally undermined its environmental objectives. Venezuela concluded that the United States had not met the burden of the proof required by Article XX.

3.48 Brazil did not disagree with the purpose of the United States which was to address the problem of air pollution in order to protect human, animal and plant life and health. However, Brazil considered that the Gasoline Rule programme did not satisfy the requirements of Article XX(b), because the burden of achieving this purpose was placed disproportionately on imported gasoline. All imported gasoline had to meet the 1990 average expressed in the statutory baseline whereas half of the domestic refineries could sell gasoline which did not meet the statutory baseline. The concerns expressed by the United States about the negative impact of imposing a single statutory baseline on domestic refiners could not justify a violation to the national treatment obligation for the following two reasons. First, EPA did not want to impose on domestic refiners whose gasoline was dirtier than the statutory baseline the burden of changing their production characteristics, but it imposed precisely this requirement on foreign refiners. Secondly, the United States had not demonstrated to the Panel why domestic refiners whose production was cleaner than the statutory baseline would downgrade to the baseline. And even assuming that such a downgrade would occur, the overall air quality would not change as long as the refiners with "dirtier" gasoline were required to upgrade to the statutory baseline. Brazil considered that a rule establishing the statutory baseline as a minimum with the additional requirement that those refiners who produced gasoline above the statutory baseline continue to do so was another option which would take care of the downgrading concern while at the same time improving air quality in the United States and eliminating discrimination against imports.

3.49 Brazil further argued that the United States had not explained why importers could not establish an individual baseline, especially using Method 3 since importers presumably maintained records of their imports and thus could have data on their 1990 imports. Even assuming that it was necessary to assign importers to the statutory baseline, this did not explain the failure to provide for individual baselines for foreign refiners. Brazil considered that the United States had not demonstrated that foreign refiners did not have sufficient data to establish their own baselines. In that context, the United States referred only to "difficulties" but, according to Brazil, mere "difficulties" did not create necessity within the meaning of Article XX(b). Moreover, assuming that these difficulties were insurmountable, they would nevertheless not allow the United States to discriminate against foreign gasoline since there was an alternative measure, reasonably available, which was the requirement that all gasoline, domestically produced and imported, meet the same statutory baseline, as Brazil had noted above.

3.50 Brazil considered that the United States had presented no factual basis to support its concern that a foreign refiner would "game" the system if given the choice between the statutory and the individual baseline. Besides, this opportunity for "gaming" could be eliminated by simply assigning all refiners, domestic or foreign, to the same baseline, statutory or individual. Regarding the use of individual baselines by foreign refiners, the United States had never made any attempts to investigate or determine empirically whether the calculation and enforcement of such baselines were possible. However it merely insisted that these problems were insurmountable and, therefore, the statutory baseline had to be applied to imported gasoline. Finally, the fact that numerous parties had objected to particular aspects of the 1994 Proposal did not mean that non-discriminatory baselines for foreign refiners were not possible. Brazil

concluded that the United States had not demonstrated why

3.53 The United States argued that the lack of a volume limitation for the use of individual baselines under the reformulated gasoline programme was not expected to affect the success of that program. US data showed that refineries with the highest olefin and sulphur levels in their baselines (i.e. the dirtiest baselines) as a group had not extended their market share after the start up of the reformulated gasoline programme. This was consistent with EPA's original expectations that the short time period during which individual baselines were used in the reformulated programme would not provide an incentive for refiners to revise their investment and production decisions based on

necessary to enforce. Moreover, for the reasons expressed under Article XX(b), the Gasoline Rule was not necessary. Thus, the United States did not meet the requirements of Article XX(d).

3.57 Brazil considered that, for the reasons it had already developed under Article XX(b), the United States failed to demonstrate that the Gasoline Rule was

had previously demonstrated to the Panel that the Gasoline Rule methodology contained loopholes which undermined its own conservation objectives, thus confirming that the discriminatory baseline system could not be "primarily aimed at" the conservation of an exhaustible natural resource.

3.62 The United States disagreed with the claim that clean air was not an exhaustible natural resource within the meaning of Article XX(g). The United States maintained that air was undoubtedly a natural resource which could be exhausted if it was rendered unfit for human, animal or plant consumption. This was similar to the recognition in previous panel proceedings that fish were an "exhaustible natural resource" since their populations could be depleted or rendered extinct[18].

b) "... made effective in conjunction with restrictions on domestic production or consumption"

3.63 The United States considered that the Gasoline Rule restricted domestic production of gasoline by requiring manufacturers to limit their production of gasoline so that over the course of the year the average of particular components of the gasoline did not exceed certain maximum levels. It also restricted domestic consumption by ensuring that the average of those components of gasoline sold did not exceed certain maximum levels.

3.64 Venezuela rejected this argument because it considered that the United States had not shown that the discriminatory baseline requirements were "primarily aimed at rendering effective" restrictions on domestic production or consumption of clean air, the "natural resource" to be conserved by the Gasoline Rule. The United States had only referred to restriction on domestic production and consumption of gasoline.

3.65 Brazil argued that, even assuming that clean air was an exhaustible natural resource, the Gasoline Rule did not restrict domestic production or consumption of clean air. At best, the Gasoline Rule sought to increase production if not consumption of clean air, not to restrict it. Moreover, neither the CAA nor the Gasoline Rule restricted in any way the quantity of gasoline that could be produced or consumed in the United States, but merely regulated its quality. Since neither the production nor the consumption of air or gasoline was restricted by the CAA or the Gasoline Rule, the Gasoline Rule did not fall under Article XX(g).

3.66 The United States argued that the Gasoline rule did restrict domestic consumption of clean air through its restriction of emissions that polluted the air. This was similar to restrictions applied on cars in order to conserve fuel. In this case, the Gasoline Rule's application to imports - including the baseline rules- was primarily aimed at rendering effective restrictions on domestic production of dirty air, or conversely the consumption of clean air, through regulation of the gasoline that caused air pollution.

7. Preamble to Article XX

3.67 The United States argued that, as it had demonstrated in the discussion concerning Article III, the Gasoline Rule applied equally to similarly situated parties. Importers and blenders were required to meet the parameters of 1990 average US gasoline because they could not ascertain the refinery of origin and the quality of the gasoline they marketed in 1990. This avoided the alternatives of either "gaming" problems or excluding most imported gasoline from

[18] "Canada - Measures Affecting Exports of Unprocessed Herring and Salmon", BISD 35S/98 (adopted on 22 March 1988) and "United States - Prohibition of Imports of Tuna and Tuna Products from Canada, BISD 29S/91 (adopted on 22 February 1982).

the market. Unlike domestic refiners, importers had the flexibility to rely on a variety of sources so as to meet an annual average quality of gasoline. Moreover, for each of the requirements, about half of US gasoline produced by domestic refiners had to be cleaner in certain respects than the annual average gasoline quality supplied by importers. In addition, a portion of the US gasoline market was being supplied with gasoline by domestic refiners which had to meet the statutory baseline because their gasoline could not be presumed to have been part of the gasoline pool in 1990. But to the extent that the enforcement conditions differed between the United States and other countries, the "same conditions" did not prevail in the United States and in other supplying countries. Accordingly, any differences

[redacted]

8. Article XXIII - Nullification and Impai

3.71 Venezuela argued that, in addi[redacted] an alternative claim of nullification and impairment under XXI[redacted] baseline requirements had resulted in shipments of [redacted] barrels of Venezuelan gasoline to the United States per da[redacted] discrimination. The price of Venezuelan gasoline and its share [redacted] investment programme for Venezuelan refineries, had also been [redacted] was aware that statistical evidence of adverse trade effects [redacted] nullification or impairment under Article XXIII:1(b) [redacted] by so affecting trade volumes, prices received for Venezuelan g[redacted] US market and PDVSA's investment programme, the Gasoline Rule had distorted the conditions of competition for trade in the United States compared to the conditions reasonably expected by Venezuela under the General Agreement. Venezuela said that if the ment

that

TBT Agreement since any averaging techniques required examination of the properties of each individual gasoline shipment. Excluding from the coverage of the TBT Agreement regulations relying on averaging would open a gaping loophole. Under this interpretation, the obligation of the Agreement could be avoided by averaging. Venezuela considered that the United States wanted to avoid examination under the TBT Agreement in order to escape the requirements contained in Article 2.2.

3.76 Brazil objected to the United States' argument that the Gasoline Rule was not a technical regulation within the meaning of the TBT Agreement. Brazil considered that the language of the CAA and that of the Gasoline Rule, referred to the establishment of product standards for gasoline when determining the fuel properties for the statutory baseline and the individual baselines. These product standards applied to gasoline were mandatory. The fact, argued by the United States, that no particular shipment of gasoline needed to meet any precise standards since the requirements were measured on an annual average basis, and thus that the "product" was the annual quantity of gasoline produced, blended, or imported, rather than each sub-unit, was irrelevant. Annual production in this case was simply the unit of production to which the standard was applied. Brazil noted that if the United States were correct in its assertion that the individual baselines applied to refiners and not to gasoline, the discrimination would then be even more apparent because foreign refiners had no baseline. In this case a mandatory requirement would apply only to imported gasoline while, under the logic of the United States, no requirement would apply to domestic gasoline, as distinct from domestic refiners. However, the enforcement and surveillance system provided for by EPA in the Gasoline Rule in order to regularly check the quality of gasoline and its property at the refinery level argued in favour of a technical regulation setting forth product characteristics. Moreover, the United States' own statements to the Panel acknowledged this fact when declaring that the "requirements" of the Gasoline Rule were "necessary to protect human, animal and plant life or health". In conclusion, Brazil considered that a rule which obliged imported gasoline that did not meet the statutory baseline to be blended with gasoline that exceeded these requirements in order to meet the mandatory statutory requirements was a "document" with mandatory product characteristics.

3.77 The United States argued that the TBT Agreement had been designed to elaborate on the disciplines of Article III of the General Agreement for a very specific subset of measures (technical regulations, standards and conformity assessment procedures). The fact that a measure was in writing, mandatory and applied to products did not make it a technical regulation. Excise taxes, for instance, met all these criteria but were not "technical regulations". Similarly, the term "technical regulation" was not so broad as to cover all government regulatory actions affecting products. For example, government regulations requiring factory smokestacks to have devices to reduce emissions were not technical regulations, though they were in writing, mandatory and specified "characteristics". Contrary to what was argued by the complainants, there were no minimum or maximum content or emissions requirements applied with respect to the non-degradation requirements for individual shipments of either reformulated or conventional gasoline under the Simple Model. A shipment or even sale of gasoline was not required to meet specific product characteristics with respect to the non-degradation requirements at issue. The Gasoline Rule was not setting uniform criteria in terms of gasoline characteristics; standardization was neither the purpose nor the result of the regulation. The United States concluded that the complainants were interpreting the term "technical regulation" out of context and such an interpretation, if accepted, would introduce into the TBT Agreement many measures which were in fact not intended to be covered. The United States also argued that Brazil's view that a "product" in this case be defined as an entire year's production, rather than a shipment or a batch, would be a radical departure from the concept of "product" under the WTO and was without basis in the WTO.

b)

objectives would be unacceptable. In that regard, Venezuela recalled that EPA itself had acknowledged that the environmental impact of gaming was speculative because it lacked "clear evidence" regarding the actual average quality of 1990 imported gasoline and did not know whether a significant amount of imported gasoline was "cleaner" than the statutory baseline. Moreover, so little gasoline was imported that the potential differential emissions -between individual and statutory baselines- would not have any significant impact on the average emission quality of the gasoline consumed in the United States.

3.83 Brazil stated that, for the reasons already expressed under arguments relating to Articles I and III of the General Agreement and Article 2.1 of the TBT Agreement, the Gasoline Rule created "unnecessary obstacles to international trade" in a manner contrary to Article 2.2 of the TBT Agreement.

2. Article 12 - Special and Differential Treatment of Developing Country Members

3.84 Venezuela observed that Article 12 of the TBT Agreement imposed certain obligations on the United States with respect to developing countries. Venezuela did not seek any special treatment but merely wanted its gasoline to be held to the same baseline requirements as US gasoline. Venezuela stated that it was not asking for the Panel to rule under Article 12 but intended to point out that the discriminatory treatment affecting Venezuelan gasoline was particularly objectionable in the light of that provision.

IV. SUBMISSIONS BY INTERESTED THIRD PARTIES

A. The European Communities

4.1 The European Communities (the "EC") stated that, as an exporter to the United States of gasoline for automobiles and other fuel oils, it had a substantial interest in the matter before the Panel. In 1994, the total volume of EC-12 exports to the United States for gasoline represented 6'423'411 metric tonnes. This volume had increased since the enlargement of the EC, on

The EC did not want to discuss the accuracy of the arguments developed by the United States with respect to the feasibility of individual baselines for foreign refiners, but assumed, for the sake of argument, that Methods 2 and 3 could not be applied to imported gasoline in this case. Considering the explanations given by the United States as to what the statutory baseline represented, and assuming they were correct, the EC failed to see why US refiners could not be subject to the statutory baseline, like importers and blenders. Such a measure would have been in total conformity with Article III, paragraphs 1 and 4. In addition, it appeared from

4.6 As to whether the Gasoline Rule fell under the TBT Agreement, the EC stated that it agreed with the United States that the requirements on chemical ingredients did not need to be satisfied by each shipment and also that, the measures at issue being based on a yearly average, the importers remained free to import different varieties of gasoline provided that the annual average met the requirements. However, the EC doubted that a standard should be excluded from the scope of the TBT Agreement only for the reason that it required compliance on a yearly basis instead of on a shipment basis. It was clear that the importer had only to balance various qualities of gasoline in order to meet the statutory baseline. From the point of view of the exporting country, the Gasoline Rule created a clear incentive for adapting its production standards if it wanted to maintain or increase its share of the US market. Exporting refiners not adapting their production standards to US requirements (or at least not gradually narrowing the difference down to total compliance) would be unlikely to increase their sales in the US since importers had to blend or balance the "dirty" imported gasoline with

environmental objectives, it introduced a disguised restriction on

5.4 In respect of the interim report's discussion of Article XX(d), the United States objected to the Panel's use of specific terms which did not appear in the text of the provision. The Panel accepted the US arguments and paragraph 6.31 of the revised findings reflects the Panel's response.

5.5 In respect of the interim report's discussion of Article XX(g), the United States objected to the Panel's use of specific terms which did not appear in the text of the provision, and the analysis of alternative measures available to the United States. Venezuela requested a change to the description of its argument under this provision. The Panel revised the report where it accepted the arguments of the US and Venezuela and paragraphs 6.35 - 6.36 and 6.40 - 6.41 of the findings reflect the Panel's response.

5.6 In respect of the interim report's descriptive section, Venezuela and the United States suggested further changes which the Panel took into account in re-examining that part of the report. The Panel revised the descriptive section of the report where it accepted the need for these changes.

VI. FINDINGS

A. Introduction

6.1 The Panel noted that the dispute arose from the following facts. The Clean Air Act aims to control and reduce air pollution in the United States. The Act and certain of its regulations (the "Gasoline Rule") set standards for gasoline quality intended to reduce air pollution, including ozone, caused by motor vehicle emissions. From 1 January 1995, the Gasoline Rule permits only gasoline of a specified cleanliness ("reformulated gasoline") to be sold in areas of high air pollution. In other areas, only gasoline no dirtier than that sold in the base year of 1990 ("

no

Gasoline Rule's non-degradation requirements, and not reformulated and conventional gasoline as such, the Panel will refer generally to

interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose".[25]

6.8 The Panel proceeded to examine this issue in the light of the ordinary meaning of the term "like". It noted that the word can mean "similar", or "identical". The Panel then examined the practice of the CONTRACTING PARTIES under the General Agreement. This practice was relevant since Article 31 of the *Vienna Convention* directs that "subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation" is also to be considered in the interpretation of a treaty. The Panel noted that various criteria for the determination of like products under Article III had previously been applied by panels. These were summarized in the 1970 *Working Party Report on Border Tax*

gasoline which was chemically-identical to a batch of domestic gasoline that met its refiner's individual baseline, but not the statutory baseline levels. In this case, sale of the imported batch of gasoline on the first day of an annual period would require the importer over the rest of the period to sell on the whole cleaner gasoline in order to remain in conformity with the Gasoline Rule. On the other hand, sale of the chemically-identical batch of domestic gasoline on the first day of an annual period would not require a domestic refiner to sell on the whole cleaner gasoline over the period in order to remain in conformity with the Gasoline Rule. The Panel also noted that this less favourable treatment of imported gasoline induced the gasoline importer, in the case of a batch of imported gasoline not meeting the statutory baseline, to import that batch at a lower price. This reflected the fact that the importer would have to make cost and price allowances because of its need to import other gasoline with which the batch could be averaged so as to meet the statutory baseline. Moreover, the Panel recalled an earlier panel report which stated that "the words 'treatment no less favourable' in paragraph 4 call for effective equality of opportunities for imported products in respect of laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products."[28] The Panel found therefore that since, under the baseline establishment methods, imported gasoline was effectively prevented from benefitting from as favourable sales conditions as were afforded domestic gasoline by an individual baseline tied to the producer of a product, imported gasoline was treated less favourably than domestic gasoline.

6.11 The Panel then examined the US argument that the requirements of Article III:4 are met because imported gasoline is treated similarly to gasoline from *similarly situated* domestic parties — domestic refiners with limited 1990 operations and blenders. According to the United States, the difference in treatment between imported and domestic gasoline was justified because importers, like domestic refiners with limited 1990 operations and blenders, could not reliably establish their 1990 gasoline quality, lacked consistent sources and quality of gasoline, or had the flexibility to meet a statutory baseline since they were not constrained by refinery equipment and crude supplies. The Panel observed that the distinction in the Gasoline Rule between refiners on the one hand, and importers and blenders on the other, which affected the treatment of imported gasoline with respect to domestic gasoline, was related to certain differences in the characteristics of refiners, blenders and importers, and the nature of the data held bBT1 0 0 1 127.92 356.0 1 381.12 356.64 Tm/F

6.13 The Panel considered that the foregoing was sufficient to dispose of the US argument. It noted, however, that even if the US approach

100 US refiners, representing 98.5 percent of gasoline produced in 1990, had received EPA approval of their individual baselines. Only three of the refiners met the statutory baseline for all parameters. Thus, while 97 percent of US refiners did not and were not required to meet the statutory baseline, the statutory baseline was required of importers of gasoline, except in the rare case (according to the parties) that they could

prospect

policy within the range of those concerning the protection of human, animal and plant life or health mentioned in Article XX(b).

2. Necessity of the inconsistent measures

6.22 The Panel recalled its finding in paragraph 6.16 that imported gasoline was treated less favourably than domestic gasoline, since, under the baseline establishment methods, imported gasoline was prevented from benefitting from as favourable sales conditions as were afforded domestic gasoline by an individual baseline tied to the producer of a product. The Panel then proceeded to examine whether the aspect of the Gasoline Rule found inconsistent with the General Agreement was necessary to achieve the stated policy objectives under Article XX(b). The Panel noted that it was not the necessity of the policy goal that was to be examined, but whether or not it was necessary that imported gasoline be effectively prevented from benefitting from as favourable sales conditions as were afforded by an individual baseline tied to the producer of a product. It was the task of the Panel to address whether these inconsistent measures were necessary to achieve the policy goal under Article XX(b). It was therefore not the task of the Panel to examine the necessity of the environmental objectives of the Gasoline Rule, or of parts of the Rule that the Panel did not specifically find to be inconsistent with the General Agreement.

6.23 The Panel then turned to the arguments of the parties relating to that aspect of the Gasoline Rule found inconsistent with the General Agreement. The United States argued that not all entities dealing in gasoline could be assigned an individual baseline and, of those who could be assigned such a baseline, not all could use the same types of secondary or tertiary evidence (Methods 2 and 3) to establish it. Certain entities including importers, blenders and refiners which did not have continuous 1990 operations, were simply not in a position to furnish this secondary or tertiary evidence. Venezuela and Brazil argued on the other hand that foreign refiners should be accorded their own individual baselines under the Gasoline Rule using the same types of evidence, as easily available to them as to domestic refiners. Alternatively, they argued that importers should be able to use individual 1990 baselines established for the

> party is bound to use, among the measures reasonably available to it, that which entails the least degree of inconsistency with other GATT provisions.[34]

The same reasoning had been adopted by the 1990 *Thai Cigarette* panel in examining a measure under Article XX(b). That panel saw no reason not to adopt the same interpretation of "necessity" under Article XX(b)

the extent that it did not distinguish between imported gasoline on the basis of its country of origin, would not necessarily contravene Article I or other provisions of the General Agreement, and that the United States, notwithstanding suggestions that certain importers might have equitable concerns, had not established the contrary.

6.26 The Panel noted the claims of the United States that allowing importers or foreign refiners to use individual baselines in such a way was not feasible for the reasons listed in paragraph 6.23. The Panel was not convinced that the United States had satisfied its burden of proving that those reasons precluded the effective use of individual baselines in a manner which would allow imported products to obtain treatment that was consistent, or less inconsistent, with obligations under Article III:4. First, while the Panel agreed that it would be necessary under such a system to ascertain the origin of gasoline, the Panel could not conclude that the United States had shown that this could not be achieved by other measures reasonably available to it and consistent or less inconsistent with the General Agreement. Indeed, the Panel noted that a determination of origin would often be feasible. The Panel examined, for instance, the case of a direct shipment to the United States. It considered that there was no reason to believe that, given the usual measures available in international trade for determination of origin and tracking of goods (including documentary evidence and third party verification) there was any particular difficulty sufficient to warrant the demands of the baseline establishment methods applied by the United States.

6.27 Second, the Panel did not agree that the United States had met its burden of showing that the "gaming" concern was an adequate justification for maintaining the inconsistency with Article III:4 resulting from the baseline establishment methods. It was uncertain if, or to what extent, gaming would actually occur, especially given the small market share of imported gasoline (approximately 3 percent). Moreover, the Panel noted that the Gasoline Rule did not guarantee in its regulation of US entities that gasoline characteristics subject to non-degradation requirements (i.e. those regulated by baselines), would remain at the 1990 average levels. For example, there was no volume cap on the production of reformulated gasoline by individual refineries, which meant that if producers of relatively dirtier gasoline expanded their relative share of production of reformulated gasoline, the national average level of pollutants subject to the non-degradation requirements would be greater than in 1990. Similarly, within the 1990 volume limitations, if the output of producers of relatively cleaner gasoline fell below 1990 levels, while output of others did not, national average levels of pollutants would be worse. Moreover, specific provisions of the Gasoline Rule permitted some refiners to produce dirtier gasoline than they produced in 1990 (e.g., certain producers of JP-4 jet fuel) and permitted others to request specific derogation from the Rule. The Panel stressed that it was not finding that such events would occur, only that they could under the Rule. Given that the Gasoline Rule did not therefore guarantee that gasoline characteristics subject to non-degradation requirements would remain at 1990 levels, the Panel considered that it was not consistent for the United States to

2. Measures "related to" the conservation of an exhaustible natural resource; and made effective "in conjunction" with restrictions on domestic production or consumption

6.38 The Panel proceeded to examine whether the baseline establishment methods

natural resources. The Panel saw no direct connection between less favourable treatment of imported gasoline that was chemically identical to domestic gasoline, and the US objective of improving air quality in the United States. Indeed, in the view of the Panel, being consistent with the obligation to provide no less favourable treatment would not prevent the attainment of the desired level of conservation of natural resources under the Gasoline Rule. Accordingly, it could not be said that the baseline establishment methods that afforded less favourable treatment to imported gasoline were primarily aimed at the conservation of natural resources. In the Panel's view, the above-noted lack of connection was underscored by the fact that affording treatment of imported gasoline consistent with its Article III:4 obligations would not in any way hinder the United States in its pursuit of its conservation policies under the Gasoline Rule. Indeed, the United States remained free to regulate in order to obtain whatever air quality it wished. The Panel therefore concluded that the less favourable baseline establishments methods at issue in this case were not primarily aimed at the conservation of natural resources.

6.41 With respect to whether the baseline establishment methods could be said to be primarily aimed at "rendering effective restrictions on domestic production or consumption", the Panel noted that it had not determined that the measures at issue were “restrictions”, and whether they were “on” domestic production or consumption. However, in light of its finding in paragraph 6.40, the Panel did not proceed to determine this issue or whether the measure met the conditions in the introductory clause of Article XX.

G. Article XXIII:1(b)

6.42 The Panel then noted the claim by Venezuela under Article XXIII:1(b) that benefits accruing to it under the General Agreement had

VIII. CONCLUSIONS

8.1 In the light of the findings above, the Panel concluded that the baseline establishment methods contained in Part 80 of Title 40 of the Code of Federa(of) TjETBT1 0 01 0 0 1 109.68 745.68 Tmo2028g7