BEFORE THE APPELLATE BODY
OF THE WORLD TRADE ORGANISATION

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

AB-2005-3

Third Participant Submission pursuant to Rule 24 (1) of the Working Procedures for Appellate Review by the European Communities

Geneva, 18 February 2005
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I. INTRODUCTION

1. The European Communities welcomes this opportunity to present its written observations in this case which is of systemic interest for the correct interpretation of the General Agreement on Tariffs and Trade (GATT) and of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU).

2. In its submission the European Communities concentrates on the following issues raised in the Dominican Republic’ appeal and Honduras’ cross-appeal:

   ➢ the Panel’ review of the tax stamp requirement under Article XX (d) GATT;

   ➢ the consistency of Panel’ findings on the bond requirement with Article 11 DSU;

   ➢ the Panel’s substantive review of the bond requirement under Article III:4 of the GATT.

II. EXECUTIVE SUMMARY

3. In the EC’ view, the Panel did not err in its findings that the Dominican Republic’ tax stamp procedure, which requires to affix tax stamps in the Dominican Republic in the presence of a tax officer is not justified under Article XX(d) of the GATT. In applying the “necessity” test as established by the Appellate Body in Korea – Various Measures on Beef the Panel correctly took into account the importance of the common interest and the contribution of the measure to the pursued objective. While the European Communities would not agree with the Panel’s assumption that the currently applied tax stamp requirement did not have had “intense” trade effect, this does not affect the eventual Panel findings which correctly conclude that the same objective could be achieved with less trade-restrictive alternative measures.

4. The European Communities considers that the Panel made an objective assessment of the “matter” under Article 11 of the DSU by taking into account not only the
legislative but also further practical purposes of the bond requirement. The "matter" within the meeting of Article 11 of the DSU is in the first place defined by Honduras Panel request. This request refers also to "practices" related to the bond requirement and any such practice was, therefore, part of the "matter" before the Panel. The fact that Honduras was not aware of this practice and, consequently, sought to exclude the "practices" from the scope of the "matter" is a question of litigation tactics to which the Panel was not bound. Moreover, the Appellate Body has established a general rule that a Panel should consider all relevant evidence in resolving the dispute.

5. Finally, the Panel was correct in finding that the fees incurred by the bond requirement did not result in a "less favourable treatment" of the imported goods, given that it is identical for the group of importers and domestic producers and in the light of its marginal and negligent impact.

III. THE PANEL' REVIEW OF THE TAX STAMP REQUIREMENT UNDER ARTICLE XX(d) OF THE GATT

A. The finding of the Panel and the arguments by the Dominican Republic on appeal

6. The Panel found that the tax stamp requirement, which requires to affix tax stamps in the Dominican Republic in the presence of a tax officer was inconsistent with Article III:4 of the GATT.\footnote{Panel Report, Dominican Republic – Import and Sale of Cigarettes, paras. 7.162 et seq.} The Panel went on to analyze whether the measure could be justified under Article XX(d) of the GATT. In assessing whether the tax stamp procedure as applied by the Dominican Republic was "necessary" under Article XX(d) of the GATT the Panel took into account several aspects, i.e.

➢ That the tax stamp procedure did not have had "any intense restrictive effects on trade"\footnote{Panel Report, Dominican Republic – Import and Sale of Cigarettes, para. 7.215.};
That the evidence presented by the Dominican Republic on the risk of forgery in case tax stamps are allowed to be affixed abroad was insufficient;

That alternative means could achieve the same level of enforcement of tax collection and prevention of cigarette smuggling.

7. In its appeal, the Dominican Republic argues that the Panel did not properly apply the test under Article XX(d) of the GATT as set out by the Appellate Body in Korea – Various Measures on Beef. The Panel did not assess the relative weight of the importance of the protected interest, namely to prevent tax evasion, smuggling and forgery of tax stamps, the minimal trade impact of the Dominican Republic’ measure and its contribution to achieve the protected interest. Moreover, the Panel did not accurately analyze that alternative measures and wrongly concluded that they would not secure an equivalent level of protection compared to the current tax stamp regime. Finally, the Dominican Republic objects that the Panel did not take into account that its tax stamp regime contributes to its citizen’s health by preventing tax evasion, smuggling and forgery.

B. The legal framework

8. The European Communities would note from the outset that the Dominican Republic’ appeal is limited to the correct application of the “necessity” test under

3 Ibid., para. 7.226.
4 Ibid., para. 7.228.
6 Dominican Republic, Appellant’s Submission, para. 20, paras. 37 et seq.
7 Ibid, para. 21, paras. 34 et seq.
8 Ibid, para. 22, paras. 41 et seq.
9 Ibid., para. 30, paras. 47 et seq.
10 Ibid., para. 39, 46.
Article XX(d) of the GATT as interpreted by the Appellate Body. Conversely, the Dominican Republic does not argue that the Appellate Body should further elaborate the general concept of the term “necessary” under Article XX(d) of the GATT.

9. The European Communities would recall that the Appellate Body Report, Korea – Various Measures on Beef established the following test for determining whether a measure was “necessary” under Article XX(d) of the GATT:

In appraising the “necessity” of a measure in these terms, it is useful to bear in mind the context in which “necessary” is found in Article XX(d). (...) Clearly, Article XX(d) is susceptible of application in respect of a wide variety of “laws and regulations” to be enforced. It seems to us that a treaty interpreter assessing a measure claimed to be necessary to secure compliance of a WTO-consistent law or regulation may, in appropriate cases, take into account the relative importance of the common interest or values that the law or regulation is intended to protect. 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.

There are other aspects of the enforcement measure to be considered in evaluating that measure as “necessary”. One is the extent to which the measure contributed to the realization of the end pursued, the securing of compliance with the law or regulation at issue. The greater the contribution, the more easily a measure might be considered to be “necessary”. Another respect is the extent to which the compliance measure produces restrictive effects on international commerce, that is, in respect of a measure inconsistent with Article III:4, restrictive effects on imported goods. A measure with a slight impact upon imported products might more easily be considered as “necessary” than a measure with intense or broader restrictive effects.

In sum, determination of whether a measure, which is not “indispensable”, may nevertheless be “necessary” within the contemplation of Article XX(d), 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.11 (Underlining added)

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11 Appellate Body Report, Korea – Various Measures on Beef, paras. 162 et seq. (footnotes omitted)
10. It is noteworthy that the Appellate Body’s list of factors is not exhaustive but it may be modified or complemented in the light of specific circumstances. In this context, the European Communities would emphasize the Appellate Body finding whereby

(...) the weighing and balancing process we have outlined above is comprehended in the determination of 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”.

11. The Panel in *Canada – Wheat Exports and Grain Imports* accurately summarized the Appellate Body jurisprudence on this point as follows:

The Appellate Body has indicated that relevant factors for determining whether an alternative measure is “reasonably available” are: (i) the extent to which the alternative measure “contributes to the realization of the end pursued”; (ii) the difficulty of implementation; and (iii) the trade impact of the alternative measure compared to that of the measure for which justification is claimed under Article XX. The Appellate Body has also stated that, in addition to “being reasonably available”, the alternative measure must also achieve the level of compliance sought. In this regard, the Appellate Body has recognized that “Members of the WTO have the right to determine for themselves the level of enforcement of their WTO-consistent laws and regulations.”

C. Review of the Panel findings

12. In the EC’ view, the Panel adequately addressed all the elements for the “necessity test” under Article XX(d) of the GATT. While it is true that the Panel did not each time attribute a specific weight to the particular elements of the necessity test the European Communities considers that this methodological approach does not
result in an error of law because the Panel’s overall reasoning demonstrates that all pertinent elements had been considered and properly “weighed and balanced”.14

1. The importance of the common interest

13. In respect of the importance of the common interest the Panel concluded the following:

The Panel finds no reason to question the Dominican Republic’s assertion in the sense that the collection of tax revenue (and conversely, the prevention of tax evasion) is a most important interest for any country and particularly for a developing country such as the Dominican Republic.15

14. The European Communities considers that the Panel thus took into account the importance of the value of the common interest. Indeed, the Panel explicitly attributed the same weight to this objective as suggested by the Dominican Republic. That said, contrary to what the Dominican Republic appears to believe, this conclusion is of course not sufficient to justify a measure. The “necessity” test entails a rather comprehensive analysis and it would therefore be mistaken to single out one element to the detriment of the others. In this context, the European Communities would also caution to overestimate the general Appellate Body’ findings whereby it would be “easier” to justify a measure if, for instance, the objective is of high value or if the measure is less trade-restrictive. What matters is the concrete case. Thus, before reaching a conclusion on whether a measure is “necessary” all elements should be properly analyzed.

15. Furthermore, the European Communities would take issue with the Dominican Republic’ attempt to introduce a new common objective for the justification of the measure. The Dominican Republic has asserted that its tax stamp requirement procedure not only prevents tax evasion, forgery and smuggling but contributes

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14 While the European Communities believes that a presentational approach taken by the Panel in US – Gambling, paras. 6.488 et seq. would have avoided certain misunderstandings this format is not mandatory for the assessment of the measure.

also to the protection of the health of citizen.\textsuperscript{16} In the EC' view, this novel objective is irrelevant. Indeed, if the Dominican Republic was really concerned about the public health in respect of its tax stamp requirement it should rather have made an argument under Article XX(b) of the GATT. Furthermore, the European Communities fails to see how the specific procedural requirement for affixing tax stamps on cigarettes in the presence of a tax officer, will in any way improve the public health. If the Dominican Republic's concern is an increase in smuggling, and therefore an eventual increase of consumption, the European Communities would submit that smuggling typically implies that cigarettes do not contain any tax stamps at all. This occurs, of course, independent on whatever procedure for affixing tax stamps a country provides for. The European Communities, therefore, considers that the protection of health is not an issue in this case.

2. Contribution of the measure to the end pursued

16. The Panel addressed the issue on whether the presence of tax authority inspectors contributed to the prevention of tax evasion, smuggling and forgery in considerable detail. The Panel concluded that on the basis of the evidence provided by the Dominican Republic

\[\ldots\] that other factors, such as security features incorporated into the tax stamps (to avoid forgery of stamps or make it more costly) and police controls on roads and different commercial levels (such as at the points of production, introduction into the country, distribution, and sale), may play a more important role in preventing the forgery of tax stamps, the tax evasion, and the smuggling of tobacco products.\textsuperscript{17}

17. Thus, the Panel did not consider that the presence of tax authorities while affixing stamps was as important for the achievement of the objective as the Dominican Republic suggested.

18. Without prejudice to the relevance of the evidence submitted by the Dominican Republic and which the European Communities is not in a position to assess, the

\textsuperscript{16} Ibid., paras. 46, 39, 20.

\textsuperscript{17} Panel Report, \textit{Dominican Republic – Import and Sale of Cigarettes}, para. 7.226.
European Communities would concur with the Panel’s analysis. The European Communities considers that it is rather unrealistic that the sheer presence of a tax office in a manufacturing facility may prevent deceptive trade practices. It is hardly conceivable that a tax officer could control the whole affixation process for each cigarette package which, therefore, would still leave room for smuggling, forgery and tax evasion.

19. In this context, the European Communities would not comment on the Dominican Republic’s allegation that the British American Tobacco (BAT), the biggest importer of cigarettes into the Dominican Republic, is actively colluding in deceptive practices. However, even if this were true the European Communities would for the reasons mentioned above fail to see how the presence of a tax officer would prevent the company from continuing these illegal practices.

20. The European Communities would, therefore, find no error in law by the implicit Panel’s findings that the tax affixation procedure does not contribute to the achievement of the end pursued to the extent the Dominican Republic ascribes to it.18

3. Trade restrictive effect of the measure

21. The Panel’s findings regarding the trade effect of the tax stamp requirement applied by the Dominican Republic are not entirely conclusive:

The Panel also notes that, although it has already found that the tax stamp requirement modifies the conditions of competition in the marketplace to the detriment of imported cigarettes, Honduras has still been able to export cigarettes to the Dominican Republic and, in fact, its exports have increased quite significantly over the last few years. So the Panel may assume that the measure has not had any intense restrictive effects on trade.19

18 Cf. Dominican Republic, Appellant’s Submission, para. 45: “The Dominican Republic’s tax stamp requirement contributes greatly [importantly] to the goal of preventing tax evasion, smuggling, and forgery of tax stamps in cigarettes. (Emphasis added), See also ibid., para. 46.

22. Thus, it is not entirely clear to the European Communities whether the Panel actually conceded that the Dominican Republic’s tax stamp requirement had no "intense restrictive effects on trade" or whether the Panel merely proceeded with an assumption in favor of the Dominican Republic’s argument.

23. Be it as it may, the European Communities would not agree with such a conclusion or assumption. Even if imports of cigarettes from Honduras into the Dominican Republic increased by more than 80% in 2003, this would not give any indication about the lost sales due to the tax stamp requirement process. Indeed, as this process is rather cumbersome one would assume that the increase of imports would have been even higher in the absence of this measure. However, given that the Panel correctly weighed the other elements, and in particular the existence of alternative measures as will be demonstrated below, the European Communities considers that this assumption by the panel did not affect its eventual findings.

4. Alternative less trade restrictive measures

24. The crucial element in the Panel’s conclusion was the existence of less trade restrictive alternative measures. Thus, the Panel found:

Since the Dominican Republic has not proved why other, reasonably available, less-GATT inconsistent, measures would not be able to achieve the same level of enforcement that it has chosen to attain, it is the Panel’s opinion that the Dominican Republic has not proven that the tax stamp requirement is a measure which is necessary to secure compliance with the Dominican Republics tax laws and regulations.\(^{21}\)

25. The Dominican Republic essentially argues that the Panel failed to assess the contribution of the alternative measure for the pursued objective and the trade consequences of its implementation, resulting in a improper weighing and balancing.\(^{22}\)

\(^{20}\) Dominican Republic, Appellant’s submission, para. 35.

\(^{21}\) Panel Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 7.230.

\(^{22}\) Dominican Republic, Appellant’s submission, paras. 52 et seq.
26. The European Communities is not convinced by the arguments advanced by the Dominican Republic and it would, therefore, concur with the Panel findings.

27. From the outset, the European Communities would reiterate that the objective to prevent smuggling of cigarettes has no place in the present case. As already noted, "smuggling" entails that cigarettes are sold without any tax stamps. This is a completely different issue compared to the question at hand whether tax stamps shall be affixed in the presence of the tax authority or whether alternatively, as suggested by the Panel, tax stamps could be sold and affixed abroad. Indeed, under both procedures, tax stamp would eventually be affixed on the cigarettes packages while in the case of smuggling cigarettes would be sold without any tax stamps. In the EC's view, smuggling may occur independent of the specific tax stamp procedure, and the European Communities fails to see how the one or the other affixation procedure may facilitate or prevent smuggling.

28. The European Communities takes note of the Dominican Republic's chosen level of protection against tax evasion and forgery, i.e. the "zero tolerance" policy. However, the European Communities considers that less-trade restrictive alternative means are reasonably available to achieve the same objective. As already noted in its Oral statement before the Panel, the European Communities considers that such an alternative measure could consist in selling stamps to authorized producers.

29. The sale of tax stamps abroad to an authorized manufacturer is a very commonly used practice in order to secure that imported cigarettes fulfill the necessary tax requirements. The risk of forgery is minimal. First, the tax authorities selling the stamps can exactly backtrack to whom they have sold the tax stamps. In the case of the Dominican Republic this might be even easier as most of the imported cigarettes come from one single importer (i.e. BAT) located in Honduras. Second,

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23 The risk of smuggling seems to be one of the major concerns for the Dominican Republic, see Dominican Republic, Appellant's submission, paras. 56 et seq.

24 Cf. Dominican Republic, Appellant's submission, paras. 55.

25 EC Oral Statement, para. 15.
the authorized manufacturer has no interest in forgery as he might lose the authorization for purchasing tax stamps. Third, a manufacturer would have normally paid for the tax stamps before affixing them, thus, he has also in interest in using these stamps.

30. The European Communities considers that any remaining risk of forgery could be adequately addressed by security features on the tax stamps and controls. In this respect, it is noteworthy that tax stamps may contain security elements comparable to banknotes and which are extremely difficult to copy.

31. The European Communities does not consider that such a measure would raise implementation difficulties. Arguably, border controls should be strengthened. But this does not necessarily imply new resources given that it would be unnecessary to provide for tax officers in the local manufacturing facility.

32. Finally, the European Communities is convinced that the alternative measure would be less trade restrictive than the current Dominican Republic's regime which involves considerable manufacturing steps for affixing tax stamps on cigarettes that have already completed the production process including packaging. It appears self-evident that it is more economical to pack cigarettes and to affix tax stamps in one production process at one place instead of having two separate procedures at two different locations.

D. Conclusion

33. For these reasons, the European Communities considers that the Panel did not err in its finding that the Dominican Republic's requirement to provide for the presence of tax authorities while affixing tax stamps on cigarettes, is not "necessary" under Article XX(d) of the GATT.
IV. THE PANEL’S REVIEW OF THE CONSISTENCY OF THE BOND REQUIREMENT UNDER ARTICLE 11 OF THE DSU

34. In its cross appeal, Honduras claims that the Panel failed to make an objective assessment of the “matter” in accordance with Article 11 of the DSU, i.e. the Dominican Republic’ legislation for the bond requirement “as such”. Honduras argues that the Panel did not only look at the legislation “as such” but also at its actual application, namely that the bond requirement serves in practice more purposes than provided for under the legislation.26

35. The Panel found:

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.

For the reasons expressed above, the Panel is not convinced by 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.27

36. Article 11 of the DSU provides in relevant part:

[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 (…).

37. Article 11 of the DSU does not further qualify the term “matter”. However, in the present case the European Communities would note that Honduras’ Panel request was very broadly formulated:

26 Honduras, Other Appellant’s submission, paras. 20 et seq.

27 Panel Report, Dominican Republic – Import and Sale of Cigarettes, paras. 7.293 et seq.
The Dominican Republic requires importers of cigarettes to post a bond pursuant to Article 14 of the Regulations. This requirement and the laws, regulations and practices implementing this requirement entail costs and administrative burdens hindering the importation of cigarettes and are therefore in the view of Honduras inconsistent with Article II:1(a) and (b) and Article XI:1 of the GATT, or – if they were deemed to be internal measures – inconsistent with Article III/2 and Article III:4 of the GATT.28

38. Thus, as Honduras’ Panel request also refers to “practices” under the bond requirement they constitute part of the “matter” under Article 11 of the DSU. For this reason alone, the Panel was, therefore, called upon to take all elements into account in order to make an “objective assessment” of the matter.

39. The European Communities understands that Honduras only learned about certain practices in the course of the proceedings and consequently tried to limit its claim to the legislative text. However, as the “matter”, including the relevant practices was already before the Panel the European Communities considers that this limitation was a choice of litigation tactics by Honduras and the Panel was not legally bound to it under Article 11 of the DSU.

40. In this context, the European Communities would disagree with Honduras’ interpretation of the case India – Patents. This case rather seems to confirm the Panels’ approach to take all elements, including the “practices”, into account. The European Communities notes that the Appellate Body analyzed India’s legislation and practices under the following chapeau:

Previous GATT/WTO panels also have conducted a detailed examination of the domestic law of a Member in assessing the conformity of that domestic law with the relevant GATT/WTO obligations. For example, in United States – Section 337 of the Tariff Act of 1930, the Panel conducted a detailed examination of the relevant United States’ legislation and practice (...).

28 WT/DS302/5 of 9 December 2003 (emphasis added).
And, just as it was necessary for the Panel in this case to seek a detailed understanding of the operation of the Patents Act as it relates to the "administrative instructions" in order to assess whether India had complied with Article 70.8(a), so, too, is it necessary for us in this appeal to review the Panel’s examination of the same Indian domestic law. 29

41. Thus, in this case both the Panel and the Appellate Body analyzed the "administrative instructions", i.e. practices, in order to determine the scope of the domestic law. 30 True, both instances eventually rejected India’s argument, but this was done on the basis of an assessment of the facts and not because of a procedural argument that the practice was not part of the "matter" before the Panel.

42. More generally speaking, the European Communities would finally consider that it is also in the interest of the object of purpose of the DSU, namely the prompt and satisfactory settlement of a situation, 31 to take into account all relevant elements for determining the "matter". Otherwise, it might be difficult to find a satisfactory solution to a dispute if important elements of a subject matter are for procedural reasons disregarded. In this context, the European Communities would refer to the very broad Appellate Body findings in Korea – Dairy which conclude

   However, under Article 11 of the DSU, a panel is charged with the mandate to determine the facts of the case and to arrive at factual findings. In carrying out this mandate, a panel has the duty to examine and consider all the evidence before it, not just the evidence submitted by one or the other party, and to evaluate the relevance and probative force of each piece thereof. 32

In the light of this very broad duty to take into account all relevant elements, the European Communities would see no error of law by the Panel when it considered the evidence presented by the Dominican Republic that the bond requirement serves other purposes than to secure the Selective Consumption Tax.


30 The Panel request by the US referred more globally to the "legal regime" of India’s patent protection, WT/DS50/4 of 8 November 1996.

31 Article 3.3 and 3.4 of the DSU.

32 Appellate Body report, Korea – Dairy, para. 137.
V. THE PANEL’S REVIEW OF THE AMOUNT OF THE BOND REQUIREMENT UNDER ARTICLE III:4 GATT

A. Honduras cross-appeal and the Panel findings

43. Honduras claims that the Panel erred in its assessment under Article III:4 of the GATT because the Panel based its conclusion on the market performance of importers in the past years rather than the bond requirement itself. As Honduras was making an “as such” claim the Panel should not at all have looked at the actual trade flows in order to examine whether the bond requirement accorded less favourable treatment to importers.\(^{33}\) Even if the market conditions had to be taken into account, the Panel’s findings were flawed as they were based on an incomplete calculation of the per-unit price only for importers but not for domestic producers.\(^{34}\) Given that importers actually faced higher per-unit costs the Panel could not have reached the conclusion that the bond requirement did not provide less favourable treatment to imported goods.\(^{35}\) Finally, as the bond requirement does not serve any purpose for importers, which have to pay the Selective Consumption Tax immediately, it imposes a higher burden on importers than on domestic producers, thus violating Article III:4 of the GATT.\(^{36}\)

44. The Panel considered the per-unit cost of the bond in relation to the effective cost entailed by it. Thus, the cost of the bond price would decrease if the output on cigarettes increases. Conversely, the relative cost would increase if the output on cigarettes decreases.\(^{37}\) The Panel concluded:

\(^{33}\) Honduras, Other Appellant’s Submission, paras. 30 \textit{et seq.}

\(^{34}\) Ibid., paras. 43 \textit{et seq.}

\(^{35}\) Ibid., paras. 48 \textit{et seq.}

\(^{36}\) Ibid., paras. 55 \textit{et seq.}

By definition, any expense that is fixed (i.e. not related to volumes of production) may lead to different costs per unit among supplier firms. As 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.\(^{38}\)

Moreover, in relation to Honduras’ argument that the bond requirement imposes an additional burden, the Panel pointed to the purposes of the bond to secure not only the Selective Consumption tax but also other applicable taxes.\(^{39}\)

**B. Discussion of the Panel’ conclusions**

1. **The fee incurred by the fixed amount of the bond requirement**

In the present case, the European Communities considers that the Panel was, as a matter of principle, correct in taking into account the per-unit cost of the total bond requirement.

The European Communities would note that the fixed amount of the bond requirement applies equally to importer and domestic producer. It is, therefore, a formally identical measure. This does, of course, not exclude that Article III:4 of the GATT is de facto affected. Thus, the GATT Panel in *US – Section 337* found:

>[T]here may be cases where the application of formally identical legal provisions would in practice accord less favourable treatment to imported products (…)\(^{40}\)

However, in order to determine whether a measure that applies equally to importer and domestic producer actually accords “less favourable treatment” to the imported goods it is inevitable to assess the factual implications of the measure on domestic and imported products. Without such an analysis the Panel could never come to a conclusion that a measure which applies equally to domestic and imported

\(^{38}\) Ibid., para. 7.300.

\(^{39}\) Ibid., para. 7.292.

\(^{40}\) Panel Report, *US – Section 337*, para. 5.11.
products alters (factually) the “conditions of competition”\textsuperscript{41} to the detriment of the latter.

49. Moreover, the European Communities would emphasize that the Appellate Body in \textit{EC - Asbestos} concluded that

\begin{quote}
A complaining Member must still establish that the measure accords to the \textit{group} of “like” \textit{imported} products "less favourable treatment” than it accords to the \textit{group} of “like” \textit{domestic} products. (Underlining added)
\end{quote}

50. Thus, it is not sufficient to look at one specific example of less favourable treatment for one importer but one needs to take the group as a whole.\textsuperscript{42} The same applies \textit{vice versa} for domestic producers. In the present case of a formally identical treatment it is even more important to establish whether the “group” of domestic producers or importers are adversely affected due to fact that the specific burden on individual operators varies depending on their respective size.

51. Honduras refers to the hypothesis that a potential importer would perhaps wish to “test” the market of the Dominican Republic, import only very small amounts and thus be disproportionately burdened.\textsuperscript{43} With this argument, Honduras only recognises half of the truth because the bond requirement would seem to have the same effect on potential domestic producers who could wish to “test” the market.

52. The Panel concluded - based on the calculation, that the costs entailed by the bond requirement only represented 0.2 per cent of the annual value of cigarettes imports\textsuperscript{44} - that the bond requirement was unlikely to affect adversely the conditions of competitions for importers. Arguably, as Honduras pointed out, the Panel should have also calculated in comparison the per-unit price for domestic cigarettes. As said, as a matter of principle, the EC agrees with the panel’s per-unit-cost approach. Yet, in addition to this relative notion, one also needs to

\textsuperscript{41} See the test in Appellate Body, \textit{Japan- Alcoholic Beverages II}, p. 16; confirmed in Appellate Body, \textit{Korea - Various Measures on Beef}, para. 135.

\textsuperscript{42} See \textit{EC' Oral Statement}, para. 21 \textit{et seq.}

\textsuperscript{43} Honduras, Other Appellant' Submission, para. 70.

\textsuperscript{44} Panel Report, \textit{Dominican Republic – Import and Sale of Cigarettes}, para. 7.299.
consider the absolute level of the burden at issue. Therefore, given the marginal negligible costs of the bond calculated per-unit, the Panel would probably not have come to a different conclusion even if it had calculated that the per-unit price for domestic cigarettes amounts to – as Honduras suggests\(^{45}\) – only one third of the per-unit price for domestic cigarettes.

53. The Panel appears to have based its reasoning on the correct assumption that the "conditions of competition" of a measure that applies equally to importers and domestic producers are not affected by just any marginal difference. However, in its appeal Honduras has pointed to several Panel and Appellate Body decisions which indicate that any kind difference constitutes a violation of Article III:2 of the GATT. The same reasoning should apply with the context of Article III:4 of the GATT.\(^{46}\)

54. The European Communities is not convinced about the relevance of these decisions in the present case. The cases cited by Honduras, i.e. the Appellate Body in *Japan – Alcoholic Beverages II* and *US – Malt Beverages*, dealt with a formally discriminatory treatment between imported and domestic goods while the amount of the bond requirement is a measure that applies equally to importers and domestic producers.

55. The legal consequences of these different situations are well demonstrated in the cases quoted by Honduras. In *US – Malt Beverages* the US Federal Excise Tax differential on Beer was different for imported and domestic goods.\(^{47}\) In similar vein, the European Communities would refer to the case in the case *US – Superfund* where the tax differentiation existed between imported and domestic products.\(^{48}\) By contrast, the present case does not draw a distinction between domestic and imported products, i.e. the total bond requirement applies to domestic and imported cigarettes in the same way. The question whether this

\(^{45}\) Honduras, Other Appellant' Submission, para. 70.

\(^{46}\) Ibid., paras. 52, 53.

\(^{47}\) Panel Report (GATT), *US – Malt Beverages*, paras. 5.4 et seq.

\(^{48}\) Panel Report (GATT), *US – Supefund*, paras. 2.1 et seq., 5.1 et seq.
amounts to a "less favourable treatment" under Article III:4 GATT cannot be answered in the affirmative, as soon as there is any minor difference in the effect of formally identical treatment on the group of like imports as compared with the group of like domestic goods.

56. Consequently, the European Communities considers that this jurisprudence is not relevant in this case. When determining the "less favourable treatment" under Article III:4 of the GATT the Panel could, therefore, come to the conclusion that the conditions of competitions are not altered in case of a measure that applies equally to domestic and imported products and which has only a minimal or negligent impact on the costs of the products.

57. Finally, the European Communities would submit that a different conclusion could have considerable consequences for the legal system of the Members. Indeed, while a "less favourable treatment" by formally discriminatory treatment of domestic and imported products is relatively easy to identify and to abolish, this is different in case of a formally identical treatment. It appears very far-reaching to interpret the criterion of "less favourable treatment" to mean that even the slightest possibility that the conditions of competitions are affected by formally identical treatment are avoided. Indeed, this may be neither practical nor possible. It is, therefore, appropriate to determine the legal benchmark for a violation of Article III:4 of the GATT in a more nuanced way when formally identical treatment is involved that allegedly imposes a higher burden on imports.

58. In support of this view, the European Communities would also find comfort in Article III:1 of the GATT which, according to the Appellate Body, informs the remainder of Article III:
Article III:1 articulates a general principle that internal measures should not be applied so as to afford protection to domestic production. This general principle informs the rest of Article III. The purpose of Article III:1 is to establish this general principle as a guide to understanding and interpreting the specific obligations contained in Article III:2 and in the other paragraphs of Article III, while respecting, and not diminishing in any way, the meaning of the words actually used in the texts of those other paragraphs.\footnote{Appellate Body Report, \textit{Japan – Alcoholic Beverages}, p. 18.}

59. In case of a formally discriminatory measure it might be considered that the element of “protection” is relatively easy to identify. However, this is different in case of a formally identical measure. Any treaty interpreter would have to be very careful in considering whether in such a situation this criterion would be fulfilled. More specifically, if a formally identical measure has only minimal or negligent practical consequences, and if that measure does not even necessarily alter the conditions of competitions to the detriment of the group of imported goods but possibly equally to the detriment of the group of domestic goods, it appears even more justified to take into account whether the measure is applied so as to afford protection to domestic production under Article III:1 of the GATT.

60. For the reasons set out above, the European Communities, therefore, considers that the Panel did not err in finding that the equal amount under the bond requirement for domestic producers and importers does not violate Article III:4 of the GATT.

2. The purpose of the bond requirement

61. In respect of Honduras’ argument that the bond requirement constitutes an additional burden to importers contrary to Article III:4 of the GATT\footnote{Honduras, Other Appellant’s submission, paras. 56 \textit{et seq.}, 63.}, the European Communities would refer to its assessment under Article 11 of the DSU above. Thus, the European Communities considers that the Dominican Republic’s practice whereby the bond requirement serves other purposes apart from securing the Selective Consumption Tax should be taken into account.
62. The European Communities notes that in Honduras' view the asymmetry remains in respect of the Selective Consumption Tax even if it is accepted that the bond requirement serves further purposes. Honduras considers that the need for security is not the same in the case of imports and domestic products, which is why the identical bond requirement results in less favourable treatment of all imports. The European Communities would agree that the extent to which the situation of importers and domestic operators is different with regard to the need to secure taxes, is a relevant criterion. In this connection, there may be a difference in the need for security between imports which face consumption taxes upon importation and where a *posteriori* payments are limited to instances of reassessments, and the situation of domestic products for which the taxes have to be paid only a certain period of time after the transaction. However, even if applying the same security in these two cases is different, the question of less favourable treatment would again depend also on the absolute level of the burden.

VI. **CONCLUSION**

63. For the reasons set out above, the European Communities considers that the Appellate Body should

> uphold the Panel’s findings regarding whether the tax stamp requirement is “necessary” under Article XX(d) GATT;

> conclude that the Panel made an objective assessment of the “matter” under Article 11 of the DSU by taking into account that the bond requirement serves further purposes than securing the Selective Consumption Tax.

> conclude on Article III:4 GATT regarding the bond requirement in the light of the comments made in this submission.

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51 Ibid., para. 65.