

**WORLD TRADE
ORGANIZATION**

WT/DS302/AB/R
25 April 2005

(05-1669)

Original: English

**DOMINICAN REPUBLIC – MEASURES AFFECTING THE IMPORTATION
AND INTERNAL SALE OF CIGARETTES**

AB-2005-3

Report of the Appellate Body

I.	Introduction.....	1
II.	Arguments of the Participants and the Third Participants	3
	A. <i>Claims of Error by the Dominican Republic – Appellant</i>	3
	1. The Necessity Analysis under Article XX(d) of the GATT 1994 in Relation to the Tax Stamp Requirement.....	3
	2. Completing the Analysis under Article XX of the GATT 1994	6
	3. The Conformity of the Panel's Examination of Exhibits DR-8 and DR- 29 with Article 11 of the DSU	7
	B. <i>Arguments of Honduras – Appellee</i>	8
	1. The Necessity Analysis under Article XX(d) of the GATT 1994 in Relation to the Tax Stamp Requirement.....	8
	2. Completing the Analysis under Article XX of the GATT 1994	10
	3. The Conformity of the Examination of Exhibits DR-8 and DR-29 with Article 11 of the DSU	11
	C. <i>Claims of Error by Honduras – Appellant</i>	12
	1. Article III:4 of the GATT 1994 and the Bond Requirement.....	12
	2. Article XX(d) of the GATT 1994 and the Bond Requirement	13
	3. Article 11 of the DSU and the Panel's Consideration of the Bond Requirement "As Such"	13
	4. The Timing of Payment of the Selective Consumption Tax and the Panel's Terms of Reference.....	14
	D. <i>Arguments of the Dominican Republic – Appellee</i>	14
	1. Article III:4 of the GATT 1994 and the Bond Requirement.....	14
	2. Article XX(d) of the GATT 1994 and the Bond Requirement	15
	3. Article 11 of the DSU and the Panel's Consideration of the Bond Requirement "As Such"	16
	4. The Timing of Payment of the Selective Consumption Tax and the Panel's Terms of Reference.....	17
	E. <i>Arguments of the Third Participants</i>	18
	1. China.....	18
	2. European Communities.....	19
	3. United States	20
III.	Issues Raised in this Appeal	21
IV.	The Necessity Analysis under Article XX(d) of the GATT 1994 in relation to the Tax Stamp Requirement.....	22
V.	The Conformity of the Examination of Exhibits DR-8 and DR-29 with Article 11 of the DSU	29
VI.	Article III:4 of the GATT 1994 and the Bond Requirement.....	34

VII.	Article 11 of the DSU and the Panel's Consideration of the Bond Requirement "As Such"	40
VIII.	The Panel's Treatment of Honduras' Contentions Regarding the Timing of Payment of the Selective Consumption Tax	46
IX.	Findings and Conclusions	50
Annex 1	Notification of an Appeal by the Dominican Republic under Article 16.4 and Article 17 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), and under Rule 20(1) of the <i>Working Procedures for Appellate Review</i>	
Annex 2	Notification of an Other Appeal by Honduras under Article 16.4 and Article 17 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), and under Rule 23(1) of the <i>Working Procedures for Appellate Review</i>	

TABLE OF CASES CITED IN THIS REPORT

Short Title	Full Case Title and Citation
<i>Australia – Salmon</i>	Appellate Body Report, <i>Australia – Measures Affecting Importation of Salmon</i> , WT/DS18/AB/R, adopted 6 November 1998, DSR 1998:VIII, 3327
<i>Canada – Autos</i>	Appellate Body Report, <i>Canada – Certain Measures Affecting the Automotive Industry</i> , WT/DS139/AB/R, WT/DS142/AB/R, adopted 19 June 2000, DSR 2000:VI, 2985
<i>Canada – Periodicals</i>	Appellate Body Report, <i>Canada – Certain Measures Concerning Periodicals</i> , WT/DS31/AB/R, adopted 30 July 1997, DSR 1997:I, 449
<i>Canada – Pharmaceutical Patents</i>	Panel Report, <i>Canada – Patent Protection of Pharmaceutical Products</i> , WT/DS114/R, adopted 7 April 2000, DSR 2000:V, 2289
<i>Canada – Wheat Exports and Grain Imports</i>	Appellate Body Report, <i>Canada – Measures Relating to Exports of Wheat and Treatment of Imported Grain</i> , WT/DS276/AB/R, adopted 27 September 2004
<i>Chile – Alcoholic Beverages</i>	Appellate Body Report, <i>Chile – Taxes on Alcoholic Beverages</i> , WT/DS87/AB/R, WT/DS110/AB/R, adopted 12 January 2000, DSR 2000:I, 281
<i>Chile – Price Band System</i>	Appellate Body Report, <i>Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products</i> , WT/DS207/AB/R, adopted 23 October 2002
<i>Dominican Republic – Import and Sale of Cigarettes</i>	Panel Report, <i>Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes</i> , WT/DS302/R, 26 November 2004
<i>EC – Asbestos</i>	Appellate Body Report, <i>European Communities – Measures Affecting Asbestos and Asbestos-Containing Products</i> , WT/DS135/AB/R, adopted 5 April 2001, DSR 2001:VII, 3243
<i>EC – Bananas III</i>	Appellate Body Report, <i>European Communities – Regime for the Importation, Sale and Distribution of Bananas</i> , WT/DS27/AB/R, adopted 25 September 1997, DSR 1997:II, 591
<i>EC – Bananas III (Article 21.5 – Ecuador)</i>	Panel Report, <i>European Communities – Regime for the Importation, Sale and Distribution of Bananas – Recourse to Article 21.5 of the DSU by Ecuador</i> , WT/DS27/RW/ECU, adopted 6 May 1999, DSR 1999:II, 803
<i>EC – Bed Linen (Article 21.5 – India)</i>	Appellate Body Report, <i>European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India – Recourse to Article 21.5 of the DSU by India</i> , WT/DS141/AB/RW, adopted 24 April 2003
<i>EC – Hormones</i>	Appellate Body Report, <i>EC Measures Concerning Meat and Meat Products (Hormones)</i> , WT/DS26/AB/R, WT/DS48/AB/R, adopted 13 February 1998, DSR 1998:I, 135
<i>EC – Poultry</i>	Appellate Body Report, <i>European Communities – Measures Affecting the Importation of Certain Poultry Products</i> , WT/DS69/AB/R, adopted 23 July 1998, DSR 1998:V, 2031
<i>EC – Sardines</i>	Appellate Body Report, <i>European Communities – Trade Description of Sardines</i> , WT/DS231/AB/R, adopted 23 October 2002
<i>EC – Tube or Pipe Fittings</i>	Appellate Body Report, <i>European Communities – Anti-Dumping Duties on Malleable Cast Iron Tube or Pipe Fittings from Brazil</i> , WT/DS219/AB/R, adopted 18 August 2003
<i>Guatemala – Cement I</i>	Appellate Body Report, <i>Guatemala – Anti-Dumping Investigation Regarding Portland Cement from Mexico</i> , WT/DS60/AB/R, adopted 25 November 1998, DSR 1998:IX, 3767

Short Title	Full Case Title and Citation
<i>India – Patents (US)</i>	Appellate Body Report, <i>India – Patent Protection for Pharmaceutical and Agricultural Chemical Products</i> , WT/DS50/AB/R, adopted 16 January 1998, DSR 1998:I, 9
<i>India – Patents (US)</i>	Panel Report, <i>India – Patent Protection for Pharmaceutical and Agricultural Chemical Products, Complaint by the United States</i> , WT/DS50/R, adopted 16 January 1998, as modified by the Appellate Body Report, WT/DS50/AB/R, DSR 1998:I, 41
<i>Japan – Agricultural Products II</i>	Appellate Body Report, <i>Japan – Measures Affecting Agricultural Products</i> , WT/DS76/AB/R, adopted 19 March 1999, DSR 1999:I, 277
<i>Japan – Film</i>	Panel Report, <i>Japan – Measures Affecting Consumer Photographic Film and Paper</i> , WT/DS44/R, adopted 22 April 1998, DSR 1998:IV, 1179
<i>Korea – Alcoholic Beverages</i>	Appellate Body Report, <i>Korea – Taxes on Alcoholic Beverages</i> , WT/DS75/AB/R, WT/DS84/AB/R, adopted 17 February 1999, DSR 1999:I, 3
<i>Korea – Dairy</i>	Appellate Body Report, <i>Korea – Definitive Safeguard Measure on Imports of Certain Dairy Products</i> , WT/DS98/AB/R, adopted 12 January 2000, DSR 2000:I, 3
<i>Korea – Various Measures on Beef</i>	Appellate Body Report, <i>Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef</i> , WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, DSR 2001:I, 5
<i>US – 1916 Act</i>	Appellate Body Report, <i>United States – Anti-Dumping Act of 1916</i> , WT/DS136/AB/R, WT/DS162/AB/R, adopted 26 September 2000, DSR 2000:X, 4793
<i>US – Carbon Steel</i>	Appellate Body Report, <i>United States – Countervailing Duties on Certain Corrosion-Resistant Carbon Steel Flat Products from Germany</i> , WT/DS213/AB/R and Corr.1, adopted 19 December 2002
<i>US – Corrosion-Resistant Steel Sunset Review</i>	Appellate Body Report, <i>United States – Sunset Review of Anti-Dumping Duties on Corrosion-Resistant Carbon Steel Flat Products from Japan</i> , WT/DS244/AB/R, adopted 9 January 2004
<i>US – Hot-Rolled Steel</i>	Appellate Body Report, <i>United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan</i> , WT/DS184/AB/R, adopted 23 August 2001, DSR 2001:X, 4697
<i>US – Gambling</i>	Appellate Body Report, <i>United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services</i> , WT/DS285/AB/R, 7 April 2005
<i>US – Gasoline</i>	Appellate Body Report, <i>United States – Standards for Reformulated and Conventional Gasoline</i> , WT/DS2/AB/R, adopted 20 May 1996, DSR 1996:I, 3
<i>US – Section 301 Trade Act</i>	Panel Report, <i>United States – Sections 301-310 of the Trade Act of 1974</i> , WT/DS152/R, adopted 27 January 2000, DSR 2000:II, 815
<i>US – Section 337</i>	GATT Panel Report, <i>United States Section 337 of the Tariff Act of 1930</i> , adopted 7 November 1989, BISD 36S/345
<i>US – Wheat Gluten</i>	Appellate Body Report, <i>United States – Definitive Safeguard Measures on Imports of Wheat Gluten from the European Communities</i> , WT/DS166/AB/R, adopted 19 January 2001, DSR 2001:II, 717
<i>US – Wool Shirts and Blouses</i>	Appellate Body Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/AB/R and Corr.1, adopted 23 May 1997, DSR 1997:I, 323

WORLD TRADE ORGANIZATION
APPELLATE BODY

**Dominican Republic – Measures Affecting
the Importation and Internal Sale of
Cigarettes**

Dominican Republic, *Appellant/Appellee*
Honduras, *Appellant/Appellee*

China, *Third Participant*
El Salvador, *Third Participant*
European Communities, *Third Participant*
Guatemala, *Third Participant*
United States, *Third Participant*

AB-2005-3

Present:

Baptista, Presiding Member
Lockhart, Member
Sacerdoti, Member

I. Introduction

1. The Dominican Republic and Honduras each appeals certain issues of law and legal interpretations developed in the Panel Report, *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes* (the "Panel Report").¹ The Panel was established on 9 January 2004 to consider claims by Honduras in respect of five measures taken by the Dominican Republic in connection with the importation and internal sale of cigarettes. Honduras made claims in respect of these measures under various provisions of Articles II, III, X, and XI of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994"). The Dominican Republic requested the Panel to dismiss all of Honduras' claims, and also submitted that certain of the Dominican Republic's measures could be justified under the terms of Articles XX(d) and XV:9(a) of the GATT 1994.

2. The Panel Report was circulated to Members of the World Trade Organization (the "WTO") on 26 November 2004. The Panel found that: the imposition by the Dominican Republic of a two percent transitional surcharge for economic stabilization is an "other duty or charge" that is inconsistent with Article II:1(b) of the GATT 1994²; the imposition by the Dominican Republic of a foreign exchange fee constitutes an "other duty or charge" that is inconsistent with Article II:1(b) of the GATT 1994 and that cannot be justified as an exchange restriction within the meaning of

¹WT/DS302/R, 26 November 2004.

²Panel Report, para. 8.1(b).

Article XV:9(a) of the GATT 1994³; and, that the requirement of the Dominican Republic that a tax stamp be affixed to all cigarette packets in its territory and under the supervision of the local tax authorities is inconsistent with Article III:4 of the GATT 1994, which cannot be justified under Article XX(d) of the GATT 1994. The Panel recommended that the Dispute Settlement Body (the "DSB") request the Dominican Republic to bring these measures into conformity with its obligations under the GATT 1994.⁴

3. The Panel made additional findings of inconsistency with respect to certain rules and administrative practices used by the Dominican Republic to determine the tax base for the purpose of applying the Selective Consumption Tax, which were no longer in force at the time of the Panel Report.⁵ The Panel, however, declined to make any recommendations to the DSB regarding these measures as they were no longer in force.⁶

4. The Panel found that Honduras had failed to establish that the requirement by the Dominican Republic that importers and domestic producers post a bond of five million pesos (RD\$5 million) is inconsistent with Article XI:1 or, alternatively, with Article III:4, of the GATT 1994.⁷

5. On 24 January 2004, the Dominican Republic notified the DSB of its intention to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, pursuant to paragraph 4 of Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU"), and filed a Notice of Appeal⁸ pursuant to Rule 20 of the *Working Procedures for Appellate Review* (the "*Working Procedures*").⁹ On 31 January 2005, the Dominican Republic filed its appellant's submission.¹⁰ On 7 February 2005, Honduras notified the DSB of its intention to appeal certain issues of law covered in the Panel Report and certain legal interpretations developed by the Panel, pursuant to Article 16.4 and Article 17 of the DSU, and filed a Notice of Other Appeal¹¹ pursuant to Rule 23(1) of the *Working Procedures*. On 8 February 2005, Honduras filed its other appellant's submission.¹² On 18 February 2005, the Dominican Republic and

³Panel Report, paras. 8.1(c) and 8.1(d).

⁴*Ibid.*, para. 8.2.

⁵*Ibid.*, paras. 8.1(b)-8.1(d).

⁶*Ibid.*, para. 8.3. The Panel also found that Honduras had failed to establish that the Dominican Republic legislation for the determination of the tax base for the Selective Consumption Tax subjected imported cigarettes to taxes in excess of those applied to like domestic products. (*Ibid.*, para. 8.3(a))

⁷*Ibid.*, para. 8.1(f).

⁸WT/DS302/8, 24 January 2005 (attached as Annex 1 to this Report).

⁹WT/AB/WP/5, 4 January 2005.

¹⁰Pursuant to Rule 21(1) of the *Working Procedures*.

¹¹WT/DS302/9, 7 February 2005 (attached as Annex 2 to this Report).

¹²Pursuant to Rule 23(3) of the *Working Procedures*.

Honduras each filed an appellee's submission.¹³ On the same day, China, the European Communities, and the United States each filed a third participant's submission.¹⁴ Also on 18 February 2005, Guatemala notified its intention to appear at the oral hearing as a third participant.¹⁵ El Salvador notified its intention to appear at the oral hearing on 7 March 2005.¹⁶

6. The oral hearing in this appeal was held on 9 March 2005. The participants and third participants presented oral arguments and responded to questions posed by the Members of the Division hearing the appeal.

II. Arguments of the Participants and the Third Participants

A. *Claims of Error by the Dominican Republic – Appellant*

1. The Necessity Analysis under Article XX(d) of the GATT 1994 in Relation to the Tax Stamp Requirement

7. The Dominican Republic submits that, in considering whether the Dominican Republic's tax stamp measure was justified under Article XX(d) of the GATT 1994, the Panel was "reviewing the decision making" of the Dominican Republic's authorities.¹⁷ As such, the Panel should have afforded the Dominican Republic a margin of discretion and should have assessed whether the Dominican Republic had a reasonable basis for its measure.

8. The Dominican Republic claims that the Panel erred in interpreting and applying the term "necessary" in Article XX(d) of the GATT 1994. The Dominican Republic points to the Reports of the Appellate Body in *Korea – Various Measures on Beef* and *EC – Asbestos* and contends that determining whether a measure is "necessary" under Article XX(d) involves, in every case, a process of weighing and balancing a series of factors. According to the Dominican Republic, a panel must weigh and balance: the trade impact of the measure; the importance of the interests protected by the measure; the contribution of the measure to the end pursued; and, the existence of alternative measures that a Member could reasonably be expected to employ. The Panel erred by analyzing only the existence of reasonably available alternatives to the tax stamp measure, and by failing to analyze, weigh, and balance the other relevant factors. The Dominican Republic points out that it is unlikely

¹³Pursuant to Rule 22 of the *Working Procedures*.

¹⁴Pursuant to Rule 24(1) of the *Working Procedures*.

¹⁵Pursuant to Rule 24(2) of the *Working Procedures*.

¹⁶Pursuant to Rule 24(4) of the *Working Procedures*.

¹⁷Dominican Republic's appellant's submission, para. 27.

that each factor will "indicate the same degree of necessity".¹⁸ Therefore, a panel must ascertain the collective strength of the factors. This requires a panel to consider the weight of each factor and to balance their relative weights, so as to determine whether, collectively, they render the measure necessary.

9. According to the Dominican Republic, a proper weighing and balancing of the relevant factors leads to the conclusion that the tax stamp requirement is "necessary" within the meaning of Article XX(d) of the GATT 1994. As regards the first factor, namely the trade impact of the measure, the Dominican Republic underlines that the Panel acknowledged that the trade impact of the tax stamp requirement is minimal. The Dominican Republic asserts that the Appellate Body has indicated that a measure with "a relatively slight impact upon imported products might more easily be considered as 'necessary' than a measure with intense or broader restrictive effects."¹⁹ For the Dominican Republic, the findings of the Panel in this respect dictate that, in the overall weighing and balancing of all the relevant factors, the tax stamp requirement may be more easily considered to be "necessary".

10. On the second factor—the importance of the interests protected by the measure—the Dominican Republic reiterates that the tax stamp requirement is designed to secure tax compliance and prevent deceptive practices, and that these interests are important. The Dominican Republic notes that the Panel acknowledged that the prevention of tax evasion is an important interest and recalls the Appellate Body's view that the "more vital or important those common interests or values are, the easier it would be to accept as 'necessary' a measure designed as an enforcement instrument."²⁰ The Dominican Republic adds that the link between cigarette smuggling and public health is well-established; consequently, as the tax stamp requirement aims to prevent the smuggling of cigarettes, it also helps to ensure the health and well-being of citizens, "both of which are interests of fundamental and critical importance".²¹ The Dominican Republic argues that, in the overall weighing and balancing, it should be easier to accept the tax stamp requirement as a "necessary" enforcement instrument because of the value and importance of the interests it protects.

¹⁸Dominican Republic's appellant's submission, para. 32.

¹⁹*Ibid.*, para. 34 (quoting Appellate Body Report, *Korea – Various measures on Beef*, para. 163).

²⁰*Ibid.*, para. 37 (quoting Appellate Body Report, *Korea – Various measures on Beef*, para. 162).

²¹*Ibid.*, para. 40.

11. The third factor addressed by the Dominican Republic is the contribution of the measure to the ends pursued. The Dominican Republic contends that affixation of tax stamps in the presence of a tax inspector contributes more to the prevention of tax evasion than affixation abroad, without the presence of a tax inspector. The Dominican Republic underlines that affixing the stamp abroad would make it possible for cigarettes smuggled into the Dominican Republic to be sold as stamped, while evading import taxes. Such a situation is prevented by the requirement to affix stamps in the Dominican Republic in the presence of a tax inspector, except if the stamp is forged. Thus, for the Dominican Republic, the tax stamp requirement not only seeks to ensure the authenticity of tax stamps, but also "contributes importantly to reducing the volume of smuggled cigarettes and increasing the volume of cigarettes bearing 'authentic tax stamps' ".²²

12. As regards the question of the existence of alternative measures that a Member could reasonably be expected to employ in place of the GATT-inconsistent measure, the Dominican Republic submits that the Panel wrongly concluded that an alternative measure is reasonably available in this case. According to the Dominican Republic, the measure to which the Panel alluded—providing secure tax stamps to foreign exporters and affixing the stamps abroad, possibly under the supervision of a reputable company that would conduct pre-shipment inspection and certification—is not an alternative that is reasonably available because it would increase the risk of smuggling and tax evasion, as compared with the tax stamp requirement, and, therefore, would be less likely to secure the goals pursued by the tax stamp requirement. The Dominican Republic points to evidence that cigarette producers actively collaborate in the smuggling of cigarettes. It also points to evidence of a higher prevalence of smuggling of alcoholic beverages, which it argues results from allowing the affixation of tax stamps outside of the territory of the Dominican Republic.

13. On this basis, the Dominican Republic submits that the Panel erred in finding that the Dominican Republic's tax stamp requirement is not "necessary" in the sense of Article XX(d) of the GATT 1994. It requests the Appellate Body to reverse the Panel's finding in this regard.

²²Dominican Republic's appellant's submission, para. 45.

14. In response to information concerning the recent modification of the tax stamp measure referred to by Honduras in its opening statement at the oral hearing²³, the Dominican Republic confirmed that a new decree had been passed that altered the application of the tax stamp requirement and allowed tax stamps to be affixed abroad.²⁴ The Dominican Republic, however, considers that the new measure reflects a change in the level of enforcement that it seeks to achieve. It therefore continues to maintain that only the affixation of stamps in the territory of the Dominican Republic, under the supervision of its tax authorities, can achieve its desired level of enforcement against smuggling and tax evasion.

2. Completing the Analysis under Article XX of the GATT 1994

15. In the event that the Appellate Body agrees with the Dominican Republic and reverses the Panel's finding that the tax stamp requirement is not "necessary" in the sense of paragraph (d) of Article XX of the GATT 1994, the Dominican Republic requests the Appellate Body to complete the legal analysis of its defence under Article XX of the GATT 1994 and find that the tax stamp requirement is not inconsistent with the GATT 1994.

16. The Dominican Republic submits that its tax stamp requirement is necessary to secure compliance with its Tax Code. It does so by alerting the Dominican Republic tax authorities that the applicable taxes have been collected and thereby prevents tax evasion. Further, the tax stamp requirement prevents cigarette smuggling because cigarettes are smuggled specifically to evade taxes and other applicable laws. The Dominican Republic observes that Honduras has not challenged the GATT-consistency of its Tax Code and itself noted that the Dominican Republic has the right to levy duties and taxes upon cigarettes. On this basis, the Dominican Republic submits that its tax stamp measure properly falls within the ambit of paragraph (d) of Article XX.

17. The Dominican Republic also submits that the tax stamp requirement is applied in a manner that satisfies the chapeau of Article XX of the GATT 1994. The tax stamp requirement is not applied

²³Paragraph 7 of Honduras' opening statement reads:

Honduras is surprised that the Dominican Republic is taking [the position that affixing tax stamps abroad is not a reasonably available alternative measure]. In October 2004, it enacted Decree No. 1360 – 04 to modify Article 37 of the Decree 79-03 in order to allow importers to affix the tax stamp abroad at the time of production. Pursuant to this Regulation, Honduras exported a cigarette shipment two weeks ago with the tax stamps affixed at the point of production. Honduras assumes that the Dominican Republic still maintains its interest of maintaining tax collection and preventing smuggling and forgery. Therefore, by allowing the tax stamps to be affixed abroad, the Dominican Republic has acknowledged that this alternative measure is reasonably available and can contribute to the ends pursued. ... (footnotes omitted)

²⁴Dominican Republic's response to questioning at the oral hearing.

in a manner that discriminates between different foreign supplying countries or between domestic and foreign suppliers of cigarettes. Indeed, Honduras has not made allegations to the contrary. Moreover, even if the Appellate Body were to find that the measure is applied in a discriminatory manner, there is nothing to suggest that any such discrimination is arbitrary or unjustifiable. Nor is there anything to suggest that the tax stamp requirement is applied in a manner that constitutes a disguised restriction on international trade.

3. The Conformity of the Panel's Examination of Exhibits DR-8 and DR-29 with Article 11 of the DSU

18. The Dominican Republic contends that the Panel failed to make an objective assessment of the facts of the case, contrary to Article 11 of the DSU, by misinterpreting evidence submitted in Exhibits DR-8 and DR-29 and by misunderstanding the proposition in support of which these exhibits were introduced. Although it recognizes that panels enjoy a margin of discretion in their appreciation of the evidence before them, according to the Dominican Republic, the Panel in this case exceeded the bounds of this discretion because an objective trier of facts could not have reached the Panel's conclusion on the basis of the evidence presented.

19. The Dominican Republic sought to demonstrate through Exhibits DR-8 and DR-29 "that, in the case of alcohol, a product in respect of which tax stamps can be affixed abroad: (a) there is smuggling into the territory of the Dominican Republic; and (b) tax stamps are forged."²⁵ The Panel, however, misread the letter incorporated in Exhibit DR-8 (Memo DAT-No. 46) and erroneously concluded that it did not demonstrate the forgery of tax stamps. The Panel also misunderstood the proposition for which Exhibit DR-8 was offered. The exhibit was offered as evidence of the existence of forgery of tax stamps, on the one hand, and smuggling of products, on the other. The Panel, however, incorrectly focussed on the relationship between smuggling and forgery. Exhibit DR-29, for its part, was offered for its probative value as to the smuggling of alcohol into the Dominican Republic. The Panel, however, simply disregarded the evidence in Exhibit DR-29, and mistakenly took it as evidence of forgery of tax stamps. Exhibit DR-29 was not offered as evidence of forgery of tax stamps. In addition, the Panel concluded that these two exhibits did not establish the existence of a causal link between allowing stamps to be affixed abroad and forgery of tax stamps. However, according to the Dominican Republic, there is irrefutable evidence on record that demonstrates that, whereas alcoholic beverages—which may be stamped outside the Dominican Republic—are

²⁵Dominican Republic's appellant's submission, para. 79.

smuggled with forged tax stamps, this practically never happens with cigarettes. The Panel failed to appreciate these facts as well. The Dominican Republic concludes that the Panel's findings, purportedly based on Exhibits DR-8 and DR-29, are wrong, and could not have been reached by an objective trier of facts. The Panel therefore failed to comply with its duty under Article 11 of the DSU.

B. *Arguments of Honduras – Appellee*

1. The Necessity Analysis under Article XX(d) of the GATT 1994 in Relation to the Tax Stamp Requirement

20. Honduras argues that the Dominican Republic has mischaracterized its appeal as one regarding the interpretation and application of Article XX(d) of the GATT 1994 to the tax stamp requirement, whereas, in reality, the Dominican Republic is asking the Appellate Body to reassess the evidence that was before the Panel and come to a different conclusion. According to Honduras, the Dominican Republic has not demonstrated that the Panel misinterpreted or misapplied the "necessity" test under Article XX(d). Honduras also submits that the Dominican Republic has not demonstrated any legal errors in the Panel's findings; rather, the Dominican Republic is seeking to re-argue the facts of the case and the conclusions that it considers should be drawn.

21. Moreover, according to Honduras, the Dominican Republic is attempting to introduce new factual elements in alleging that cigarette producers collaborate in smuggling, and that it would not, therefore, be appropriate to cede any control over the tax stamping process to producers. Honduras observes that there is no undisputed evidence upon which to base this assertion and urges the Appellate Body to disregard these allegations. In addition, the Dominican Republic is seeking to introduce the protection of human health as an objective to be secured by the discriminatory aspects of the tax stamp requirement. However, the Dominican Republic has not demonstrated why its measure protects human health. Honduras notes that protection of human health is dealt with under Article XX(b), not Article XX(d), and that arguments regarding human health were not made before the Panel. There are, therefore, no factual findings that would support the Dominican Republic's arguments regarding human health and the Appellate Body should give them "no credence".²⁶

22. Turning to the substantive question of whether the tax stamp requirement is "necessary" in the sense of Article XX(d) of the GATT 1994, Honduras disagrees with the Dominican Republic's submission that the Panel failed to weigh and balance the factors identified by the Appellate Body in *Korea – Various Measures on Beef* as relevant to the assessment of necessity under Article XX(d).

²⁶Honduras' appellee's submission, para. 22.

In Honduras' view, the Panel properly examined the relative importance of the interest served by the measure at issue. Honduras contests the Dominican Republic's assertion, which was not put forward before the Panel, that the measure aims to protect human life or health. The thrust of the tax stamp requirement is fiscal in nature, which, although important, is not on a par with the protection of human life or health. According to Honduras, the Panel also examined the extent to which the tax stamp requirement contributes to securing compliance with the Dominican Republic's tax laws and regulations. The Panel found that the Dominican Republic had not proven that discriminatory enforcement of the tax stamp requirement facilitates the prevention of tax evasion and smuggling. Moreover, the Dominican Republic did not provide the text of any laws against smuggling with which the tax stamp requirement would secure compliance. The Panel also examined whether the tax stamp requirement had restrictive effects on international commerce. Although, in this regard, the Panel felt it could assume that the measure did not have "intense restrictive effects on trade"²⁷, the fact that it went on to consider less-trade restrictive alternatives demonstrates that it considered the measure had at least some adverse affect on trade. In the view of Honduras, contrary to the submission of the Dominican Republic, the Panel properly weighed and balanced these considerations.

23. The Panel also properly identified a less-trade restrictive alternative to the tax stamp requirement imposed by the Dominican Republic, in accordance with the applicable standard for evaluating whether a measure is "necessary" in the sense of Article XX(d). The Panel was correct to find that allowing stamps to be affixed abroad, coupled with pre-shipment inspection and certification, would achieve the same level of enforcement. Honduras dismisses the two factors raised by the Dominican Republic in seeking to rebut the Panel's finding in this regard. First, with respect to the Dominican Republic's argument that cigarette producers actively collude in the smuggling of cigarettes, Honduras submits that this is an *ex post facto* justification for the measure, which, in any event, is merely an unsubstantiated assertion. The same is true of the Dominican Republic's second argument, namely the allegedly higher rate of smuggling that occurs with respect to alcohol resulting from the affixation of stamps outside of the territory of the Dominican Republic. The Dominican Republic has a weak factual basis upon which to assert that there is a higher prevalence of smuggling with respect to alcohol and there is no evidence of a causal relationship between the tax stamp requirement for cigarettes and the allegedly lower level of smuggling. Against that background, the Panel correctly found that allowing importers to affix stamps abroad during the production process would achieve the same level of enforcement as the existing measure; that this alternative measure would be administratively feasible for the Dominican Republic; and that this alternative measure would be less-trade restrictive than the current measure.

²⁷Honduras' appellee's submission, para. 51 (quoting Panel Report, para. 7.215).

24. Because the Dominican Republic has not demonstrated why the Panel erred in its application of the necessity test under Article XX(d), the Appellate Body should uphold the Panel's analysis.

25. At the oral hearing, Honduras drew attention to the fact that, in October 2004, the Dominican Republic enacted a new Decree modifying the tax stamp requirement so as to allow importers to affix tax stamps abroad, at the time of production.²⁸ Pursuant to this new measure, Honduras recently exported to the Dominican Republic a shipment of cigarettes with stamps attached at the factory. With these developments in mind, Honduras expressed surprise that the Dominican Republic continues to maintain that the only measure reasonably available to it is affixation of tax stamps within the Dominican Republic, under the supervision of the tax authorities. Honduras nevertheless confirmed that it requests the Appellate Body to rule on the WTO-consistency of the original measure embodying the tax stamp requirement, and requested that the Appellate Body make a recommendation under Article 19.1 of the DSU requesting the Dominican Republic to bring its measure into conformity with its obligations under the GATT 1994.

2. Completing the Analysis under Article XX of the GATT 1994

26. Honduras contends that, even if the Appellate Body were to reverse the finding of the Panel regarding the interpretation and application of the "necessity" test under Article XX(d) of the GATT 1994, it would have to find, in any event, that the Dominican Republic did not demonstrate that the measure at issue meets the requirement of the chapeau to Article XX. Honduras observes that an analysis under the chapeau would require the Appellate Body to focus upon "the *application* of the [tax stamp] measure and not the measure *as such*".²⁹ The burden of proof in such an analysis falls upon the party raising the defence. In Honduras' submission, the Dominican Republic did not discharge its burden under the chapeau before the Panel; nor has it done so before the Appellate Body. The Dominican Republic has not presented any evidence to substantiate its assertions that the tax stamp requirement is applied in a manner that is consistent with the chapeau. Indeed, there are no factual findings by the Panel regarding the application of the chapeau. Nor are there undisputed facts on the record. It is not, therefore, legally possible for the Appellate Body to complete the analysis in this case.

27. Honduras further submits that, even if the Appellate Body were nevertheless to complete the analysis under the chapeau to Article XX of the GATT 1994, it should find that the tax stamp requirement is applied in a manner that constitutes arbitrary or unjustifiable discrimination between countries where the same conditions prevail. Honduras points to evidence in Exhibit DR-3 that

²⁸See paragraph 7 of Honduras' opening statement, *supra*, footnote 23.

²⁹Honduras' appellee's submission, para. 75. (original emphasis)

suggests that, in practice, the Dominican Republic allows domestic producers to deduct the cost of tax stamps from their eventual liability under the Selective Consumption Tax. This deduction is not authorized on the face of the legislation governing the application of the tax stamp requirement, and is not available to importers. This differential in the treatment of importers and domestic producers constitutes both arbitrary and unjustifiable discrimination, and, therefore, is inconsistent with the chapeau to Article XX.

3. The Conformity of the Examination of Exhibits DR-8 and DR-29 with Article 11 of the DSU

28. Honduras submits that the Panel made an objective assessment of the facts of the case and did not exceed the bounds of its discretion in its consideration of Exhibits DR-8 and DR-29. Honduras observes that the Dominican Republic, in its first written submission to the Panel, argued that Exhibit DR-8 provided evidence regarding smuggling and tax evasion, "*as well as* forgery of tax stamps".³⁰ The Dominican Republic also entitled Exhibit DR-8 "Evidence of forgery, smuggling and tax evasion". The Dominican Republic is therefore wrong, in its appeal, to blame the Panel for finding that Exhibit DR-8 provided no evidence as to the relationship between smuggling and forgery of tax stamps. Any reasonable trier of facts could have construed the evidence as the Panel did: that is, as referring to a single case in which alcohol products were smuggled into the Dominican Republic with forged tax stamps. Indeed, the Panel correctly found that the evidence in Exhibit DR-8 was completely unrelated to any problem of forgery and that Memo DAT-No. 46, which was included in Exhibit DR-8, did not prove the occurrence of forgery in stamps. Honduras does not consider that certain minor errors by the Panel in its characterization of the evidence was anything more than an inconsequential mistake. Such minor errors do not constitute an egregious error by the Panel that would warrant a finding that the Panel failed to meet its obligations under Article 11 of the DSU.

29. With respect to Exhibit DR-29, Honduras recalls that panels enjoy broad discretion to choose which evidence to utilize in making findings and that panels are not required to accord to factual evidence the same weight as do the parties. Against that background, the Panel committed no error in deciding not to deal with Exhibit DR-29. The Panel was not bound to draw the same conclusion from this evidence as the Dominican Republic wanted it to draw.

³⁰Honduras' appellee's submission, para. 101 (quoting the Dominican Republic's first written submission to the Panel, para. 61). (emphasis added by Honduras)

C. *Claims of Error by Honduras – Appellant*

1. Article III:4 of the GATT 1994 and the Bond Requirement

30. Honduras challenges the Panel's conclusion that the bond requirement does not accord less favourable treatment to imported cigarettes in terms of Article III:4 of the GATT 1994. Honduras submits that the Panel failed to recognize that the bond requirement imposes an "extra burden" on imported products compared with domestic products. According to Honduras, the bond requirement secures only the payment of the Selective Consumption Tax. Whereas the importer has to pay the amount due for the Selective Consumption Tax prior to importation and has to post a bond to secure a tax liability that has already been discharged, the domestic producer has until the twentieth day of the month following the taxable transaction to pay the Selective Consumption Tax.³¹ Honduras contends that this lack of symmetry between the liabilities secured by the bond constitutes an "extra hurdle" or "extra burden" for imported products.³² Also, Honduras argues that the Panel erred in finding that the Dominican Republic has demonstrated that its tax authorities have the legal powers to reassess and adjust the applicable tax liabilities for a period of up to three years.

31. Honduras submits that the bond requirement creates situations in which imported products are accorded conditions of competition less favourable than those accorded to domestic products. In particular, Honduras underlines that, as in 2003 "the amount of Selective Consumption Tax imposed on domestic cigarettes ... was about *three times higher* than the amount imposed on imported cigarettes ... the per-unit cost of the bond requirement for imported cigarettes was ... three times higher than for domestic products."³³ For Honduras, this illustrates that the bond requirement creates situations in which imported products are accorded conditions of competition less favourable than those accorded to domestic products.

32. Honduras also considers that the Panel erred in its evaluation of the per-unit cost of the bond. According to Honduras, the Panel should have examined the conditions of competition established by the legislation, rather than the market situation in which the bond requirement was applied. In any event, Honduras notes that the bond requirement was introduced in March 2003 and argues that the per-unit cost determined by the Panel was incorrect, because it was based on the volume of imports in the years 2000-2002, and on the cost charged by financial institutions for a bond fee in 2004.³⁴ Honduras adds that, as the Panel did not determine the per-unit cost for domestic producers, it could

³¹Honduras' other appellant's submission, para. 63.

³²*Ibid.*

³³*Ibid.*, para. 70. (original emphasis)

³⁴*Ibid.*, para. 44.

not compare the per-unit costs between imported products and domestic like products. Accordingly, Honduras argues, the Panel did not have any basis upon which to conclude that there was no less favourable treatment being accorded to imports. Finally, Honduras submits that the Panel erred because it stated that the fact that a fixed expense (that is, an expense not related to volume of production) may lead to different per-unit costs among supplier firms is not in itself enough to conclude that the expense creates less favourable treatment for imported products.

2. Article XX(d) of the GATT 1994 and the Bond Requirement

33. At the oral hearing, Honduras responded to the claim raised by the Dominican Republic that, even if the Appellate Body accepts Honduras' appeal under Article III:4 of the GATT 1994 against the bond requirement, the measure is nevertheless justified under Article XX(d) of the GATT 1994. Honduras submits that the Dominican Republic must have in place alternative measures for products, other than cigarettes and alcohol, that are also subject to the Selective Consumption Tax. These alternative measures would be reasonably available to secure compliance with tax laws in the case of cigarettes as well. In Honduras' view, the Appellate Body should find that the Dominican Republic has not proven that its bond requirement is necessary to secure compliance with its tax laws.

3. Article 11 of the DSU and the Panel's Consideration of the Bond Requirement "As Such"

34. Honduras claims that the Panel failed to make an objective assessment of the matter before it, contrary to Article 11 of the DSU, in finding that the bond requirement secured obligations other than the Selective Consumption Tax. Honduras emphasizes that its claims relate to the bond requirement as such, independently from the application of that legislation in specific circumstances. According to Honduras, the Panel did not, however, consider the legislative basis of the bond requirement as such, but instead relied upon a letter from the Dominican Republic Director-General of Internal Taxes (referred to as Exhibit DR-12) that contradicted the terms of the underlying legislation. Honduras argues that, in analyzing its claim against the bond requirement as such, the Panel "should have properly examined only ... the terms of the legislation and [should] not have relied on the unsubstantiated views of one officer of an agency of the Dominican Republic".³⁵ Honduras finds support for its view in the Report of the Appellate Body in *India – Patents (US)*, where the Appellate Body found that certain "administrative instructions" regarding the application of India's Patents Act were insufficient to alter the WTO-inconsistent nature of that legislation because they appeared to contradict the terms of that legislation.

³⁵Honduras' other appellant's submission, para. 22.

4. The Timing of Payment of the Selective Consumption Tax and the Panel's Terms of Reference

35. Honduras submits that the Panel erred in treating certain contentions regarding the timing of payment of the Selective Consumption Tax as a separate claim outside of the Panel's terms of reference. Honduras submits that these contentions were simply arguments in support of its claim that the bond requirement violated Article III:4 of the GATT 1994. Honduras asks the Appellate Body to reverse the Panel's finding that these contentions were outside the Panel's terms of reference.

D. *Arguments of the Dominican Republic – Appellee*

1. Article III:4 of the GATT 1994 and the Bond Requirement

36. The Dominican Republic submits that the Panel correctly interpreted the term "treatment no less favourable" in Article III:4 of the GATT 1994 and requests the Appellate Body to reject Honduras' appeal against this finding. The Dominican Republic submits that Honduras advocates an erroneous interpretation of Article III:4.

37. According to the Dominican Republic, the Panel reached its conclusion with respect to the application of Article III:4 after properly identifying that Article III:4 requires an analysis of the conditions of competition prevailing between imports and like domestic products and having examined the impact of the bond requirement upon conditions of competition in the relevant market. The Dominican Republic submits that Honduras' main criticism is that the Panel considered the relevant market to determine whether the bond requirement accords less favourable treatment to imported cigarettes. For the Dominican Republic, however, an examination of whether a measure accords less favourable treatment to imports requires a panel to analyze the "thrust and effect" of the measure on conditions of competition in the relevant market.³⁶ This means that the existence of formally different treatment is not sufficient to show a violation of Article III:4. By the same token, the need for close scrutiny of the "effect" of a measure means that formally identical treatment is not necessarily consistent with Article III:4. Instead, the application of Article III:4 depends upon whether the measure in question modifies the conditions of competition to the detriment of importers. The question that a panel must answer, therefore, is whether the measure gives domestic producers a competitive advantage in the relevant market.

³⁶Dominican Republic's appellee's submission, para. 46 (referring to Appellate Body Report, *Korea – Various Measures on Beef*, para. 142).

38. According to the Dominican Republic, Honduras' objection to the Panel's approach is based on the untenable proposition that, in a case where a Member challenges a measure "as such", alleging *de facto* less favourable treatment, a panel cannot look beyond the text of the measure itself to consider the factual evidence that would prove *de facto* discrimination. The Dominican Republic notes that, although Honduras recognizes that the bond requirement imposes formally equal treatment, Honduras would preclude examination of evidence other than the text of the legislation in examining whether the formally equal treatment under the law nevertheless establishes *de facto* discrimination.

39. The Dominican Republic argues that Honduras' position is contrary to WTO jurisprudence on national treatment, in which panels and the Appellate Body have consistently looked to the application of the measure in question, its operation, and its effects on the conditions of competition in the relevant market. The Dominican Republic points to the approach taken to the analysis of *de facto* discrimination by the Appellate Body in *Canada – Autos* and in *Chile – Alcoholic Beverages* and by panels in *EC – Bananas III (Article 21.5 – Ecuador)*, *Canada – Pharmaceutical Patents*, and *Japan – Film* in support of its argument that Honduras is incorrect to claim on appeal that the Panel should have examined the effect of the bond requirement without looking at the relevant market or the application of the measure, and without considering evidence beyond the four-corners of the Dominican Republic legislation.

40. The Dominican Republic observes that the Panel considered the evidence adduced by the Dominican Republic to rebut the charges raised by Honduras that the bond requirement was inconsistent with Article III:4 of the GATT 1994. The Dominican Republic submits that Honduras failed to present any evidence to show that the bond requirement did, in fact, alter the conditions of competition in the relevant market. The Panel was correct, therefore, to find that Honduras had failed to establish that the bond requirement accords less favourable treatment to imported cigarettes. The Panel properly found that the bond requirement does not create a disincentive to import cigarettes; that the bond requirement secures the payment of tax liabilities for imported cigarettes; and that a bond for a fixed amount can secure the payment of a variable tax liability and still be consistent with Article III:4 of the GATT 1994.

2. Article XX(d) of the GATT 1994 and the Bond Requirement

41. In the event that the Appellate Body reverses the Panel's finding with respect to the bond requirement under Article III:4 of the GATT 1994 and finds that the bond requirement accords less favourable treatment to imported cigarettes, the Dominican Republic requests the Appellate Body to find that the bond requirement is nevertheless justified as necessary to secure compliance with GATT-consistent laws and regulations under Article XX(d) of the GATT 1994.

42. The Dominican Republic submits that Article XX(d) requires a two-step analysis. First, the measure must be provisionally justified under Article XX(d). Secondly, it must comply with the requirements of the chapeau to Article XX. The Dominican Republic says that its measure secures compliance with its tax laws and regulations, and that these tax laws and regulations are consistent with the GATT 1994. The Dominican Republic refers to certain findings by the Panel, which, it claims, substantiate these assertions. The Dominican Republic also argues that the bond requirement is "necessary" to secure compliance with the tax laws and regulations of the Dominican Republic, in the sense that it is "indispensable". Moreover, even if the Appellate Body were to find that the bond requirement is not indispensable, an appropriate weighing and balancing of the four factors identified for the analysis of necessity in *Korea – Various Measures on Beef* demonstrates that the measure in question remains necessary in the sense of Article XX(d). The measure therefore satisfies the requirements of Article XX(d) and is provisionally justified under that provision.

43. In addition, the Dominican Republic submits that its measure is not applied in a manner that discriminates between countries where the same conditions prevail and that any alleged discrimination is neither arbitrary nor unjustifiable. The Dominican Republic also submits that the bond requirement is not applied in a manner that constitutes a disguised restriction on international trade. Accordingly, in addition to being provisionally justified under paragraph (d) of Article XX, the bond requirement also satisfies the conditions of the chapeau to Article XX. It therefore meets the requirements of Article XX of the GATT 1994 and thus falls within the general exception provided by that provision.

3. Article 11 of the DSU and the Panel's Consideration of the Bond Requirement "As Such"

44. The Dominican Republic submits that the Panel made an objective assessment of the facts of the case in addressing Honduras' "as such" claim against the bond requirement. It accordingly requests the Appellate Body to reject Honduras' appeal in this regard.

45. The Dominican Republic submits that the Appellate Body has said it will interfere with a panel's appreciation of the evidence before it only if it is satisfied that the panel "exceeded its discretion" and, in effect, made an "egregious error".³⁷ It observes that Honduras has made a claim against legislative provisions establishing the bond requirement "as such". Honduras' claim thus focuses on the meaning of a municipal law of the Dominican Republic. In addressing the meaning of municipal law, panels must examine the law as a matter of fact, taking into account the evidence as to the meaning of the law presented by the parties. In ascertaining the meaning of a municipal law,

³⁷Dominican Republic's appellee's submission, para. 23 (quoting Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 186).

nothing precludes a panel from considering statements made by representatives of the responding Member regarding that law; indeed, such statements have been relied upon by panels (such as in *US – Section 301 Trade Act*) and the Appellate Body (for example, in *US – Hot-Rolled Steel*) in the past.

46. In this case, the Panel correctly treated the meaning of the Dominican Republic's municipal law as a fact whose meaning was to be proved by evidence. The Panel thus considered the text of the legislation itself, as well as a letter from the Director-General of Internal Taxes, the senior official of the Dominican Republic responsible for administering the relevant matter at the municipal level. Honduras did nothing to rebut the contents of the letter, other than to claim it was inadmissible as evidence.

47. The Dominican Republic contests Honduras' assertion that the letter from the Director-General of Internal Taxes is inconsistent with the wording of Article 376 of the Tax Code. Nothing on the face of the law precludes the bond from being applied to fiscal obligations other than the Selective Consumption Tax. The Dominican Republic also disagrees with the position of Honduras that the letter should have been disregarded as it was somehow tainted because it came from an official of the Dominican Republic. The Dominican Republic says that a Member is obliged under Article 3.10 of the DSU to engage in dispute settlement "in good faith". Representations by a Member made during dispute settlement therefore cannot be presumed to be tainted, merely because they are made in dispute settlement.

4. The Timing of Payment of the Selective Consumption Tax and the Panel's Terms of Reference

48. The Dominican Republic argues that the Panel was correct in concluding that the timing of the payment of the Selective Consumption Tax, as a separate claim, was outside the terms of reference of the Panel. The Dominican Republic notes that the timing of payment of the Selective Consumption Tax was not addressed in Honduras' request for the establishment of the Panel; nor was it addressed in Honduras' first written submission to the Panel. Rather, it was mentioned for the first time in a single paragraph of Honduras' second written submission to the Panel. According to the Dominican Republic, the Panel did not overlook the distinction between claims and arguments. The Panel was well aware of this distinction and correctly distinguished between the argument made by Honduras in support of its legal claim that the bond requirement was inconsistent with Article III:4 of the GATT 1994, and its veiled claim that the difference in timing of the payment of the Selective Consumption Tax accorded less favourable treatment to importers.

E. *Arguments of the Third Participants*

1. China

- (a) The necessity analysis under Article XX(d) of the GATT 1994 in relation to the tax stamp requirement

49. China notes that a party invoking Article XX(d) of the GATT 1994 must demonstrate that its measure is "necessary" to secure compliance with GATT-consistent laws or regulations. China synthesizes the jurisprudence of the Appellate Body on this issue as suggesting that "necessary" in this context should mean "almost indispensable".³⁸ China also observes that the Appellate Body has set out a number of factors that need to be considered in assessing whether a measure is "necessary". These include three factors identified in *Korea – Various Measures on Beef*: the contribution of the measure to the ends pursued; the importance of the interests protected; and the trade impact of the measure. There is also another factor from earlier jurisprudence, which the Appellate Body described as "encapsulating" these three factors, namely, the existence of reasonably available alternatives to the impugned measure that are consistent, or less inconsistent, with other GATT provisions. In China's view, the three factors identified in *Korea – Various Measures on Beef* have not replaced the traditional test. However, the application of all relevant factors may have an impact on the burden of proof: if a party invoking Article XX(d) demonstrates that its measure stands up with respect to the first three factors, then it has established a *prima facie* case that Article XX(d) applies; the burden then shifts to the other party to rebut this presumption. This could be achieved by demonstrating the existence of a GATT-consistent alternative measure.

- (b) Article III:4 of the GATT 1994 and the bond requirement

50. With respect to Honduras' appeal regarding the application of Article III:4 of the GATT 1994 to the bond requirement, China submits that less favourable treatment in the sense of Article III:4 is judged by reference to modification of the conditions of competition. The term "no less favourable" is unqualified and is thus not subject to a *de minimis* exception; any less favourable treatment is inconsistent with Article III:4. China also notes that formal equality of treatment is not sufficient to show equally favourable treatment if it is demonstrated that, in practice, less favourable treatment results.

³⁸China's third participant's submission, para. 6.

2. European Communities

- (a) The necessity analysis under Article XX(d) of the GATT 1994 in relation to the tax stamp requirement

51. The European Communities considers that the Panel was correct to find that the tax stamp requirement was not justified by the provisions of Article XX(d) of the GATT 1994. The European Communities submits that the Panel properly applied the test outlined by the Appellate Body in *Korea – Various Measures on Beef* for determining whether a measure is "necessary" in terms of Article XX(d). The European Communities argues that the Panel correctly took into account the importance of the common interest served by the tax stamp requirement and the contribution of the tax stamp requirement to the objective pursued. The European Communities questions the Panel's assumption that the measure in question had no "intense restrictive effects on trade"³⁹; however, given that the Panel properly weighed the other relevant considerations—in particular the existence of alternative measures—the European Communities considers that this assumption did not affect the Panel's ultimate conclusion. The European Communities agrees with the finding of the Panel that less-trade restrictive alternatives to the tax stamp requirement were available to the Dominican Republic. The European Communities notes that the sale of tax stamps abroad is a commonly used practice. It submits that the risk of forgery is minimal and that implementation of this measure would not raise implementation difficulties. Furthermore, such a measure would inevitably be less-trade restrictive. Accordingly, the European Communities maintains that the Panel did not err in its analysis of the tax stamp requirement under Article XX(d) of the GATT 1994.

- (b) Article III:4 of the GATT 1994 and the bond requirement

52. The European Communities also submits that the Panel was correct in finding that the fees incurred as a result of the bond requirement did not result in "less favourable treatment" for importers in the sense of Article III:4 of the GATT 1994. The European Communities notes that the fixed amount of the bond accords formally equal treatment to importers and domestic producers. The question whether it nevertheless results in *de facto* discrimination requires an analysis of the facts of the case to determine whether the measure alters the conditions of competition. The European Communities recalls that the Panel noted that the costs entailed by the bond requirement were so low as to be unlikely to adversely affect the conditions of competition prevailing in the marketplace. As a matter of principle, the European Communities agrees with this analysis; conditions of competition are not affected by a marginal, negligible difference in costs. The European Communities also points to the principle elaborated in paragraph 1 of Article III, which indicates that internal measures should

³⁹European Communities' third participant's submission, para. 22 (quoting Panel Report, para. 7.215).

not be applied so as to afford protection to domestic production. A measure with formally equal treatment and minimal or negligible practical consequences is unlikely to be applied so as to afford protection.

- (c) Article 11 of the DSU and the Panel's consideration of the bond requirement "as such"

53. The European Communities submits that the Panel made an objective assessment of Honduras' claims regarding the bond requirement, consistent with the requirements of Article 11 of the DSU. According to the European Communities, the matter before the Panel was defined, in the first place, by Honduras' request for the establishment of the Panel. Honduras' panel request referred not only to the legislation establishing the bond requirement, but also to "practices" under the bond requirement. Accordingly, it was appropriate for the Panel to consider such practices in addressing Honduras' claims against the bond requirement. The European Communities thus disagrees with the position of Honduras regarding the import of *India – Patents (US)*. Contrary to the position of Honduras, *India – Patents (US)*, in which the panel reviewed practices as well as the underlying legislation, would tend to confirm the approach of the Panel in this case. Indeed, it is consistent with the object and purpose of the DSU for a panel to take into account all relevant elements for its determinations regarding the matter before it.

3. United States

- (a) The necessity analysis under Article XX(d) of the GATT 1994 in relation to the tax stamp requirement

54. The United States argues that the Panel's interpretation of the term "necessary" in Article XX(d) adds to and diminishes WTO Members' rights and obligations under the GATT 1994. The United States raises three concerns with the Panel's interpretation. First, the United States considers incorrect the notion that Article XX(d) requires a Member to select a less GATT-inconsistent alternative where no GATT-consistent alternative is available. There is nothing to justify use of a concept of degrees of inconsistency in the application of Article XX(d). Moreover, such a concept would be difficult to administer and is logically incoherent. In this case, the Panel characterizes as "less GATT-inconsistent" possible alternative measures that are "less trade-restrictive".⁴⁰ In so doing, the Panel impermissibly imports into Article XX(d) a requirement that a Member use a less-trade restrictive measure, if one is available. There is no basis in the GATT 1994 for doing so. Secondly, the United States submits that the Panel has distorted the meaning of "necessary" in Article XX(d) by equating it with "sufficient", implying that a measure that does not

⁴⁰United States' third participant's submission, para. 7.

succeed in securing compliance with a Member's desired level of protection is not "necessary". Thirdly, the United States argues that a measure that would involve continuation of a risk that a Member seeks to avoid cannot be a reasonably available alternative to an impugned measure. The United States emphasizes the right of Members to determine their own desired level of protection.

(b) Article III:4 of the GATT 1994 and the bond requirement

55. The United States also suggests that, in its appeal regarding the application of Article III:4 of the GATT 1994 to the bond requirement, Honduras mischaracterizes the standard for finding "treatment no less favourable" under Article III:4. The United States submits that the Panel properly articulated the relevant test as one based on the conditions of competition prevailing in the market, and correctly found that the differences in the per-unit costs of the bond were not in themselves sufficient to demonstrate that importers received less favourable treatment. In addition, according to the United States, throughout its appeal, Honduras alleges that the Panel improperly applied Article III:4 because it took into account the market performance of importers in the past years as the decisive element, rather than the bond itself. However, although Honduras criticizes the Panel for examining the market performance of importers, according to the United States, it is Honduras that improperly seeks a finding of less favourable treatment on this basis.

III. Issues Raised in this Appeal

56. The following issues are raised in this appeal:

- (a) whether the Panel erred in finding that the tax stamp requirement is not justified under Article XX(d) of the GATT 1994, based on its interpretation and application of the term "necessary" in that provision;
- (b) whether the Panel failed to make an objective assessment of the facts of the case, as required by Article 11 of the DSU, in its examination of Exhibits DR-8 and DR-29;
- (c) whether the Panel erred in finding that Honduras failed to establish that the bond requirement accords less favourable treatment to imported cigarettes than that accorded to like domestic products, in a manner inconsistent with Article III:4 of the GATT 1994;
- (d) whether the Panel failed to make an objective assessment of the matter before it, as required by Article 11 of the DSU, in its consideration of Honduras' claim against the bond requirement "as such"; and,

- (e) whether the Panel erred in finding that Honduras' contentions regarding the timing of payment of the Selective Consumption Tax represented a separate claim outside the Panel's terms of reference.

IV. The Necessity Analysis under Article XX(d) of the GATT 1994 in relation to the Tax Stamp Requirement

57. The Dominican Republic requires that tax stamps be affixed to cigarette packets in the territory of the Dominican Republic under the supervision of the Dominican Republic's tax authorities (the "tax stamp requirement"). The Panel found that the tax stamp requirement is inconsistent with the national treatment obligation set out in Article III:4 of the GATT 1994.⁴¹ According to the Panel, although the tax stamp requirement is applied in a formally equal manner to domestic and imported cigarettes, it modifies the conditions of competition in the marketplace to the detriment of imports. The Panel found that the tax stamp requirement results in additional processes and costs for imported products, and leads to imported cigarettes being presented to final consumers in a less appealing manner. Having found that the tax stamp requirement was inconsistent with Article III:4 of the GATT 1994, the Panel then examined the Dominican Republic's argument, under Article XX(d) of the GATT 1994, that the tax stamp requirement is necessary to secure compliance with the Dominican Republic tax laws and regulations, to fight tax evasion, and to prevent smuggling of cigarettes. The Panel concluded that the Dominican Republic had failed to establish that the tax stamp requirement is justified under Article XX(d) of the GATT 1994.⁴²

58. On appeal, the Dominican Republic limits its challenge to the Panel's finding that the tax stamp requirement is not justified under Article XX(d) of the GATT 1994. The Dominican Republic does not appeal the Panel's finding that the tax stamp requirement is inconsistent with the national treatment obligation set out in Article III:4 of the GATT 1994. Therefore, we need not express any view on the finding under Article III:4.

59. In considering the Dominican Republic's argument under Article XX(d), the Panel began its analysis by assuming that the tax laws and regulations to be enforced through the tax stamp requirement are not inconsistent with the provisions of the GATT 1994. The Panel then examined whether the tax stamp requirement is "necessary" to secure compliance with those laws and regulations. The Panel acknowledged that "the collection of tax revenue (and, conversely, the prevention of tax evasion) is a most important interest" for the Dominican Republic.⁴³ The Panel also

⁴¹Panel Report, paras. 7.198 and 8.1(e).

⁴²*Ibid.*, paras. 7.232, 7.233 and 8.1(e).

⁴³*Ibid.*, para. 7.215.

said that "the measure has not had any intense restrictive effects on trade".⁴⁴ The Panel found, however, no supporting evidence "that there is a causal link between allowing stamps to be affixed abroad and the forgery of tax stamps."⁴⁵ According to the Panel, the requirement of affixing tax stamps in the Dominican Republic and under the supervision of the Dominican Republic authorities "would only serve to guarantee that those tobacco products that enter legally into the country and go through the proper customs procedures will carry authentic tax stamps as a proof that the appropriate tax has been paid."⁴⁶ The Panel added that the tax stamp requirement, "in and of itself, would not prevent the forgery of tax stamps, nor smuggling and tax evasion."⁴⁷ In the opinion of the Panel, the Dominican Republic did not discharge its duty to prove why other reasonably available GATT-consistent or less GATT-inconsistent measures would not be able to achieve the level of enforcement with regard to tax collection and cigarette smuggling that the Dominican Republic sought to attain with the tax stamp requirement.⁴⁸ For the Panel, a reasonably available alternative to the tax stamp requirement would be to provide secure tax stamps to foreign exporters.⁴⁹ In this light, the Panel concluded that the tax stamp requirement is not "necessary" to secure compliance with the Dominican Republic's tax laws and regulations. Accordingly, the Panel found that the tax stamp requirement is not justified under Article XX(d) of the GATT 1994.⁵⁰

60. The Dominican Republic claims that the Panel erred in interpreting and applying the term "necessary" in Article XX(d) of the GATT 1994. The Dominican Republic relies mainly on the Appellate Body Report in *Korea – Various Measures on Beef*, contending that, determining whether a measure is "necessary" under Article XX(d), involves in every case a process of weighing and balancing a series of factors.⁵¹ According to the Dominican Republic, a panel must weigh and balance the following four factors as part of the necessity analysis: (1) the trade impact of the measure; (2) the importance of the interests protected by the measure; (3) the contribution of the measure to the end pursued; and (4) the existence of alternative measures that a Member could reasonably be expected to employ.⁵² Thus, "the Panel improperly interpreted and applied the term

⁴⁴Panel Report, para. 7.215.

⁴⁵*Ibid.*, para. 7.226.

⁴⁶*Ibid.*

⁴⁷*Ibid.*

⁴⁸*Ibid.*, para. 7.228.

⁴⁹Thus, tax stamps would be affixed on cigarette packets in the course of the foreign manufacturer's production process and prior to importation into the Dominican Republic.

⁵⁰Given its conclusion that the tax stamp requirement is not "necessary" under Article XX(d), the Panel considered that it did not need to analyze consistency of the measure with the chapeau of Article XX.

⁵¹Dominican Republic's appellant's submission, para. 30 (referring to Appellate Body Report, *Korea – Various Measures on Beef*, para. 164).

⁵²*Ibid.*, para. 31.

'necessary' because it failed to examine fully all the factors relevant to determining whether a measure is 'necessary' under Article XX(d), including weighing and balancing them, as required by Article XX(d)."⁵³ The Dominican Republic adds that a proper weighing and balancing of the relevant factors leads to the conclusion that the tax stamp requirement is "necessary" within the meaning of Article XX(d) of the GATT 1994. In particular, the Dominican Republic contends that affixation of tax stamps in the presence of a tax inspector contributes more to the prevention of tax evasion than affixation abroad, without the presence of a tax inspector. The Dominican Republic underlines that affixing the stamp abroad would make it possible for cigarettes smuggled into the Dominican Republic to be sold as stamped, while evading import taxes. This would be prevented by the requirement to affix stamps in the Dominican Republic in the presence of a tax inspector, unless the stamp is forged. Thus, for the Dominican Republic, the tax stamp requirement not only seeks to ensure the authenticity of tax stamps, but also "contributes importantly to reducing the volume of smuggled cigarettes and increasing the volume of cigarettes bearing 'authentic tax stamps'."⁵⁴

61. Regarding the question of the existence of alternative measures that a Member could reasonably be expected to employ in place of the GATT-inconsistent measure, the Dominican Republic submits that the Panel erred in concluding that an alternative measure is reasonably available. According to the Dominican Republic, the alternative identified by the Panel—providing secure tax stamps to foreign exporters—is not a reasonably available alternative because it would increase the risk of smuggling and tax evasion, as compared with the tax stamp requirement, and, therefore, would be less likely to secure the goals pursued by the tax stamp requirement.

62. For Honduras, the Dominican Republic's contention that the Panel did not properly weigh and balance the relevant factors in its analysis under Article XX(d) should be rejected. Honduras maintains that "the Panel properly set out and applied the appropriate factors in its assessment of the measure under Article XX(d)."⁵⁵ Honduras adds that "the Panel did examine the relevant factors in its assessment of whether there were less trade restrictive alternative measures that the Dominican Republic could have employed."⁵⁶

⁵³Dominican Republic's appellant's submission, para. 30.

⁵⁴*Ibid.*, para. 45.

⁵⁵Honduras' appellee's submission, para. 37.

⁵⁶*Ibid.*, para. 65.

63. At the oral hearing, Honduras drew attention to the fact that, on 25 October 2004, the Dominican Republic enacted a new decree modifying the tax stamp requirement to allow tax stamps to be affixed abroad at the time of production.⁵⁷ The Dominican Republic confirmed that it had enacted the new decree. Honduras stated that, pursuant to this new measure, it had recently exported to the Dominican Republic a shipment of cigarettes with stamps attached at the factory. Honduras expressed surprise that, in these circumstances, the Dominican Republic continues to maintain that the only measure reasonably available to it is affixation of tax stamps within the Dominican Republic, under the supervision of the tax authorities. Both participants nevertheless requested the Appellate Body to rule on whether the original measure is justified under Article XX(d) of the GATT 1994.

64. We begin our consideration of Article XX(d) by noting that the analysis of a measure under Article XX is two-tiered:

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.⁵⁸

65. In *Korea – Various Measures on Beef*, the Appellate Body explained the analysis to be undertaken in considering the justification of a measure under paragraph (d) of Article XX:

For a measure ... to be justified provisionally under paragraph (d) of Article XX, two elements must be shown. First, the measure must be one designed to "secure compliance" with laws or regulations that are not themselves inconsistent with some provision of the GATT 1994. Second, the measure must be "necessary" to secure such compliance.⁵⁹

66. The Appellate Body also explained that determining whether a measure is "necessary" within the meaning of Article XX(d):

⁵⁷The new decree was enacted after the issuance of the Panel Report to the parties on 20 October 2004. We also referred to the enactment of the new decree in paragraph 14 of this Report.

⁵⁸Appellate Body Report, *US – Gasoline*, p. 22, DSR 1996:I, 3, at 20.

⁵⁹Appellate Body Report, *Korea – Various Measures on Beef*, para. 157.

... involves in every case a process of weighing and balancing a series of factors which prominently include the contribution made by the compliance measure to the enforcement of the law or regulation at issue, the importance of the common interests or values protected by that law or regulation, and the accompanying impact of the law or regulation on imports or exports.⁶⁰

67. The Appellate Body also referred to the GATT panel report in *US – Section 337*, in particular to the statement that a Member's inconsistent measure cannot be deemed to be necessary "if an alternative measure which it could reasonably be expected to employ and which is not inconsistent with other GATT provisions is available to it."⁶¹

68. In *EC – Asbestos*, the Appellate Body considered whether the measure challenged in those proceedings was "necessary" to protect public health within the meaning of Article XX(b) of the GATT 1994. The Appellate Body stated that "in determining whether a suggested alternative measure is 'reasonably available', several factors must be taken into account, besides the difficulty of implementation."⁶² Relying on its Report in *Korea – Various Measures on Beef*, the Appellate Body reiterated, in the context of Article XX(b), that "one aspect of the 'weighing and balancing process ... comprehended in the determination of whether a WTO-consistent alternative measure' is reasonably available is the extent to which the alternative measure 'contributes to the realization of the end pursued'.⁶³ Another factor to be taken into account in determining whether an alternative measure is reasonably available is the importance of the interests or values pursued: "[t]he more vital or important [the] common interests or values' pursued, the easier it would be to accept as 'necessary' measures designed to achieve those ends."⁶⁴

69. In *US – Gambling*, the Appellate Body considered the "necessity" test in the context of Article XIV of the *General Agreement on Trade in Services*. The Appellate Body confirmed that an assessment of the "necessity" of a measure involves a weighing and balancing of "the 'relative importance' of the interests or values furthered by the challenged measure", along with other factors, which will usually include "the contribution of the measure to the realization of the ends pursued by it

⁶⁰Appellate Body Report, *Korea – Various Measures on Beef*, para. 164.

⁶¹*Ibid.*, para. 165 (quoting GATT Panel Report, *US – Section 337*, para. 5.26).

⁶²Appellate Body Report, *EC – Asbestos*, para. 170.

⁶³*Ibid.*, para. 172 (quoting Appellate Body Report, *Korea – Various Measures on Beef*, paras. 166 and 163).

⁶⁴*Ibid.*, para. 172 (quoting Appellate Body Report, *Korea – Various Measures on Beef*, para. 162).

[and] the restrictive impact of the measure on international commerce."⁶⁵ The Appellate Body went on to explain that:

A comparison between the challenged measure and possible alternatives should then be undertaken, and the results of such comparison should be considered in the light of the importance of the interests at issue. It is on the basis of this "weighing and balancing" and comparison of measures, taking into account the interests or values at stake, that a panel determines whether a measure is "necessary" or, alternatively, whether another, WTO-consistent measure is "reasonably available".⁶⁶

70. The Appellate Body Reports in *Korea – Various Measures on Beef*, *EC – Asbestos* and *US – Gambling* indicate that, in the assessment of whether a proposed alternative to the impugned measure is reasonably available, factors such as the trade impact of the measure, the importance of the interests protected by the measure, or the contribution of the measure to the realization of the end pursued, should be taken into account in the analysis. The weighing and balancing process of these three factors also informs the determination whether a WTO-consistent alternative measure which the Member concerned could reasonably be expected to employ is available, or whether a less WTO-inconsistent measure is reasonably available. Furthermore, in *US – Gambling*, the Appellate Body indicated:

An alternative measure may be found not to be "reasonably available", however, where it is merely theoretical in nature, for instance, where the responding Member is not capable of taking it, or where the measure imposes an undue burden on that Member, such as prohibitive costs or substantial technical difficulties. Moreover, a "reasonably available" alternative measure must be a measure that would preserve for the responding Member its right to achieve its desired level of protection with respect to the objective pursued ...⁶⁷

71. In assessing whether a WTO-consistent measure was reasonably available, the Panel in the present case discussed the factors identified by the Appellate Body in previous appeals, namely, the importance of the interests protected by the tax stamp requirement, its trade impact and its contribution to the realization of the end pursued. As regards the first factor, "the Panel [did] not disagree with the Dominican Republic's argument that tax stamps may be a useful instrument to monitor tax collection on cigarettes and, conversely, to avoid tax evasion."⁶⁸ The Panel also recognized that "the collection of tax revenue (and, conversely, the prevention of tax evasion) is a

⁶⁵Appellate Body Report, *US - Gambling*, para. 306.

⁶⁶*Ibid.*, para. 307.

⁶⁷*Ibid.*, para. 308.

⁶⁸Panel Report, para. 7.217.

most important interest for any country and particularly for a developing country such as the Dominican Republic."⁶⁹ With respect to the trade impact of the measure, the Panel noted that the tax stamp requirement did not prevent Honduras from exporting cigarettes to the Dominican Republic and that its exports had increased significantly over recent years.⁷⁰ Accordingly, the Panel assumed "that the measure has not had any intense restrictive effects on trade."⁷¹ As far as the third factor is concerned, the Panel noted the Dominican Republic's claim that "the tax stamp requirement secures compliance with its tax laws and regulations generally, and more specifically with the provisions governing the Selective Consumption Tax."⁷² The Panel, however, was of the view that the tax stamp requirement was of limited effectiveness in preventing tax evasion and cigarette smuggling. According to the Panel, requiring that tax stamps be affixed in the Dominican Republic under the supervision of the tax authorities "in and of itself, would not prevent the forgery of tax stamps, nor smuggling and tax evasion."⁷³ In this respect, the Panel indicated that other factors, such as security features incorporated into the tax stamps, or police controls on roads and at different commercial levels, would play a more important role in preventing forgery of tax stamps, tax evasion and smuggling of tobacco products.⁷⁴ Having considered the importance of the interests protected by the tax stamp requirement, its trade impact, and its contribution to the realization of the end pursued, we are of the view that the Panel conducted an appropriate analysis, following the approach set out in the Appellate Body Reports in *Korea – Various Measures on Beef* and in *EC – Asbestos*, and affirmed in *US - Gambling*. We see no error in the approach taken by the Panel or in the results of its analysis. We note that, in this particular case, the Panel's conclusion concerning the contribution of the measure to the realization of the end pursued is based on findings of fact (limited effectiveness of the tax stamp requirement in preventing forgery, smuggling and tax evasion; greater effectiveness and efficiency of measures such as security features incorporated into the tax stamps or police controls) that have not been challenged under Article 11 of the DSU and, therefore, fall outside the scope of appellate review.

72. Having assessed the importance of the interests protected by the tax stamp requirement, its trade impact, and its contribution to the realization of the end pursued, the Panel also considered whether a WTO-consistent alternative measure is reasonably available to secure compliance with the Dominican Republic's tax laws and regulations appropriate to the level of enforcement pursued by the Dominican Republic. In the light of its analysis of the relevant factors, especially the measure's contribution to the realization of the end pursued, the Panel opined that the alternative of providing

⁶⁹Panel Report, para. 7.215.

⁷⁰*Ibid.*

⁷¹*Ibid.*

⁷²*Ibid.*, para. 7.210.

⁷³*Ibid.*, para. 7.226.

⁷⁴*Ibid.*

secure tax stamps to foreign exporters, so that those tax stamps could be affixed on cigarette packets in the course of their own production process, prior to importation, would be equivalent to the tax stamp requirement in terms of allowing the Dominican Republic to secure the high level of enforcement it pursues with regard to tax collection and the prevention of cigarette smuggling.⁷⁵ The Panel gave substantial weight to its finding that the tax stamp requirement is of limited effectiveness in preventing tax evasion and cigarette smuggling; in particular, it found "no evidence to conclude that the tax stamp requirement secures a zero tolerance level of enforcement with regard to tax collection and the prevention of cigarette smuggling."⁷⁶ We consider that the Panel conducted an appropriate analysis, following the approach set out in *Korea – Various Measures on Beef* and in *EC – Asbestos*, and affirmed in *US - Gambling*. We see no reason to disturb the Panel's conclusions in respect of the existence of a reasonably available alternative measure to the tax stamp requirement.

73. In the light of these considerations, we *uphold* the Panel's finding, in paragraphs 7.232, 7.233 and 8.1(e) of the Panel Report, that the tax stamp requirement is not "necessary" within the meaning of Article XX(d) of the GATT 1994 and, therefore, is not justified under Article XX(d) of the GATT 1994.

74. The Dominican Republic requests us to complete the legal analysis under Article XX of the GATT 1994 should we find that the Panel misinterpreted or misapplied the term "necessary" in Article XX(d) of the GATT 1994. As we agree with the Panel's interpretation of the term "necessary" and we uphold the Panel's finding that the tax stamp requirement is not "necessary" within the meaning of Article XX(d) of the GATT 1994, the contingency on which the Dominican Republic's request is based does not arise and, therefore, there is no need for us to complete the legal analysis under Article XX of the GATT 1994.

V. The Conformity of the Examination of Exhibits DR-8 and DR-29 with Article 11 of the DSU

75. We turn next to consider the Dominican Republic's claim on appeal that the Panel erred in its appreciation of the evidence in Exhibits DR-8 and DR-29, such that it failed to make an objective assessment of the facts as required by Article 11 of the DSU. According to the Dominican Republic, this evidence relates to "tax evasion, smuggling, and forgery of tax stamps with respect to alcohol products".⁷⁷ The Dominican Republic sought to demonstrate, through Exhibits DR-8 and DR-29,

⁷⁵Panel Report, para. 7.228.

⁷⁶*Ibid.*, para. 7.229.

⁷⁷Dominican Republic's appellant's submission, para. 79.

"that, in the case of alcohol, a product in respect of which tax stamps can be affixed abroad: (a) there is smuggling into the territory of the Dominican Republic; and (b) tax stamps are forged."⁷⁸

76. Article 11 of the DSU requires that a panel, *inter alia*:

... make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements, and make such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the covered agreements.

77. In *EC – Hormones*, the first appeal presenting an Article 11 challenge to a Panel's fact-finding⁷⁹, the Appellate Body identified the "duty to make an objective assessment of the facts [as], among other things, an obligation to consider the evidence presented to a panel and to make factual findings on the basis of that evidence."⁸⁰ The Appellate Body also observed in that appeal that the:

[d]etermination of the credibility and weight properly to be ascribed to (that is, the appreciation of) a given piece of evidence is part and parcel of the fact finding process and is, in principle, left to the discretion of a panel as the trier of facts.⁸¹

78. The Appellate Body has consistently emphasized, since *EC – Hormones*, that, within the bounds of their obligation under Article 11 to make an objective assessment of the facts of the case, panels enjoy a "margin of discretion" as triers of fact.⁸² Panels are thus "not required to accord to

⁷⁸Dominican Republic's appellant's submission, para. 79.

⁷⁹Prior to *EC – Hormones*, an Article 11 claim was raised on appeal in *US – Wool Shirts and Blouses*, but that claim dealt solely with "whether Article 11 of the DSU entitles a complaining party to a finding on each of the legal claims it makes to a panel". (Appellate Body Report, *US – Wool Shirts and Blouses*, p. 17, DSR 1997:I, 323, at 338) As such, the claim did not challenge the panel's "assessment of the facts of the case". In addition, in *Canada – Periodicals*, the appellant raised Article 11 when challenging the panel's reliance on a "hypothetical example" to make a determination of "like products" under Article III:2 of the GATT 1994. (Appellate Body Report, *Canada – Periodicals*, p. 5, DSR 1997:I, 449, at 452) The Appellate Body, however, made no ruling as to the panel's compliance with Article 11. (*Ibid.*, pp. 20-23, DSR 1997:I, 449, at 465-468)

⁸⁰Appellate Body Report, *EC – Hormones*, para. 133.

⁸¹*Ibid.*, para. 132.

⁸²Appellate Body Report, *EC – Asbestos*, para. 161. See also, for example, Appellate Body Report, *EC – Tube or Pipe Fittings*, para. 125; Appellate Body Report, *EC – Bed Linen (Article 21.5 – India)*, paras. 170, 177, and 181; Appellate Body Report, *EC – Sardines*, para. 299; Appellate Body Report, *Korea – Alcoholic Beverages*, paras. 161-162; Appellate Body Report, *Japan – Agricultural Products II*, paras. 141-142; Appellate Body Report, *US – Wheat Gluten*, para. 151; Appellate Body Report, *Australia – Salmon*, para. 266; and Appellate Body Report, *Korea – Dairy*, para. 138.

factual evidence of the parties the same meaning and weight as do the parties"⁸³ and may properly "determine that certain elements of evidence should be accorded more weight than other elements".⁸⁴

79. Consistent with this margin of discretion, the Appellate Body has recognized that "not every error in the appreciation of the evidence (although it may give rise to a question of law) may be characterized as a failure to make an objective assessment of the facts."⁸⁵ When considering claims under Article 11 of the DSU, the Appellate Body does not "second-guess the Panel in appreciating either the evidentiary value of ... studies or the consequences, if any, of alleged defects in [the evidence]".⁸⁶ Indeed:

[i]n assessing the panel's appreciation of the evidence, we cannot base a finding of inconsistency under Article 11 simply on the conclusion that we might have reached a different factual finding from the one the panel reached. Rather, we must be satisfied that the panel has exceeded the bounds of its discretion, as the trier of facts, in its appreciation of the evidence.⁸⁷

Where participants challenging a panel's fact-finding under Article 11 have failed to establish that a panel exceeded the bounds of its discretion as the trier of facts, the Appellate Body has not interfered with the findings of the panel.⁸⁸

80. The Dominican Republic alleges that the Panel erred in its appreciation of Exhibits DR-8 and DR-29 because: (1) the Panel "misread"⁸⁹ a letter from the *Dirección General de Impuestos Internos* ("DGII") dated 6 April 2004 ("Memo DAT-No. 46", included in Exhibit DR-8)⁹⁰, confusing the stamps of half a cent (discontinued) and the current stamps of RD\$0.50 in attributing to the half a cent stamps the reasons why the RD\$0.50 stamps are forged; (2) the Panel "misunderstood the

⁸³Appellate Body Report, *Australia – Salmon*, para. 267.

⁸⁴Appellate Body Report, *EC – Asbestos*, para. 161.

⁸⁵Appellate Body Report, *EC – Hormones*, para. 133.

⁸⁶Appellate Body Report, *EC – Asbestos*, para. 177 (quoting Appellate Body Report, *Korea – Alcoholic Beverages*, para. 161).

⁸⁷*Ibid.*, para. 159 (quoting Appellate Body Report, *US – Wheat Gluten*, para. 151).

⁸⁸See, for example, Appellate Body Report, *EC – Bed Linen (Article 21.5 – India)*, para. 170; Appellate Body Report, *US – Carbon Steel*, para. 142 (quoting Appellate Body Report, *US – Wheat Gluten*, para. 151).

⁸⁹Dominican Republic's appellant's submission, para. 83. See also *ibid.*, paras. 84-85.

⁹⁰Apart from Memo DAT-No. 46, Exhibit DR-8 submitted by the Dominican Republic to the Panel comprises a compilation of documents providing information on a batch of alcoholic beverages seized in a commercial establishment in July 2001.

proposition for which Exhibit DR-8 was offered"⁹¹; (3) the Panel "disregarded"⁹² the evidence in Exhibit DR-29⁹³; and (4) the Panel erred in concluding "that Exhibits DR-8 and DR-29 do not establish a causal link between allowing stamps to be affixed abroad and forgery of tax stamps."⁹⁴

81. As regards the first allegation of the Dominican Republic (misreading Memo DAT-No. 46), we do not see in the Panel's treatment of Memo DAT-No. 46 any error that would amount to a violation of Article 11 of the DSU. The Panel did not give "conclusive"⁹⁵ weight to Memo DAT-No. 46 in considering whether forgery of tax stamps is possible, justifying its position on two bases: first, Memo DAT-No. 46 does not definitely establish that the tax stamps referred to therein were forged, as, in that letter, "the Department of Alcohol and Tobacco of the DGII explicitly states that only the National Treasury would be in a position to confirm whether a set of stamps were forged"⁹⁶; secondly, the seizure documented in Exhibit DR-8 occurred in the year 2001, whereas, in Memo DAT-No. 46, "the doubts expressed about the stamps refer to the format of stamps since 2002."⁹⁷ In our view, the approach followed by the Panel and its decision not to give "conclusive" weight to Memo DAT-No. 46 fall within its margin of discretion as the trier of facts and are, therefore, consistent with the obligations of panels set out in Article 11 of the DSU. We acknowledge that the Panel, in its description of Memo DAT-No. 46, appears to have confused the stamps of half a cent (discontinued) and the current stamps of RD\$0.50, in attributing to the half cent stamps details suggesting forgery of the RD\$0.50 stamps. However, this did not play a role in the reasoning that led the Panel not to give conclusive weight to Memo DAT-No. 46. Accordingly, we are of the view that the Panel did not commit an error in the appreciation of the evidence that "may be characterized as a failure to make an objective assessment of the facts."⁹⁸

82. The Dominican Republic also submits that the Panel "misunderstood the proposition for which Exhibit DR-8 was offered"⁹⁹, because "[t]he Panel ... incorrectly focused on the relationship between smuggling and forgery"¹⁰⁰, whereas "Exhibit DR-8 was offered as evidence of (a) smuggling

⁹¹Dominican Republic's appellant's submission, para. 87.

⁹²*Ibid.*, para. 89.

⁹³Exhibit DR-29 submitted by the Dominican Republic to the Panel contains information on a batch of garlic and alcoholic beverages seized in March 2002.

⁹⁴Dominican Republic's appellant's submission, para. 91.

⁹⁵Panel Report, para. 7.223.

⁹⁶*Ibid.*

⁹⁷*Ibid.*

⁹⁸Appellate Body Report, *EC – Hormones*, para. 133.

⁹⁹Dominican Republic's appellant's submission, para. 87.

¹⁰⁰*Ibid.*, para. 88.

and, separately, (b) forgery of tax stamps of a product in respect of which the Dominican Republic allows stamps to be affixed outside its territory."¹⁰¹ In our view, the Panel did not act in a manner inconsistent with Article 11 of the DSU in not finding that Memo DAT-No. 46 "adds any conclusive elements as relate to the relationship between the seizure of alcoholic beverages and the possible forgery of tax stamps".¹⁰² A panel does not act in a manner inconsistent with Article 11 of the DSU simply because it draws inferences from some of the evidence that do not coincide with the reason for which a party adduced it.¹⁰³

83. Thirdly, the Dominican Republic contends that, "[w]ith respect to Exhibit DR-29, the Panel simply disregarded the evidence therein"¹⁰⁴, but offers no reason in support of this assertion. We have no reason to conclude that the Panel did not examine Exhibit DR-29. On the contrary, the Panel noted that Exhibit DR-29 "contain[s] information on a batch of garlic and alcoholic beverages seized in March 2002"¹⁰⁵, which suggests that the Panel did consider the evidence therein. The Dominican Republic may object to the fact that the Panel did not ascribe as much weight to Exhibit DR-29 as the Dominican Republic would have wished, but this cannot be characterized as a failure to make an objective assessment of the facts as required by Article 11 of the DSU. As to the Dominican Republic's assertion that the Panel referred to Exhibit DR-29 in the context of a statement it made on the forgery of tax stamps, whereas Exhibit DR-29 was to serve the purpose of demonstrating that alcoholic beverages are being smuggled, we observe that a panel does not act in a manner inconsistent with Article 11 of the DSU if it draws inferences from some of the evidence that do not coincide with the reason for which a party adduced it.

84. The Dominican Republic disagrees with the Panel's position that Exhibits DR-8 and DR-29 do not establish a causal link between allowing stamps to be affixed abroad and forgery of tax stamps. It contends that such a causal link exists, basing its contention on an inference it draws from evidence of smuggling and forgery of tax stamps with respect to alcohol products.¹⁰⁶ However, a mere divergence of views between a party and a panel on the inferences to be drawn from pieces of evidence is not a sufficient ground to conclude that the Panel failed to "make ... an objective assessment of the facts of the case". The Dominican Republic has not explained why the divergence

¹⁰¹Dominican Republic's appellant's submission, para. 88.

¹⁰²Panel Report, para. 7.223.

¹⁰³Appellate Body Report, *Australia – Salmon*, para. 267.

¹⁰⁴Dominican Republic's appellant's submission, para. 89.

¹⁰⁵Panel Report, para. 7.224.

¹⁰⁶The Dominican Republic made this clarification in response to our questioning at the oral hearing. According to the Dominican Republic, Exhibits DR-8 and DR-29 relate to "tax evasion, smuggling, and forgery of tax stamps with respect to alcohol products". (Dominican Republic's appellant's submission, para. 79)

of views between it and the Panel on the inferences to be drawn from Exhibits DR-8 and DR-29 would amount to a failure to "make ... an objective assessment of the facts of the case". Therefore, we are of the opinion that the Panel did not act in a manner inconsistent with Article 11 of the DSU in stating that it "finds no supporting evidence in Exhibits DR-8 and DR-29 to the Dominican Republic's assertion that there is a causal link between allowing stamps to be affixed abroad and the forgery of tax stamps."¹⁰⁷

85. In sum, we conclude that the Panel did not fail to comply with the obligations set out in Article 11 of the DSU in respect of Exhibits DR-8 and DR-29. Accordingly, we *find* that the Panel did not fail to make an objective assessment of the facts of the case, as required by Article 11 of the DSU, in its appreciation of the evidence in Exhibits DR-8 and DR-29.

VI. Article III:4 of the GATT 1994 and the Bond Requirement

86. We now move to consider Honduras' appeal regarding the application of Article III:4 of the GATT 1994 to the requirement, imposed by the Dominican Republic, that importers and domestic producers of cigarettes post a bond to ensure payment of taxes (the "bond requirement"). The Panel found that "the bond requirement is applied in an equal manner, both formally and in practice, to domestic and imported cigarettes"¹⁰⁸, and that "Honduras has failed to establish that the bond requirement ... accords less favourable treatment to imported cigarettes than that accorded to the like domestic products, in a manner inconsistent with Article III:4 of the GATT 1994."¹⁰⁹

87. In reaching this conclusion, the Panel noted that the Dominican Republic's tax law imposes the requirement to post a bond on both importers and domestic producers of cigarettes.¹¹⁰ The Panel rejected the argument of Honduras that the bond requirement creates a disincentive against importing cigarettes. The Panel reasoned that a local company that intends to sell cigarettes in the Dominican Republic has two options: either to buy from a domestic producer or to buy from an importer. In neither case would the local company need to post a bond, because the posting of a bond is requested only from manufacturers and importers.¹¹¹ Honduras also argued that the bond requirement results in

¹⁰⁷Panel Report, para. 7.226.

¹⁰⁸*Ibid.*, para. 7.310.

¹⁰⁹*Ibid.*, para. 7.311.

¹¹⁰*Ibid.*, para. 7.234; the amount of the bond is RD\$5 million for both importers and domestic producers: Article 14 of Decree 79-03, Exhibit HOND-4 submitted by Honduras to the Panel. The Panel noted that "[a]ccording to the evidence provided by Honduras, in the specific case of the importer of cigarettes from that country, the annual fee charged by the insurance company that issued the bond was RD\$84,000 (approximately US\$1,873)". (*Ibid.*, para. 7.299)

¹¹¹*Ibid.*, para. 7.282.

less favourable treatment for imported cigarettes because it serves to guarantee the payment of a tax (the "Selective Consumption Tax") that is fully collected upon importation. This is in contrast to domestic cigarettes, where payment of the Selective Consumption Tax does not fall due until the twentieth day of the month following that in which the cigarettes are sold. The Panel discarded this argument, finding that "the evidence available does not support Honduras' assertion that there is no liability that the bond requirement would serve to secure."¹¹² For the Panel, "the Dominican Republic ... demonstrated that its tax authorities have the legal powers to reassess and eventually readjust the applicable tax liabilities for a period of up to three years."¹¹³ Thus, the importer may be asked to make a new payment as a result of the readjustment, and the bond would serve to guarantee this payment.¹¹⁴ Furthermore, the Panel relied on a written declaration from the Director-General of Internal Taxes¹¹⁵ to find that, in the exercise of its enforcement powers, the Dominican Republic tax authorities regard the bond as a guarantee of compliance with internal tax obligations other than the Selective Consumption Tax.¹¹⁶ Finally, the Panel concluded that "Honduras has not presented evidence to support its argument that the different cost per unit generated by complying with the bond requirement has a detrimental impact on the competitive conditions for imported products in relation to domestic products in the Dominican Republic cigarette market."¹¹⁷

88. On appeal, Honduras challenges the Panel's conclusion that the bond requirement does not accord less favourable treatment in terms of Article III:4 of the GATT 1994. Honduras submits that the Panel failed to recognize that the bond requirement imposes an "extra burden" on imported products compared with domestic products. According to Honduras, the bond requirement secures only the payment of the Selective Consumption Tax¹¹⁸; whereas "an importer has to pay the amount due for the Selective Consumption Tax prior to importation and has to post a bond to secure a tax liability that has already been discharged", "the domestic producer has up to 20 days following the month in which the transaction was made to pay the Selective Consumption Tax."¹¹⁹ Honduras

¹¹²Panel Report, para. 7.292.

¹¹³*Ibid.*

¹¹⁴*Ibid.*

¹¹⁵Letter from the Director-General of Internal Taxes, Exhibit DR-12 submitted by the Dominican Republic to the Panel.

¹¹⁶Panel Report, paras. 7.291 and 7.293.

¹¹⁷*Ibid.*, para. 7.301.

¹¹⁸Honduras' other appellant's submission, para. 60.

¹¹⁹*Ibid.*, para. 63.

contends that "this lack of symmetry between the liabilities that bond secures ... constitutes an 'extra hurdle' or 'extra burden' for imported products."¹²⁰

89. Honduras also submits that the Panel erred because it evaluated the current per-unit cost of the bond fee for a specific importer in the light of its volume of imports for 2001-2003.¹²¹ According to Honduras, the Panel should have examined the conditions of competition established by the legislation, rather than the market situation in which the bond requirement was applied.¹²² In any event, Honduras notes that the bond requirement was introduced in March 2003 and argues that the per-unit cost determined by the Panel was incorrect, because it was based on the volume of imports in the years 2000-2002, and on the cost charged by financial institutions for a bond fee in 2004.¹²³ Honduras adds that, as the Panel did not determine the per-unit cost for domestic producers, it could not compare the per-unit costs between imported products and domestic like products. Accordingly, Honduras argues, the Panel "did not have any basis upon which to conclude that there was no less favourable treatment being accorded to imports."¹²⁴ Finally, Honduras submits that the Panel erred because it stated that the fact that a fixed expense (i.e., an expense not related to volume of production) may lead to different per-unit costs among supplier firms is not "in itself ... enough to conclude that the expense creates a less favourable treatment for imported products."¹²⁵

90. The Dominican Republic contests Honduras' appeal of the Panel's findings regarding the bond requirement under Article III:4 of the GATT 1994. The Dominican Republic contends that the Panel correctly concluded that the bond requirement does not modify the conditions of competition to the detriment of the imported cigarettes, and that it should not be presumed that any difference in the per-unit cost of the bond modifies the conditions of competition and is inconsistent with Article III:4. The Dominican Republic also submits that, in the event the Appellate Body reverses the Panel's finding regarding the bond requirement under Article III:4, the Appellate Body should nevertheless find that the bond requirement is justified under Article XX(d) of the GATT 1994.

91. In *Korea – Various Measures on Beef*, the Appellate Body stated that, under Article III:4 of the GATT 1994, the question of whether:

¹²⁰Honduras' other appellant's submission, para. 63.

¹²¹*Ibid.*, para. 33; Panel Report, paras. 7.299-7.300.

¹²²Honduras' other appellant's submission, paras. 30-42.

¹²³*Ibid.*, para. 44.

¹²⁴*Ibid.*, para. 45.

¹²⁵Panel Report, para. 7.300; Honduras' other appellant's submission, paras. 48-54.

... imported products are treated "less favourably" than like domestic products should be assessed ... by examining whether a measure modifies the *conditions of competition* in the relevant market to the detriment of imported products.¹²⁶

92. In *EC – Asbestos*, the Appellate Body said the following about "less favourable treatment" as embodied in Article III:4 of the GATT 1994:

The term "less favourable treatment" expresses the general principle, in Article III:1, that internal regulations "should not be applied ... so as to afford protection to domestic production". If there is "less favourable treatment" of the group of "like" imported products, there is, conversely, "protection" of the group of "like" domestic products.¹²⁷

93. Therefore, the question that a panel must answer in an analysis under Article III:4 is whether the measure at issue modifies the conditions of competition in the relevant market to the detriment of imported products. In other words, a measure accords less favourable treatment to imported products if it gives domestic like products a competitive advantage in the market over imported like products. In this respect, we note that the bond requirement applies equally to importers and domestic producers, and is fixed at RD\$5 million (indexed for inflation)¹²⁸ for both importers and domestic producers.¹²⁹

94. Honduras acknowledges that the bond requirement is imposed equally on importers and domestic producers, but nevertheless claims that it accords less favourable treatment to imported cigarettes. Honduras argues that the bond requirement imposes an "extra burden" on imported products compared with domestic products because, as far as importers are concerned, the secured tax liability is non-existent or smaller than that of domestic producers. We recognize that a measure that applies equally to importers and domestic producers might, in some circumstances, nevertheless be inconsistent with Article III:4 of the GATT 1994.¹³⁰ In this case, however, the Panel did not rely in its reasoning exclusively on the equal application of the bond requirement to importers and domestic producers. The Panel rejected Honduras' argument "that the bond requirement results in a less

¹²⁶Appellate Body Report, *Korea – Various Measures on Beef*, para. 137. (original emphasis)

¹²⁷Appellate Body Report, *EC – Asbestos*, para. 100.

¹²⁸The bond of RD\$5 million represents approximately US\$110,000.

¹²⁹Article 14 of Decree 79-03, Exhibit HOND-4 submitted by Honduras to the Panel.

¹³⁰We note that in *Korea – Various Measures on Beef*, the Appellate Body stated:

A formal difference in treatment between imported and like domestic products is ... neither necessary, nor sufficient, to show a violation of Article III:4.

(Appellate Body Report, *Korea – Various Measures on Beef*, para. 137)

favourable treatment for imported cigarettes, because for those cigarettes there is no liability that the bond requirement would serve to secure."¹³¹ The Panel did so on the basis of two findings of fact. First, the Panel found that the Dominican Republic tax authorities have the legal power to reassess and eventually adjust the tax liabilities as they relate to the payment of the Selective Consumption Tax for a period of up to three years, and that the bond would serve to guarantee any payment resulting from the reassessment.¹³² Honduras does not make a claim under Article 11 of the DSU against this finding of fact. Hence, we do not disturb it.

95. Secondly, the Panel found that, in the exercise of their broad enforcement powers, the Dominican Republic tax authorities may use the bond to enforce tax liabilities other than the Selective Consumption Tax.¹³³ Honduras challenges this finding of fact under Article 11 of the DSU. In the next section of this Report, we explain why we reject this claim. As we find no reason to dispute the Panel's findings of fact regarding the reassessment of the Selective Consumption Tax and the possible uses of the bond, we consider that the Panel did not improperly reject Honduras' argument "that the bond requirement results in a less favourable treatment for imported cigarettes, because for those cigarettes there is no liability that the bond requirement would serve to secure".¹³⁴

96. Nor do we accept Honduras' argument that the bond requirement accords "less favourable treatment" to imported cigarettes because, as the sales of domestic cigarettes are greater than those of imported cigarettes on the Dominican Republic market, the per-unit cost of the bond requirement for imported cigarettes is higher than for domestic products.¹³⁵ The Appellate Body indicated in *Korea – Various Measures on Beef* that imported products are treated less favourably than like products if a measure modifies the conditions of competition in the relevant market *to the detriment of imported products*.¹³⁶ However, the existence of a detrimental effect on a given imported product resulting from a measure does not necessarily imply that this measure accords less favourable treatment to imports if the detrimental effect is explained by factors or circumstances unrelated to the foreign origin of the product, such as the market share of the importer in this case. In this specific case, the mere demonstration that the per-unit cost of the bond requirement for imported cigarettes was higher than for some domestic cigarettes during a particular period is not, in our view, *sufficient* to establish "less favourable treatment" under Article III:4 of the GATT 1994. Indeed, the difference between the

¹³¹Panel Report, para. 7.294.

¹³²*Ibid.*, para. 7.292.

¹³³*Ibid.*, para. 7.293.

¹³⁴*Ibid.*, para. 7.294.

¹³⁵Honduras' other appellant's submission, para. 70.

¹³⁶Appellate Body Report, *Korea – Various Measures on Beef*, para. 137.

per-unit costs of the bond requirement alleged by Honduras is explained by the fact that the importer of Honduran cigarettes has a smaller market share than two domestic producers¹³⁷ (the per-unit cost of the bond requirement being the result of dividing the cost of the bond by the number of cigarettes sold on the Dominican Republic market). In this case, the difference between the per-unit costs of the bond requirement alleged by Honduras does not depend on the foreign origin of the imported cigarettes. Therefore, in our view, the Panel was correct in dismissing the argument that the bond requirement accords less favourable treatment to imported cigarettes because the per-unit cost of the bond was higher for the importer of Honduran cigarettes than for two domestic producers.

97. Honduras also submits that the Panel erred because it evaluated the current per-unit cost of the bond fee for the importer of Honduran cigarettes in the light of the volume of imports for 2001-2003.¹³⁸ Honduras considers that the Panel's calculation is incorrect and that, in any event, it should also have calculated the per-unit cost for domestic producers. In our view, the Panel committed no error in seeking to make an illustrative evaluation of the per-unit cost of the bond fee with respect to the importer of Honduran cigarettes. First, we note that the Panel performed this exercise in response to Honduras' argument that the per-unit cost of the bond would be higher for the importer of Honduran cigarettes than for two domestic producers, because each of these domestic manufacturers has a larger market share than that of the importer of Honduran cigarettes.¹³⁹ Secondly, the calculation was merely illustrative: the Panel wanted a rough estimate of what the bond requirement meant for the importer of Honduran cigarettes in terms of cost. The Panel was not seeking to compare this cost with the per-unit cost of the bond for the two domestic producers, as it assumed, from the outset of its analysis, that the per-unit cost of the bond would be higher for the importer as a result of its smaller market share. Although methodologies other than that followed by the Panel might have produced more accurate results of the per-unit cost, the Panel was merely seeking to arrive at a rough estimate of the cost of the bond requirement to the importer and hence its approach was adequate for its purposes. The calculation carried out by the Panel shows that the bond requirement represents a very small cost for the importer—"equivalent to 0.2 per cent of the value of cigarette imports made by the importer in the year 2003."¹⁴⁰

¹³⁷Before the Panel, Honduras suggested that "since two domestic manufacturers have a higher market share than the importer of Honduran cigarettes, the per unit cost of the bond (the result of dividing the cost of the bond by the number of cigarettes sold) would be higher for imported cigarettes than for domestic cigarettes." (Panel Report, para. 7.295)

¹³⁸Honduras' other appellant's submission, para. 33; Panel Report, paras. 7.299-7.300.

¹³⁹Panel Report, para. 7.295.

¹⁴⁰*Ibid.*, para. 7.299.

98. In any event, the calculation on which Honduras focuses is not the thrust of the Panel's reasoning. For the Panel, a fixed expense, such as the annual fee for the bond, leads necessarily to different per-unit costs among supplier firms, to the extent that these firms have different volumes of production or volumes of sales. The Panel was of the view that "[a]s long as the difference in costs does not alter the conditions of competition in the relevant market to the detriment of imported products, that fact in itself should not be enough to conclude that the expense creates a less favourable treatment for imported products."¹⁴¹ We agree with the Panel, for the reasons explained above.¹⁴²

99. Accordingly, Honduras has not shown that the Panel erred in finding that the bond requirement does not accord less favourable treatment to imported cigarettes within the meaning of Article III:4 of the GATT 1994. Therefore, we *uphold* the Panel's finding, in paragraphs 7.311, 7.316, and 8.1(f) of the Panel Report, that Honduras failed to establish that the bond requirement accords less favourable treatment to imported cigarettes than that accorded to like domestic products, in a manner inconsistent with Article III:4 of the GATT 1994.

100. Finally, we observe that the Dominican Republic has argued that, in the event we reverse the Panel's finding regarding the bond requirement under Article III:4 of the GATT 1994, we should nevertheless find that the bond requirement is justified as necessary to ensure compliance with GATT-consistent laws and regulations under Article XX(d) of the GATT 1994. As we are of the view that the Panel committed no error in reaching its finding under Article III:4, there is no need for us to undertake an analysis of the Dominican Republic's defence under Article XX(d).

VII. Article 11 of the DSU and the Panel's Consideration of the Bond Requirement "As Such"

101. We next consider Honduras' appeal, under Article 11 of the DSU, regarding the Panel's assessment of Honduras' claim against the bond requirement. As discussed in the preceding section of this Report, a key argument by Honduras regarding the inconsistency of the bond requirement with Article III:4 of the GATT 1994 was that the bond requirement served to guarantee liability only for the Selective Consumption Tax and that such liability did not exist for importers, who must pay that tax in full at the time of importation.¹⁴³ The Dominican Republic responded that, notwithstanding payment of the Selective Consumption Tax at the time of importation, the bond nevertheless served to secure payment of that tax in the event of an adjustment of the taxpayers' total liability at some point in the future. The Dominican Republic also argued that:

¹⁴¹Panel Report, para. 7.300.

¹⁴²*Supra*, para. 96 of this Report.

¹⁴³See Panel Report, para. 7.284.

... although Article 376 of the Tax Code appears to refer only to the Selective Consumption Tax, in practice [the Dominican Republic] tax authority treats the bond as a guarantee of compliance with other internal tax obligations incumbent on the domestic producer and the importer of cigarettes, including the tax on the transfer of goods and services ("ITBIS") (Articles 335 through 360 of the Dominican Republic Tax Code), and the income tax (Articles 267 through 334 of the Dominican Republic Tax Code).¹⁴⁴

In support of this second argument, the Dominican Republic "presented a copy of a written declaration to that effect from its Director General of Internal Taxes."¹⁴⁵

102. The Panel accepted the arguments of the Dominican Republic and found "that the evidence available does not support Honduras's assertion that there is no liability that the bond requirement would serve to secure."¹⁴⁶ With respect to the Dominican Republic's assertion that the bond served to guarantee liabilities other than the Selective Consumption Tax, the Panel stated:

While the Dominican Republic has admitted that there is no explicit legal provision that authorizes the use of the bond as a guarantee of compliance for internal tax obligations other than the Selective Consumption Tax, the Panel finds that there is no reason to question its assertion that, in practice and in the exercise of its enforcement powers, the Dominican Republic tax authorities regard the bond as a guarantee of compliance for internal tax obligations such as the tax on the transfer of goods and services ("ITBIS") and the income tax.¹⁴⁷

103. On this basis the Panel concluded:

For the reasons expressed above, the Panel is not convinced by Honduras's argument that the bond requirement results in a less favourable treatment for imported cigarettes, because for those cigarettes there is no liability that the bond requirement would serve to secure.¹⁴⁸

104. On appeal, Honduras claims that the Panel failed to make an objective assessment of the matter before it, contrary to Article 11 of the DSU, in finding that the bond requirement secured obligations other than the Selective Consumption Tax. Honduras emphasizes that its claims relate to the bond requirement *as such*, independently from the application of that legislation in specific

¹⁴⁴Panel Report, para. 7.285.

¹⁴⁵*Ibid.*, para. 7.291.

¹⁴⁶*Ibid.*, para. 7.292.

¹⁴⁷*Ibid.*, para. 7.293.

¹⁴⁸*Ibid.*, para. 7.294.

circumstances.¹⁴⁹ According to Honduras, the Panel did not, however, consider the legislative basis of the bond requirement as such, but instead relied upon a letter from the Dominican Republic Director-General of Internal Taxes (referred to as Exhibit DR-12) that contradicted the terms of the underlying legislation. Honduras argues that, in analyzing its claim against the bond requirement as such, the Panel "should have properly examined only ... the terms of the legislation and [should] not have relied on the unsubstantiated views of one officer of an agency of the Dominican Republic."¹⁵⁰

105. Article 11 of the DSU provides that a panel "should make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements". The Appellate Body underlined in *Chile – Price Band System* that "Article 11 obliges panels not only to make 'an objective assessment of the facts of the case', but also 'an objective assessment of the matter before it'".¹⁵¹ The "matter" is constituted by both the facts of the case (and, in particular, the specific measures at issue) as well as the legal claims raised.¹⁵² The corollary is that a panel is not entitled to make an assessment of a matter that is *not* before it, for example, by making findings on a claim not raised by the complainant.¹⁵³

106. Honduras' appeal engages both dimensions of the Panel's duty under Article 11. Honduras asserts that the Panel failed to make an objective assessment of the *matter* before it by failing to consider its claims against the bond requirement *as such*. In addition, Honduras contests the Panel's treatment of the *evidence* before it and contends that the Panel erred in considering evidence that contradicted the terms of the legislation establishing the bond requirement. These two dimensions of Honduras' appeal under Article 11 of the DSU are woven together. The central thrust of Honduras' appeal is that the evidence relevant to its "as such" claim against the bond requirement is limited to the express terms of the legislation establishing that requirement.

107. In considering the first of the two dimensions of Article 11 raised in the appeal by Honduras, we observe that the Appellate Body has consistently affirmed the right of WTO Members to challenge legislation laying down norms or rules "as such", as well as their right to bring claims against the application of such measures in specific instances.¹⁵⁴ In our view, Honduras' claim before the Panel regarding the bond requirement was clearly in the nature of an "as such" claim. Indeed, as Honduras

¹⁴⁹Honduras' other appellant's submission, para. 14 (referring to Appellate Body Report, *US – Corrosion-Resistant Steel Sunset Review*, para. 82).

¹⁵⁰*Ibid.*, para. 22.

¹⁵¹Appellate Body Report, *Chile – Price Band System*, para. 172.

¹⁵²Appellate Body Report, *Guatemala – Cement I*, para. 73.

¹⁵³Appellate Body Report, *Chile – Price Band System*, para. 173.

¹⁵⁴See for example, Appellate Body Report, *US – 1916 Act*, paras. 60-61; and Appellate Body Report, *US – Corrosion-Resistant Steel Sunset Review*, para. 82.

emphasizes on appeal, the bond requirement had not been applied to its cigarette exporter at the time the Panel was established.¹⁵⁵ Having acknowledged this, however, we find no indication in the Panel Report to support the view that the Panel failed to consider the bond requirement as such, and instead undertook an analysis of a particular application or applications of the law.

108. We observe in this regard that the Panel said it would:

... consider the argument presented by Honduras in the sense that there is no liability that the bond requirement would serve to secure, as well as the two responses from the Dominican Republic: (i) that the bond serves as a guarantee of tax liabilities in the event of latter reassessments and adjustments of the tax liability of taxpayers; and, (ii) that it serves as a guarantee of compliance with internal tax obligations other than the Selective Consumption Tax.¹⁵⁶

This statement indicates that the Panel intended to undertake a general examination of the bond requirement, and, in particular, the types of tax liabilities that it serves to guarantee. In this statement, the Panel foreshadows an analysis of the characteristics of the measure as such. There is no indication in this statement that the Panel intended to consider particular applications of the measure at all.

109. After considering the issue, the Panel found that the bond requirement "would serve to guarantee" payment of Selective Consumption Tax not paid by an importer at the time of importation, in the event that the tax was reassessed and adjusted subsequent to importation.¹⁵⁷ In addition, the Panel found no reason to question the assertion of the Dominican Republic authorities that they "regard the bond as a guarantee of compliance for internal tax obligations such as the tax on the transfer of goods and services ('ITBIS') and the income tax."¹⁵⁸ Neither of these findings refers to a particular application of the bond requirement; rather, each is in the nature of a general finding regarding the obligations that the bond requirement, as such, secures. We therefore reject the argument of Honduras insofar as it asserts that the Panel failed to examine the bond requirement as such, as opposed to particular applications of the bond requirement.

110. We turn to the second dimension raised in the Article 11 appeal by Honduras and observe that much of Honduras' argument focuses not on the distinction between "as such" claims and "as applied" claims, but rather on the nature of the *evidence* that will be relevant to an "objective assessment" of an "as such" claim. Honduras thus contends that, because the "bond requirement stated unambiguously that the tax obligation secured by the bond was the Selective Consumption Tax, and

¹⁵⁵See Honduras' other appellant's submission, paras. 3 and 14.

¹⁵⁶Panel Report, para. 7.286.

¹⁵⁷*Ibid.*, para. 7.292.

¹⁵⁸*Ibid.*, para. 7.293.

nothing more", the "Panel should have ... examined only ... the terms of the legislation and [should] not have relied on the unsubstantiated views of one officer of an agency of the Dominican Republic."¹⁵⁹ In this way, a key basis for Honduras' assertion that the Panel failed to undertake the objective assessment required by Article 11 of the DSU is that "the Panel did not undertake an analysis of the legislation *alone*".¹⁶⁰

111. Honduras' argument in this regard takes issue with the Panel's treatment of the evidence before it. The Appellate Body has emphasized repeatedly that it is generally within the discretion of the Panel to decide which evidence it chooses to utilize in making findings and that the Appellate Body "will not interfere lightly with the panel's exercise of its discretion".¹⁶¹ We note also that, in *US – Carbon Steel*, the Appellate Body indicated that the analysis of a Member's municipal law (such as the bond requirement at issue in this dispute) requires a panel to consider and weigh the evidence put forward by the parties:

The party asserting that another party's municipal law, as such, is inconsistent with relevant treaty obligations bears the burden of introducing evidence as to the scope and meaning of such law to substantiate that assertion. Such evidence will typically be produced in the form of the text of the relevant legislation or legal instruments, which may be supported, as appropriate, by evidence of the consistent application of such laws, the pronouncements of domestic courts on the meaning of such laws, the opinions of legal experts and the writings of recognized scholars. The nature and extent of the evidence required to satisfy the burden of proof will vary from case to case.¹⁶²

112. Against this background, and consistent with the view expressed by the Appellate Body in *US – Carbon Steel*, we agree with Honduras that consideration of the express wording of the text of legislation establishing a measure is a fundamental element of an assessment of that legislation. That said, however, we see no merit in the proposition advanced by Honduras that a panel must limit itself, in considering a claim against legislation as such, *exclusively* to the wording of legislation itself. Indeed, in *US – Carbon Steel*, the Appellate Body recognized that different types of evidence may support assertions as to the meaning and scope of an impugned measure. A panel enjoys a margin of discretion in weighing such evidence, commensurate with its role as trier of fact.

¹⁵⁹Honduras' other appellant's submission, para. 22.

¹⁶⁰*Ibid.*, para. 23. (emphasis added)

¹⁶¹Appellate Body Report, *US – Wheat Gluten*, para. 151.

¹⁶²Appellate Body Report, *US – Carbon Steel*, para 157. (footnote omitted)

113. In this case, the Panel took into account the legal provision establishing the bond requirement as well as supplementary evidence, put forward by the Dominican Republic, in the form of a letter from the Dominican Republic Director-General of Internal Taxes.¹⁶³ The letter from the Director-General of Internal Taxes indicates that, in the exercise of their broad powers to enforce the tax laws, the Dominican Republic tax authorities may apply the proceeds of the bond toward payment of taxes other than the Selective Consumption Tax.¹⁶⁴ The position taken by the Director-General of Internal Taxes in the letter relates to the scope of its enforcement powers with respect to the uses to which the bond may be put; it is not an interpretative statement of Article 376 of the Tax Code. Honduras does not appear to have put forward evidence that would call into question or otherwise rebut the statements made in the letter of the Director-General of Internal Taxes concerning the scope of the enforcement powers of the Dominican Republic tax authorities. As the question of the possible uses to which the bond might be put was a contentious issue before the Panel, and because Exhibit DR-12 provided information relevant to this issue, we do not think that the Panel exceeded its margin of discretion in considering and giving some weight to that letter. Accordingly, we reject Honduras' claim that the Panel failed to meet its obligations under Article 11 of the DSU in its consideration of this issue.

114. Finally, we observe that the situation in this appeal is different from that prevailing in *India – Patents (US)*, upon which Honduras relies. *India – Patents (US)* was a case in which certain "administrative instructions" were held to be insufficient evidence of India's compliance with its obligations under the "mailbox" requirements of the *TRIPS Agreement*, whereas certain legislative provisions were clearly inconsistent with those obligations. The panel and the Appellate Body were not required in *India – Patents (US)* to interpret the words of the relevant legislation *alone*, in isolation from other evidence, as Honduras would have had the Panel do in this case. Indeed, in *India – Patents (US)*, there was a considerable amount of evidence available regarding the proper interpretation of the express terms of the Indian Patents Act, which included, but was not limited to, the text of the legislation itself. The panel in that case was thus able to balance India's assertion that its "administrative instructions"—which required officials to disregard certain mandatory provisions of the Patents Act—were sufficient to implement India's WTO obligations, against evidence that the Indian government itself considered that legislative amendment was necessary. Thus, in *India – Patents (US)*, the panel made full use of the record that was before it. Although the record in that case appears to have been considerably richer than the one available in these proceedings (which appears to consist only of the text of the measure and the letter from the Director-General of Internal Taxes), it

¹⁶³Exhibit DR-12 submitted by the Dominican Republic to the Panel.

¹⁶⁴See Panel Report, para. 7.291 (referring to Exhibit DR-12 submitted by the Dominican Republic to the Panel).

appears to us that the Panel in this case also considered all of the evidence that was before it. Accordingly, although the facts of this case differ from *India – Patents (US)*, the panels in each case followed the same—correct—approach in taking into account relevant factual information presented by the parties.

115. For all these reasons, we *find* that the Panel conducted an objective assessment of Honduras' claims regarding the bond requirement as such, consistent with Article 11 of the DSU.

VIII. The Panel's Treatment of Honduras' Contentions Regarding the Timing of Payment of the Selective Consumption Tax

116. We turn, finally, to address Honduras' appeal in respect of the Panel's treatment of its contentions regarding the timing of payment of the Selective Consumption Tax.

117. Before the Panel, Honduras claimed that the bond requirement accorded treatment less favourable to imported cigarettes than to domestic cigarettes contrary to Article III:4 of the GATT 1994. This was because, according to Honduras, the bond served to guarantee payment only of the Selective Consumption Tax. In the case of domestic producers, the Selective Consumption Tax is due on the twentieth day of the month following the taxable transaction. By contrast, in the case of imports, the Selective Consumption Tax is payable immediately upon importation. Accordingly, in the case of an importer, following importation there is simply no tax liability for the bond to secure.¹⁶⁵ Honduras submitted that this accorded less favourable treatment to imported cigarettes, compared to domestic production because:

[t]his accords domestic producers the opportunity to earn interest income on the Selective Consumption Tax for a period of 20-50 days. On the other hand, importers have to pay the Selective Consumption Tax in advance. This entails either financing costs or opportunity costs on the part of the importers.¹⁶⁶

118. Ultimately, the Panel rejected Honduras' claim under Article III:4 of the GATT 1994 in respect of the bond requirement on several grounds. It dealt with Honduras' contentions regarding the absence of tax liabilities for importers secured by the bond in two ways. First, it accepted the submissions of the Dominican Republic that, notwithstanding the payment of Selective Consumption Tax at the time of importation, the bond nevertheless served to secure tax obligations; these included payment of the Selective Consumption Tax in the case of reassessment and adjustment. The Panel also accepted that the tax authorities of the Dominican Republic regard the bond as security for

¹⁶⁵See Panel Report, paras. 7.268 and 7.284.

¹⁶⁶*Ibid.*, para. 7.268.

payment of taxes other than the Selective Consumption Tax.¹⁶⁷ Secondly, with respect to the possibility that domestic producers could earn interest on the value of the tax liability during the period between a taxable transaction and the moment when payment of the tax became due, while importers were forced to bear financing costs in respect of the tax paid at the time of importation, the Panel found this matter to be distinct from Honduras' claims in respect of the bond requirement.¹⁶⁸ It reasoned that, although the "claim on the bond requirement is part of the terms of reference of the Panel", there was "nothing in the request for establishment of the Panel that would lead to the conclusion that the Panel would be asked to make any finding regarding the difference in timing of the payment of the Selective Consumption Tax between domestic producers and importers."¹⁶⁹ The Panel concluded, therefore:

... that Honduras's claim regarding the different costs for domestic producers and importers arising from the time of payment of the Selective Consumption Tax is not directly related with the bond requirement and it is not within the Panel's terms of reference.¹⁷⁰

119. On appeal, Honduras submits that the Panel erred in treating its contentions regarding the timing of payment of the Selective Consumption Tax as a separate claim outside of the Panel's terms of reference. Honduras submits that these contentions were simply arguments in support of its claim that the bond requirement violated Article III:4 of the GATT 1994.¹⁷¹

120. We begin our analysis of this issue by observing that Article 6.2 of the DSU deals with the request for the establishment of a panel and provides, in relevant part, as follows:

The request for the establishment of a panel shall be made in writing. It shall indicate whether consultations were held, identify the specific measures at issue and provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly.

In *US – Carbon Steel*, the Appellate Body noted that Article 6.2 sets forth:

¹⁶⁷Panel Report, para. 7.293.

¹⁶⁸*Ibid.*, paras. 7.307-7.308.

¹⁶⁹*Ibid.*, para. 7.308.

¹⁷⁰*Ibid.*

¹⁷¹Honduras' other appellant's submission, paras. 76-81.

... two distinct requirements, namely identification of *the specific measures at issue*, and the provision of a *brief summary of the legal basis of the complaint* (or the *claims*). Together, they comprise the "matter referred to the DSB", which forms the basis for a panel's terms of reference under Article 7.1 of the DSU.¹⁷²

The Appellate Body has consistently maintained that, where a panel request fails to identify adequately particular measures or fails to specify a particular claim, then such measures or claims will not form part of the matter covered by the panel's terms of reference.¹⁷³

121. We also observe that the Appellate Body has consistently distinguished between the *claims* of a Member regarding the application of the various provisions of the *WTO Agreement*, and the *arguments* presented in support of those claims. Claims, which are typically allegations of violation of the substantive provisions of the *WTO Agreement*, must be set out clearly in the request for the establishment of a panel. Arguments, by contrast, are the means whereby a party progressively develops and supports its claims. These do not need to be set out in detail in a panel request; rather, they may be developed in the submissions made to the panel.¹⁷⁴

122. Against this background, the contentions of Honduras regarding the timing of payment of the Selective Consumption Tax may be characterized in two ways. First, insofar as the contentions regarding the timing of payment of the Selective Consumption Tax were made in support of Honduras' assertion that importers bore no tax liability that would be secured by the bond requirement, the contentions did—as Honduras submits on appeal—comprise *arguments* in support of its claims regarding the bond requirement. Nothing prevented Honduras from raising such arguments before the Panel, even though these arguments were not set out in the panel request.¹⁷⁵ Secondly, insofar as Honduras' contentions represent an assertion that the timing of payment of the Selective Consumption Tax resulted in a violation of Article III:4 of the GATT 1994 in itself, these contentions comprised a separate *claim* that was not included in the panel request. For the reasons that follow, however, regardless of the way in which Honduras' contentions in this regard are characterized, we see no error in the manner in which the Panel dealt with them.

123. In considering Honduras' claim under Article III:4 of the GATT 1994 regarding the bond requirement, the question presented to the Panel by Honduras was whether the bond requirement secured any liability for importers and whether the absence of such liability created an imbalance in

¹⁷²Appellate Body Report, *US – Carbon Steel*, para. 125. (original emphasis; footnote omitted)

¹⁷³See, for example, Appellate Body Report, *US – Carbon Steel*, para. 171.

¹⁷⁴Appellate Body Report, *EC – Bananas III*, para. 141.

¹⁷⁵See Request for Establishment of a Panel by Honduras, WT/DS302/5, 9 December 2003.

the conditions of competition between imported and domestic cigarettes. In addressing this issue, the Panel noted, in paragraph 7.284 of the Panel Report, Honduras' argument that, with respect to imported cigarettes, the Selective Consumption Tax is collected upon importation, whereas for domestic cigarettes, the tax may be paid up to the twentieth day of the month following that in which the sale is made. The Panel then indicated it would:

... consider the argument presented by Honduras in the sense that there is no liability that the bond requirement would serve to secure, as well as the two responses from the Dominican Republic: (i) that the bond serves as a guarantee of tax liabilities in the event of latter reassessments and adjustments of the tax liability of taxpayers; and, (ii) that it serves as a guarantee of compliance with internal tax obligations other than the Selective Consumption Tax.¹⁷⁶

124. In this way, the Panel Report shows that the Panel addressed Honduras' argument regarding the timing of payment for the Selective Consumption Tax and the two responses from the Dominican Republic as a whole. Ultimately, the Panel found that importers do bear liabilities that are secured by the bond. Thus, although the Panel did not consider specifically and in detail Honduras' contentions regarding the timing of payment of the Selective Consumption Tax in its analysis of the bond requirement, it reached a view on the facts that was sufficient for it to reject Honduras' theory that the bond secured no liabilities for importers. In that light, we do not believe that the Panel committed any error in the manner in which it dealt with the timing of payment of the Selective Consumption Tax, insofar as this was relevant to the question of whether the bond secures tax liability for importers. The Panel did not overlook or ignore the contentions advanced by Honduras on this point. Rather, the Panel Report reveals that the Panel bore these considerations in mind in the context of a global analysis of the question whether the bond secures tax liability for importers.

125. In any event, we note that there is no obligation upon a panel to consider each and every argument put forward by the parties in support of their respective cases, so long as it completes an objective assessment of the matter before it, in accordance with Article 11 of the DSU.¹⁷⁷

126. Nor do we see error in the Panel's finding that, insofar as Honduras' contentions represented a separate allegation of inconsistency with Article III:4 of the GATT 1994, those contentions were *claims* in respect of a measure not specified in the request for the establishment of the Panel. We also note, as pointed out by the Dominican Republic¹⁷⁸, that the issue of the timing of payment of the

¹⁷⁶Panel Report, para. 7.286.

¹⁷⁷Appellate Body Report, *EC – Poultry*, para. 135.

¹⁷⁸Dominican Republic's appellee's submission, para. 79.

Selective Consumption Tax is not dealt with in the legislative provisions identified by Honduras in connection with its claims against the bond requirement. In this light, we agree with the Panel that:

[w]hether imported cigarettes may be accorded less favourable treatment than the like domestic products due to the difference in the time of payment of the Selective Consumption Tax is ... a different issue from the bond requirement, although the two may be tangentially related. Although the bond would serve as a guarantee for the payment of the Selective Consumption Tax and other liabilities, if there was any challenge against the conditions for payment of the tax, that challenge would not have to do with the bond requirement, but with the rules on the tax itself. The time of payment of the Selective Consumption Tax is not part of the bond requirement.¹⁷⁹

127. Accordingly, because such a challenge was not included in the panel request, we see no error in the Panel's finding that such a matter was outside its terms of reference. For these reasons, we *find no error* in the Panel's treatment of Honduras' contentions regarding the timing of payment of the Selective Consumption Tax.

IX. Findings and Conclusions

128. For the reasons set out in this Report, the Appellate Body:

- (a) *finds no error* in the Panel's interpretation and application of the term "necessary" in Article XX(d) of the GATT 1994; *finds it unnecessary* to complete the analysis of the Dominican Republic's defence under Article XX(d) of the GATT 1994; and, consequently, *upholds* the Panel's finding, in paragraphs 7.232, 7.233 and 8.1(e) of the Panel Report, that the tax stamp requirement is not justified under Article XX(d) of the GATT 1994;
- (b) *finds* that the Panel made an objective assessment of the facts of the case, as required by Article 11 of the DSU, in its examination of Exhibits DR-8 and DR-29;
- (c) *upholds* the Panel's finding, in paragraphs 7.311, 7.316, and 8.1(f) of the Panel Report, that Honduras failed to establish that the bond requirement accords less favourable treatment to imported cigarettes than that accorded to like domestic products, in a manner inconsistent with Article III:4 of the GATT 1994;

¹⁷⁹Panel Report, para. 7.307.

- (d) *finds* that the Panel made an objective assessment of the matter before it, as required by Article 11 of the DSU, in its consideration of Honduras' claim against the bond requirement "as such"; and,
- (e) *finds no error* in the Panel's treatment of Honduras' contentions regarding the timing of payment of the Selective Consumption Tax.

129. At the oral hearing, the participants agreed that the tax stamp regime as a whole had been altered by a new decree in October 2004.¹⁸⁰ Both participants nevertheless requested the Appellate Body to rule on the WTO-consistency of the original measure. In view of the above, the Appellate Body *recommends* that the Dispute Settlement Body request the Dominican Republic to bring the tax stamp requirement, found in this Report and in the Panel Report as modified by this Report to be inconsistent with the GATT 1994, into conformity with its obligations under that Agreement if, and to the extent that, the said modifications to the tax stamp regime have not already done so.

130. The Appellate Body also *recommends* that the Dispute Settlement Body request the Dominican Republic to bring its other measures, found in the Panel Report as modified by this Report, to be inconsistent with the GATT 1994, into conformity with its obligations under that Agreement.

¹⁸⁰*Supra*, paras. 14 and 63 of this Report.

Signed in the original in Geneva this 7th day of April 2005 by:

Luiz Olavo Baptista
Presiding Member

John Lockhart
Member

Giorgio Sacerdoti
Member

ANNEX 1

**WORLD TRADE
ORGANIZATION**

WT/DS302/8
24 January 2005
(05-0297)

Original: English

**DOMINICAN REPUBLIC – MEASURES AFFECTING THE IMPORTATION
AND INTERNAL SALE OF CIGARETTES**

Notification of an Appeal by the Dominican Republic
under Article 16.4 and Article 17 of the Understanding on Rules
and Procedures Governing the Settlement of Disputes (DSU),
and under Rule 20(1) of the Working Procedures for Appellate Review

The following notification, dated 24 January 2005 , from the Delegation of the Dominican Republic, is being circulated to Members.

Pursuant to Articles 16.4 and 17.4 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 20 of the Working Procedures for Appellate Review, the Dominican Republic appeals certain issues of law and legal interpretation in the Panel Report in *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes* (WT/DS302/R).

1. The Dominican Republic believes that the Panel committed legal error in paragraphs 7.232, 7.233, and 8.1(e) of the Panel Report, by concluding that the Dominican Republic's "tax stamp requirement" (Article 37 of Decree 79-03 of 4 February 2003 and Decree 130-02 of 11 February 2002) is not justified under Article XX(d) of the GATT 1994.
 - a. The Panel erred in interpreting and applying the term "necessary" in Article XX(d). In this regard, the Dominican Republic intends to make arguments relating to the Panel's reasoning in, *inter alia*, paragraphs 7.213-7.230 of the Panel Report.
 - b. The Panel failed to make an objective assessment of the facts of the case, inconsistent with its duty under Article 11 of the DSU, by exceeding the bounds of its discretion in examining evidence submitted by the Dominican Republic regarding tax evasion, smuggling, and forgery of tax stamps. The Panel also failed to make an objective assessment of the facts regarding the lack of reasonably available alternative instruments. In this regard, the Dominican Republic intends to make arguments relating to the Panel's reasoning in, *inter alia*, paragraphs 7.221-7.226 and 7.228-7.229 of the Panel Report.

2. In the event that the Appellate Body reverses the Panel's conclusion that the tax stamp requirement is not justified under paragraph (d) of Article XX of the GATT 1994, the Dominican Republic requests that the Appellate Body complete the legal analysis under Article XX of the GATT 1994.

The provisions of the covered agreements that the Dominican Republic considers to have been erroneously interpreted or applied by the Panel include Article XX(d) of the GATT 1994 and Article 11 of the DSU.

ANNEX 2

**WORLD TRADE
ORGANIZATION**

WT/DS302/9
7 February 2005
(05-0517)

Original: English

**DOMINICAN REPUBLIC – MEASURES AFFECTING THE IMPORTATION
AND INTERNAL SALE OF CIGARETTES**

Notification of an Other Appeal by Honduras
under Article 16.4 and Article 17 of the Understanding on Rules
and Procedures Governing the Settlement of Disputes (DSU),
and under Rule 23(1) of the Working Procedures for Appellate Review

The following notification, dated 7 February 2005, from the Delegation of Honduras, is being circulated to Members.

Pursuant to Rule 23 of the Appellate Body's Working Procedures for Appellate Review, Honduras hereby notifies its decision to appeal to the Appellate Body certain issues of law covered in the Panel Report *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes*, WT/DS302/R, (the "Panel Report") and certain legal interpretations developed by the Panel in that Report.

Honduras seeks appellate review of:

- a) the Panel's findings and conclusion set out in paragraphs 7.291-7.294 that there are tax liabilities in addition to the Selective Consumption Tax that the bond requirement secures;
- b) the Panel's findings and conclusion, set out in paragraphs 7.297-7.301 of the Panel Report, that it was not demonstrated that the fixed amount of the bond accords to imported cigarettes treatment less favourable than that accorded to domestic cigarettes;
- c) the Panel's findings and conclusion, set out in paragraphs 7.306-7.308 of the Panel Report, that the difference in timing of the payment of the Selective Consumption Tax between domestic producers and importers in connection with the bond is not a matter within the Panel's terms of reference; and
- d) the Panel's conclusion, set out in paragraphs 7.310-7.311, that Honduras had failed to establish that the bond requirement accords less favourable treatment to imported cigarettes than that accorded to the like domestic products.

The above findings and conclusions are based on the following legal errors:

- the Panel did not make an objective assessment of the matter before it, namely, Honduras's challenge to the bond requirement on its face, because it examined the "application" of the bond requirement, contrary to Article 11 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") (paras. 7.291 – 7.294 of the Panel Report);
- the Panel erred in examining the market conditions in the Dominican Republic in order to determine the consistency of the bond requirement with Article III:4 of the *General Agreement on Tariffs and Trade 1994* ("GATT") (paras. 7.297 – 7.301 of the Panel Report);
- the Panel's error was compounded by the fact that the Panel made unsubstantiated assumptions with respect to the per-unit cost of the bond fee for importers, did not determine the per-unit cost of the bond fee for domestic producers and did not make the comparison between the per-unit costs for importers and domestic producers (paras. 7.297 – 7.301 of the Panel Report);
- the Panel erred in its finding that a difference in costs for importers of posting the bond do not alter the conditions of competition in the Dominican Republic's market and, therefore, do not create less favourable treatment for imported products within the meaning of Article III:4 of the GATT (paras. 7.297 – 7.301 of the Panel Report);
- the Panel failed to make a finding that importers face an additional burden compared to domestic producers, even though only importers have to post the bond and pay the Selective Consumption Tax upon importation, which is contrary to the requirement of Article III:4 of the GATT, (paras. 7.292 – 7.294 of the Panel Report); and
- the Panel erred in characterising the difference in timing of the payment of the Selective Consumption Tax in connection with the posting of the bond as a separate claim which was not within the terms of reference of the Panel (paras. 7.306 – 7.308 of the Panel Report).

Honduras requests the Appellate Body to reverse or modify, where appropriate, the findings or conclusions of the Panel. The provisions of the WTO Agreement that Honduras considers the Panel to have erroneously interpreted or applied are Article III:4 of the GATT and Article 11 of the DSU.
