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MEXICO – TAX MEASURES ON SOFT DRINKS AND OTHER BEVERAGES

AB-2005-10

Report of the Appellate Body

CASES CITED IN THIS REPORT

Short Title	Full Case Title and Citation
Argentina – Poultry Anti-Dumping Duties	Panel Report, *Argentina – Definitive Anti-Dumping Duties on Poultry from Brazil*, WT/DS241/R, adopted 19 May 2003, DSR 2003:V, 1727
Australia – Salmon	Appellate Body Report, *Australia – Measures Affecting Importation of Salmon*, WT/DS18/AB/R, adopted 6 November 1998, DSR 1998:VIII, 3327
Canada – Aircraft	Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, adopted 20 August 1999, DSR 1999:III, 1377
Canada – Wheat Exports and Grain Imports	Appellate Body Report, *Canada – Measures Relating to Exports of Wheat and Treatment of Imported Grain*, WT/DS276/AB/R, adopted 27 September 2004
Dominican Republic – Import and Sale of Cigarettes	Appellate Body Report, *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes*, WT/DS302/AB/R, adopted 19 May 2005
EC – Bananas III	Appellate Body Report, *European Communities – Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, adopted 25 September 1997, DSR 1997:II, 591
EC – Export Subsidies on Sugar	Appellate Body Report, *European Communities – Export Subsidies on Sugar*, WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R, adopted 19 May 2005
EC – Hormones	Appellate Body Report, *EC Measures Concerning Meat and Meat Products (Hormones)*, WT/DS26/AB/R, WT/DS48/AB/R, adopted 13 February 1998, DSR 1998:I, 135
India – Patents (US)	Appellate Body Report, *India – Patent Protection for Pharmaceutical and Agricultural Chemical Products*, WT/DS50/AB/R, adopted 16 January 1998, DSR 1998:I, 9
Korea – Various Measures on Beef	Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, DSR 2001:I, 5
Mexico – Corn Syrup (Article 21.5 – US)	Appellate Body Report, *Mexico – Anti-Dumping Investigation of High Fructose Corn Syrup (HFCS) from the United States – Recourse to Article 21.5 of the DSU by the United States*, WT/DS132/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6675
Mexico – Taxes on Soft Drinks	Panel Report, *Mexico – Tax Measures on Soft Drinks and Other Beverages*, WT/DS308/R, 7 October 2005
US – 1916 Act	Appellate Body Report, *United States – Anti-Dumping Act of 1916*, WT/DS136/AB/R, WT/DS162/AB/R, adopted 26 September 2000, DSR 2000:X, 4793
US – Corrosion-Resistant Steel Sunset Review	Appellate Body Report, *United States – Sunset Review of Anti-Dumping Duties on Corrosion-Resistant Carbon Steel Flat Products from Japan*, WT/DS244/AB/R, adopted 9 January 2004
US – FSC (Article 21.5 – EC)	Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/AB/RW, adopted 29 January 2002, DSR 2002:I, 55
US – Gambling	Appellate Body Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, WT/DS285/AB/R, adopted 20 April 2005
US – Gasoline	Appellate Body Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R, adopted 20 May 1996, DSR 1996:I, 3

Short Title	Full Case Title and Citation
US – Section 337	GATT Panel Report, *United States Section 337 of the Tariff Act of 1930*, adopted 7 November 1989, BISD 36S/345
US – Shrimp	Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, adopted 6 November 1998, DSR 1998:VII, 2755
US – Shrimp (Article 21.5 – Malaysia)	Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products – Recourse to Article 21.5 of the DSU by Malaysia*, WT/DS58/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6481
US – Wool Shirts and Blouses	Appellate Body Report, *United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India*, WT/DS33/AB/R and Corr.1, adopted 23 May 1997, DSR 1997:I, 323

ABBREVIATIONS USED IN THIS REPORT

Abbreviation	**Description**
Division	Appellate Body Division hearing this appeal
DSB	Dispute Settlement Body
DSU	*Understanding on Rules and Procedures Governing the Settlement of Disputes*
GATT 1994	*General Agreement on Tariffs and Trade 1994*
HFCS	high-fructose corn syrup
Inter-American Convention	Inter-American Convention for the Protection and Conservation of Sea Turtles
ITO	International Trade Organization
NAFTA	North American Free Trade Agreement
Panel	Panel in *Mexico – Taxes on Soft Drinks*
Panel Report	Panel Report, *Mexico – Taxes on Soft Drinks*
Working Procedures	*Working Procedures for Appellate Review*, WT/AB/WP/5, 4 January 2005
WTO	World Trade Organization

WORLD TRADE ORGANIZATION
APPELLATE BODY

Mexico – Tax Measures on Soft Drinks and Other Beverages

Mexico, *Appellant*
United States, *Appellee*

Canada, *Third Participant*
China, *Third Participant*
European Communities, *Third Participant*
Guatemala, *Third Participant*
Japan, *Third Participant*

AB-2005-10

Present:

Taniguchi, Presiding Member
Janow, Member
Sacerdoti, Member

I. Introduction

1. Mexico appeals certain issues of law and legal interpretations developed in the Panel Report, *Mexico – Tax Measures on Soft Drinks and Other Beverages* (the "Panel Report").[1] The Panel was established to consider a complaint by the United States concerning certain tax measures and bookkeeping requirements imposed by Mexico on soft drinks and other beverages that use sweeteners other than cane sugar.

2. The measures challenged by the United States include: (i) a 20 per cent tax on the transfer or, as applicable, the importation of soft drinks and other beverages that use any sweetener other than cane sugar (the "soft drink tax"); (ii) a 20 per cent tax on specific services (commission, mediation, agency, representation, brokerage, consignment, and distribution), when such services are provided for the purpose of transferring products such as soft drinks and other beverages that use any sweetener other than cane sugar (the "distribution tax"); and (iii) a number of requirements imposed on taxpayers subject to the soft drink tax and to the distribution tax (the "bookkeeping requirements").[2] Before the Panel, the United States claimed that these measures are inconsistent with paragraphs 2 and 4 of Article III of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994").

3. In its first written submission to the Panel, Mexico requested that the Panel decide, as a preliminary matter, to "decline to exercise its jurisdiction in this case"[3] and that it "recommend to the

[1]WT/DS308/R, 7 October 2005.

[2]These measures are described in more detail in paragraphs 2.2-2.5 of the Panel Report.

[3]Panel Report, para. 4.2.

parties that they submit their respective grievances to an Arbitral Panel, under Chapter Twenty of the NAFTA[4], which can address both Mexico's concern with respect to market access for Mexican cane sugar in the United States under the NAFTA and the United States' concern with respect to Mexico's tax measures."[5] Mexico also stated that, in the event the Panel decided to exercise jurisdiction, the Panel should find that the measures are justified pursuant to Article XX(d) of the GATT 1994.[6]

4. On 18 January 2005, the Panel issued a preliminary ruling in which it rejected Mexico's request.[7] In doing so, the Panel concluded that, "under the DSU[8], it had no discretion to decide whether or not to exercise its jurisdiction in a case properly before it."[9] The Panel added that, "even if it had such discretion, the Panel did not consider that there were facts on record that would justify the Panel declining to exercise its jurisdiction in the present case."[10]

5. In its Report, circulated to Members of the World Trade Organization (the "WTO") on 7 October 2005, the Panel concluded that:

(a) With respect to Mexico's soft drink tax and distribution tax:

(i) As imposed on sweeteners, imported beet sugar is subject to internal taxes in excess of those applied to like domestic sweeteners, in a manner inconsistent with Article III:2, first sentence, of the GATT 1994;

(ii) As imposed on sweeteners, imported HFCS[11] is being taxed dissimilarly compared with the directly competitive or substitutable products, so as to afford protection to the Mexican domestic production of cane sugar, in a manner inconsistent with Article III:2, second sentence, of the GATT 1994;

(iii) As imposed on sweeteners, imported beet sugar and HFCS are accorded less favourable treatment than that accorded to like products of national origin, in a manner inconsistent with Article III:4 of the GATT 1994;

(iv) As imposed on soft drinks and syrups, imported soft drinks and syrups sweetened with non-cane sugar sweeteners (including HFCS and beet sugar) are subject to internal taxes in excess of those applied to like domestic products, in a manner inconsistent with Article III:2, first sentence, of the GATT 1994.

[4]North American Free Trade Agreement (the "NAFTA").

[5]Panel Report, para. 3.2.

[6]*Ibid.*

[7]The Panel's preliminary ruling is reproduced as Annex B to the Panel Report.

[8]*Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU").

[9]Panel Report, para. 7.1.

[10]*Ibid.*

[11]High-fructose corn syrup ("HFCS").

(b) With respect to Mexico's bookkeeping requirements: As imposed on sweeteners, imported beet sugar and HFCS are accorded less favourable treatment than that accorded to like products of national origin, in a manner inconsistent with Article III:4 of the GATT 1994.[12]

The Panel rejected Mexico's defence under Article XX(d) of the GATT 1994, concluding that "the challenged tax measures are not justified as measures that are necessary to secure compliance by the United States with laws or regulations which are not inconsistent with the provisions of the GATT 1994."[13] The Panel therefore recommended "that the Dispute Settlement Body request Mexico to bring the inconsistent measures … into conformity with its obligations under the GATT 1994."[14]

6. On 6 December 2005, Mexico notified the Dispute Settlement Body (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 of the DSU, and filed a Notice of Appeal[15] pursuant to Rule 20(1) of the *Working Procedures for Appellate Review* (the "*Working Procedures*").[16] On 13 December 2005, Mexico filed an appellant's submission.[17] In its appeal, Mexico challenges the Panel's preliminary ruling rejecting Mexico's request that the Panel decline to exercise jurisdiction in this case, as well as the Panel's findings concerning Article XX(d) of the GATT 1994. Mexico did not appeal the Panel's findings under Article III of the GATT 1994. On 6 January 2006, the United States filed an appellee's submission.[18] On the same day, China, the European Communities, and Japan each filed a third participant's submission.[19] Also on the same day, Canada and Guatemala each notified the Appellate Body Secretariat of its intention to appear at the oral hearing as a third participant.[20]

7. By letter dated 5 January 2006, Mexico requested authorization to correct certain clerical errors in its appellant's submission pursuant to Rule 18(5) of the *Working Procedures*. On 9 January 2006, the Appellate Body Division hearing the appeal ("the Division") invited all participants and third participants to comment on Mexico's request, in accordance with Rule 18(5). On 11 January 2006, the United States responded that, although some of the requested corrections are

[12]Panel Report, para. 9.2. (original underlining)

[13]*Ibid.*, para. 9.3.

[14]*Ibid.*, para. 9.5.

[15]WT/DS308/10 (attached as Annex I to this Report).

[16]WT/AB/WP/5, 4 January 2005.

[17]Pursuant to Rule 21(1) of the *Working Procedures*. A courtesy English translation of Mexico's appellant's submission, prepared by Mexico, was provided to the participants and third participants on 16 December 2005.

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

[19]Pursuant to Rule 24(1) of the *Working Procedures*.

[20]Pursuant to Rule 24(2) of the *Working Procedures*.

not "clearly clerical", within the meaning of Rule 18(5), "[i]n the circumstances of this dispute", the United States did not object to Mexico's request. No other comments were received. By letter dated 16 January 2006, the Division authorized Mexico to correct the clerical errors in its appellant's submission but emphasized, however, that it had not been requested, and did not make, a finding "as to whether all of the corrections requested by Mexico are 'clerical' within the meaning of Rule 18(5) of the *Working Procedures*."

8. On 13 January 2006, the Appellate Body received an *amicus curiae* brief from *Cámara Nacional de las Industrias Azucarera y Alcoholera* (National Chamber of the Sugar and Alcohol Industries) of Mexico.[21] The Division did not find it necessary to take the brief into account in resolving the issues raised in this appeal.

9. The oral hearing in this appeal was held on 18 January 2006. The participants and third participants presented oral arguments (with the exception of Guatemala) 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 Mexico – Appellant*

1. Exercise of Jurisdiction

10. Mexico argues that the Panel erred in rejecting Mexico's request that it decline to exercise jurisdiction in the circumstances of the present dispute. According to Mexico, the Panel's decision was primarily based on the Panel's view that Article 11 of the DSU "compels a WTO [p]anel to address the claims" on which a finding is necessary to enable the DSB to make sufficiently precise recommendations or rulings to the parties to the dispute and that, therefore, a WTO panel has no discretion to decline to exercise validly established jurisdiction.[22] Mexico submits that this is incorrect and ignores the fact that, like other international bodies and tribunals, WTO panels have certain "implied jurisdictional powers"[23] that derive from their nature as adjudicative bodies. According to Mexico, such powers include the power to refrain from exercising substantive

[21]At the oral hearing, Mexico stated that its arguments are set out in its appellant's and oral submissions. Mexico added, however, that it would not object should the Appellate Body decide to accept the *amicus* brief. The United States noted that the *amicus* brief had been received late in the proceedings and that it presented new arguments and claims of error that were not part of Mexico's Notice of Appeal. Accordingly, while taking the view that the Appellate Body had the authority to accept the brief, the United States argued that it should decline to do so in the circumstances of this dispute.

[22]Mexico's appellant's submission, para. 64 ("*obliga a un Grupo Especial de la OMC a abordar las reclamaciones*").

[23]*Ibid.*, para. 65 ("*facultades implícitas en relación con su competencia*").

jurisdiction in circumstances where "the underlying or predominant elements of a dispute derive from rules of international law"[24] under which claims cannot be judicially enforced in the WTO, such as the NAFTA provisions or when one of the disputing parties refuses to take the matter to the "appropriate forum".[25] Mexico contends, in this regard, that the United States' claims under Article III of the GATT 1994 are inextricably linked to a broader dispute[26] concerning the conditions provided under the NAFTA for access of Mexican sugar to the United States market, and that only a NAFTA panel could resolve the dispute between the parties.

11. Mexico further emphasizes that there is nothing in the DSU that explicitly rules out the existence of a WTO panel's power to decline to exercise its jurisdiction even in a case that is properly brought before it. Mexico adds that the application by panels of the principle of "judicial economy" illustrates that notwithstanding the requirement of Article 7.2 of the DSU that panels address the relevant provisions in any covered agreement or agreements cited by the parties to the dispute, WTO panels can decide not to address certain claims. Thus, according to Mexico, there is no question that WTO panels have an implicit or inherent competence. As other examples of panels' "implied jurisdictional powers", Mexico points, *inter alia*, to the power of panels to determine whether they have substantive jurisdiction over a matter and the power to decide all matters that are inherent to the "adjudicative function"[27] of panels.

12. Finally, referring to the ruling of the Permanent Court of International Justice (the "PCIJ") in the *Factory at Chorzów* case, Mexico calls into question the "applicability" of its WTO obligations towards the United States in the context of this dispute.[28]

2. Article XX(d) of the GATT 1994

13. Mexico appeals the Panel's finding that the measures at issue are not justified pursuant to Article XX(d) of the GATT 1994. In addition, Mexico requests the Appellate Body to complete the analysis and find that its tax measures are justified under Article XX(d) of the GATT 1994, because

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[24]Mexico's appellant's submission, para. 73 ("*los elementos predominantes de una disputa derivan de reglas del derecho internacional*").

[25]*Ibid.* ("*foro adecuado*").

[26]*Ibid*.

[27]*Ibid.*, para. 67 ("*función jurisdiccional*").

[28]See *ibid.*, paras. 73-74. The passage of the ruling that Mexico refers to reads as follows:

> … one party cannot avail himself of the fact that the other has not fulfilled some obligation … if the former party has … prevented the latter … from having recourse to the tribunal which would have been open to him.

(Permanent Court of International Justice, *Factory at Chorzów (Germany v. Poland)* (Jurisdiction), 1927, PCIJ Series A, No. 9, p. 31) (underlining added by Mexico omitted)

the measures are necessary "to secure compliance" by the United States of its obligations under the NAFTA.

14. Mexico asserts that the Panel erred in finding that the measures at issue are not designed "to secure compliance" within the meaning of Article XX(d). According to Mexico, this finding is based on an erroneous interpretation of the terms "to secure compliance" as involving enforcement action within a *domestic* legal system. Mexico argues that there is no basis to exclude action taken to enforce *international* treaty obligations from the scope of Article XX(d). Mexico adds that, in the broader context of international law, countermeasures are measures aimed at securing compliance with international obligations. Mexico further submits that the Panel erred by equating the concept of "enforcement" with that of "coercion". In Mexico's view, the Panel's effort to distinguish between actions at the domestic level and at the international level based on its understanding of the concept of coercion in this dispute has no textual basis, because Article XX(d) simply does not refer to the use of coercion.

15. Moreover, Mexico asserts that the Panel erred by confusing the issue of the "design" of the measure under Article XX(d) with the issue of its "outcome".[29] Rather than examining whether Mexico's measures were put in place in order to secure the United States' compliance with its NAFTA obligations, the Panel considered the effectiveness of those measures. Mexico emphasizes that "even if the outcome of a measure is completely uncertain or unpredictable, the measure in question can, nevertheless be 'designed to secure compliance with laws and regulations' within the meaning of Article XX(d)".[30] Contrary to the Panel's finding, the issue of the likely outcome of a given measure is not legally relevant to the assessment of the design of the measure under Article XX(d). Thus, Mexico takes issue with the Panel's finding that the "uncertain outcome of international countermeasures is a reason for disqualifying them as measures eligible for consideration under Article XX(d)".[31] Mexico notes, in this regard, that nothing in the text of Article XX(d) suggests that any measure is *a priori* ineligible as a measure "to secure compliance with laws and regulations" on the basis of its "uncertain outcome".

16. Turning to the meaning of the terms "laws and regulations" in Article XX(d), Mexico notes that the Panel's interpretation of these terms is based on the erroneous conclusions reached by the Panel with respect to the terms "to secure compliance". Mexico submits that the words "laws" and

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[29]Mexico's appellant's submission, para. 98 ("*destino*"; "*resultado*").

[30]*Ibid.*, para. 102 ("*aun si el resultado de la medida es totalmente incierto, impredecible, bien puede estar 'destinada a lograr la observancia de las leyes y reglamentos' en el sentido del artículo XX(d)*").

[31]*Ibid.*, para. 104 ("*el resultado incierto de las contramedidas internacionales es una razón para excluirlas como medidas que pueden ser objeto de consideración, en el marco del inciso (d) del artículo XX*") (quoting Panel Report, para. 8.187).

"regulations" are expressly qualified in other provisions of the covered agreements; the absence of qualifying language in Article XX(d) thus supports the view that the terms are not limited to *domestic* laws or regulations, but include international agreements. Mexico adds that a review of the Article XX exceptions reveals that only three—(paragraphs (c), (g), and (i))—are, expressly or by implication, concerned with an activity that would occur *within* the territory of the Member seeking to justify its measures. This position, according to Mexico, is supported by the Appellate Body's findings in *US – Shrimp (Article 21.5 – Malaysia)*.[32]

17. Mexico further requests, in the event the Appellate Body should reverse the Panel's conclusion, that it complete the Panel's analysis and find that the Mexican measures are "necessary" within the meaning of Article XX(d) and meet the requirements of the chapeau of that Article. According to Mexico, the uncontested facts and evidence in the Panel record, and the Panel's acknowledgement that Mexico's measures have "attracted the attention" of the United States, provide an ample basis on which to complete the analysis and conclude that the measures are "necessary" within the meaning of Article XX(d).

18. Mexico observes that, before the Panel, the United States could not identify any alternative measure that Mexico could and should have used in order to attain its legitimate objective. It further explains that the fact that a measure does not or has not yet achieved its objective does not mean that it is not "necessary" within the meaning of Article XX(d). It may mean that it is insufficient to secure compliance, or that it is insufficient to secure immediate compliance, but can do so over time; however, it says nothing about whether the measure is "necessary". Moreover, Mexico submits that the evidence on the record demonstrates that the measures at issue have contributed to securing compliance in the circumstances of this case by changing the dynamics of the NAFTA dispute and forcing the United States to pay attention to Mexico's grievances, and also contradicts the Panel's finding that Mexico's measures do not contribute to securing compliance in this dispute.

19. As regards the chapeau of Article XX of the GATT 1994, Mexico asserts that its measures neither arbitrarily nor unjustifiably discriminate between countries where the same conditions prevail. Rather than constituting "arbitrary or unjustifiable discrimination", the measures constitute "limited

[32]Mexico's appellant's submission, paras. 174 and 177-178 (referring to Appellate Body Report, *US – Shrimp (Article 21.5 – Malaysia)*, paras. 123-124 and 128-130).

sectoral retaliation in the relevant market segment (*i.e.*, the sweeteners market)."[33] Nor can the measures be said to be a "disguised restriction on [international] trade" because they constitute "a proportionate, legitimate and legally justified response to actions and omissions of the United States"[34], and, furthermore, the measures have been published.

20. Finally, Mexico argues that the Panel, "separately and in addition"[35] to the previous errors, failed to make "an objective assessment of the facts", as required by Article 11 of the DSU, in finding that "Mexico has not established that its measures contribute to securing compliance in the circumstances of this case."[36] According to Mexico, the Panel's finding is based solely on the Panel's view that attracting the attention of the United States is not equivalent to securing compliance with a law or regulation and ignores that "achieving the objectives sought by the countermeasures can take time".[37]

B. *Arguments of the United States – Appellee*

1. Exercise of Jurisdiction

21. The United States submits that the Panel properly rejected Mexico's request for the Panel to refrain from exercising jurisdiction in the present dispute.

22. Referring to Article 11 of the DSU, the United States observes that, if the Panel had declined to exercise jurisdiction over this dispute, or had agreed to Mexico's request that it refrain from issuing findings and recommendations, the Panel would have made no findings on the United States' claims that Mexico's tax measures are inconsistent with Article III of the GATT 1994. This would have left the DSB "unable to give any rulings or (as is appropriate in this dispute) to make any

[33]Mexico's appellant's submission, para. 173 ("*retorsiones sectoriales limitadas al segmento del mercado relevante (i.e., el mercado de los edulcorantes)*"). Mexico asserts that the facts of this case are similar to the situation examined by the Appellate Body in *US – Shrimp (Article 21.5 – Malaysia)*. Mexico explains that, in that dispute, the Appellate Body found that a United States unilateral measure was not inconsistent with the chapeau of Article XX of the GATT 1994. According to Mexico, in that case, the Appellate Body did not require the United States to conclude an international agreement with the disputing parties, but rather required it to have made good faith efforts in that direction. In this case, Mexico argues that it has sought to resolve the dispute through NAFTA and bilateral negotiations, but "the United States has essentially blocked Mexico's ability to have its grievance resolved." (Mexico's appellant's submission, paras. 174-181 ("*Estados Unidos esencialmente ha bloqueado la posibilidad de México para resolver su agravio.*"))

[34]*Ibid.*, para. 182 ("*una respuesta proporcional, legítima y legalmente justificada a las acciones y omisiones de Estados Unidos*").

[35]*Ibid.*, heading III.E ("*independiente y adicional*").

[36]Panel Report, para. 8.186. See also, Mexico's Notice of Appeal, para. 3.

[37]Mexico's appellant's submission, para. 166 ("*la consecución de los objetivos de las contramedidas puede llevar tiempo*").

recommendations"[38] in accordance with the rights and obligations under the DSU and the GATT 1994. The United States emphasizes that such a result is incompatible with the text of the DSU and would have required the Panel to disregard the mandate given to it by the DSB. Moreover, the United States observes that the Panel's own terms of reference in this dispute instructed the Panel to examine the matter referred to the DSB by the United States and to make such findings as will assist the DSB in making the recommendations and rulings provided for under the DSU.

23. Referring to Articles 3.2 and 19.2 of the DSU, the United States adds that, if a panel were to decline to exercise jurisdiction over a particular dispute, it would diminish the rights of the complaining Member under the DSU and other covered agreements. The United States further notes that prior reports of panels and the Appellate Body also support the Panel's findings. In this regard, the United States refers to *Mexico – Corn Syrup (Article 21.5 – US)*, where the Appellate Body stated that "panels are required to address issues that are put before them by the parties to a dispute."[39]

24. The United States observes that Mexico has referred to the principle of judicial economy as an example of "situations where WTO panels have refrained from exercising validly established substantive jurisdiction on certain claims that are before them."[40] However, the United States submits that, "when a panel exercises judicial economy, it does not decline to exercise substantive jurisdiction either over a dispute or certain claims in a dispute. Rather, the panel … declines to make findings on certain claims when resolution of such claims is not necessary for the panel to fulfill its mandate under Article 11 of the DSU and its terms of reference."[41] In other words, judicial economy "does not relieve a panel from its duty to carry out its mandate under Articles 7 and 11 of the DSU to resolve the dispute"[42] before it.

2. Article XX(d) of the GATT 1994

25. The United States submits that the Panel properly found that Mexico's tax measures are not designed "to secure compliance" and, thus, are not justified as measures "to secure compliance with laws or regulations" within the meaning of Article XX(d) of the GATT 1994. It notes that previous GATT and WTO disputes in which Article XX(d) has been invoked have involved domestic laws or regulations.

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[38]United States' appellee's submission, para. 124.

[39]*Ibid.*, para. 127 (quoting Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 36).

[40]*Ibid.*, para. 129 (quoting Mexico's appellant's submission, para. 68).

[41]*Ibid.* (referring to Appellate Body Report, *US – Wool Shirts and Blouses*, p. 19, DSR 1997:I, 323, at 340; and to Appellate Body Report, *Canada – Wheat Exports and Grain Imports*, para. 133).

[42]*Ibid.*, para. 130.

26. The United States agrees with the Panel's analysis of the terms "laws or regulations" and, therefore, supports the Panel's finding that these terms refer only to *domestic* laws or regulations and not to obligations under international agreements. The United States explains that Article XX(d) refers to "laws" and "regulations" in the plural, while the singular "law" is used when referring to "international law".[43] The United States further observes that the terms "laws or regulations" precede the words "which are not inconsistent" in Article XX(d) and explains that the term "inconsistent" appears elsewhere in the GATT 1994 in connection with domestic measures. In contrast, the WTO agreements use the word "conflict" when referring to international obligations.

27. The United States further submits that Mexico's interpretation of the terms "laws or regulations" would undermine Articles 22 and 23 of the DSU, as it would permit action, including the suspension of concessions, by any Member "outside the rules of the DSU".[44] The United States observes that Article XX(d) was not intended to provide the basis for suspending concessions under the WTO agreements upon a mere allegation of a breach of a non-WTO international agreement. Otherwise, according to the United States, "this would effectively convert WTO dispute settlement into a forum of general dispute resolution for all international agreements."[45] Furthermore, the United States argues that, if the terms "laws or regulations" are read to include obligations under non-WTO agreements, the WTO dispute settlement system "would become a forum for WTO Members to allege and obtain findings as to the consistency of another Member's measure with any non-WTO agreement."[46] The United States, therefore, disagrees with Mexico's arguments that the phrase "laws or regulations" in Article XX(d) refers to international agreements.

28. With respect to the Panel's interpretation of the phrase "to secure compliance", the United States notes that the references to coercion were intended "merely [to] reinforce the Panel's view that 'enforcement' does not refer to the international level"[47] and not, as Mexico argues, to create an additional requirement for justifying a measure under Article XX(d). The United States therefore agrees with the Panel that the terms "to secure compliance" do not apply to measures taken by one Member to induce another Member to comply with obligations under a non-WTO treaty.

29. The United States also rejects Mexico's submission that the "Panel wrongly found that measures with an 'uncertain outcome' are '*a priori* ineligible' as measures to secure compliance with

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[43]The United States observes that Article 3.2 of the DSU and Article 17.6 of the *Anti-Dumping Agreement* also use the term "law" in the singular when referring to "public international law".

[44]United States' appellee's submission, para. 37.

[45]*Ibid.*, para. 85. (footnote omitted)

[46]*Ibid.*, para. 41.

[47]*Ibid.*, para. 54 (referring to Panel Report, paras. 8.175 and 8.178).

laws or regulations."[48] While the United States concedes that the Panel's analysis "could have admittedly been clearer"[49], it also notes that the Panel did not require certainty, and argues that the Panel's remarks on this point simply characterized Mexico's failure to "put forth *any* evidence that its tax measures were designed to [secure] compliance."[50] The United States agrees with Mexico that "Article XX(d) does not require the party invoking the defense to establish that its measure will, without a doubt or with certainty, secure compliance with laws or regulations."[51] Nevertheless, the United States submits that Mexico has to provide some evidence that the measure is "designed" to secure such compliance.

30. For all these reasons, the United States submits that the Appellate Body should uphold the Panel's conclusion that Mexico's tax measures are *not* designed to secure compliance and, thus, are *not* justified as measures "to secure compliance with laws or regulations" within the meaning of Article XX(d) of the GATT 1994.

31. In the event the Appellate Body should reverse the Panel's finding and accept Mexico's request to complete the analysis, the United States asserts that Mexico's measures are neither "necessary" for purposes of Article XX(d), nor do they meet the requirements of the chapeau of that Article. According to the United States, Mexico has not demonstrated that the measures at issue contribute to compliance by the United States with its NAFTA obligations and "ignores"[52] the fact that the trade impact of a measure is one of the factors that must be weighed and balanced when determining whether a measure is "necessary". The impact of Mexico's measures was "essentially [to] prohibit the use of imported HFCS in Mexican soft drinks and other beverages and to reduce import volumes".[53] The United States adds that "[i]t is difficult to understand how discriminating against imports from potentially every WTO Member is 'necessary' to secure [the United States'] compliance with [its] obligations under the NAFTA."[54] The United States further observes that the absence of alternative measures that could be reasonably available does not, in itself, mean that the challenged measures are "necessary". In any event, the United States submits that if Mexico's objective was to attract the attention of the United States, it could have pursued a variety of other actions, including pursuing the diplomatic avenues available under the NAFTA.

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[48]United States' appellee's submission, para. 70 (quoting Mexico's appellant's submission, paras. 104-105).

[49]*Ibid.*, para. 71.

[50]*Ibid.* (original emphasis)

[51]*Ibid.*, para. 72. (footnote omitted)

[52]*Ibid*., para. 96.

[53]*Ibid.*, para. 97.

[54]*Ibid.*

32. The United States submits, furthermore, that Mexico's measures do not meet the requirements of the chapeau of Article XX of the GATT 1994. The only evidence that Mexico offers to support its contention that the measures do not constitute arbitrary or unjustifiable discrimination is the characterization of the measures as international countermeasures.[55] This is insufficient, argues the United States, for Mexico to meet its burden of proof. Moreover, the fact that Mexico may have been transparent about its measures is not sufficient to establish that such measures are not a "disguised restriction on trade".[56]

33. Lastly, the United States requests the Appellate Body to reject Mexico's contention that the Panel did not make an objective assessment of the facts, as required by Article 11 of the DSU. According to the United States, the Panel did not "ignore" arguments or evidence submitted by Mexico. The United States further explains that, in any event, the errors alleged by Mexico in support of its claim under Article 11 of the DSU "relate to the interpretation of Article XX, and do not support a conclusion that the Panel breached Article 11."[57]

C. *Arguments of the Third Participants*

1. China

34. Referring to Articles 7 and 11 of the DSU, China argues that a WTO panel does not have an implied power to refrain from performing its "statutory function".[58] China submits that, if a panel that is "empowered and obligated"[59] to assist the DSB in the settlement of a dispute declines to exercise jurisdiction, such a decision would create legal uncertainty and be contrary to the aim of providing security and predictability to the multilateral trading system as well as the prompt settlement of disputes as provided for in Article 3.3 of the DSU. China argues, moreover, that the notion of judicial economy is "relevant and applicable"[60] only if a panel has assumed the jurisdiction defined by its

[55]According to the United States, the Appellate Body rulings in *US – Shrimp (Articles 21.5 – Malaysia)* do not support Mexico's position, because that dispute did not involve a disagreement about the commitments made under an international agreement. (United States' appellee's submission, paras. 109-110)

[56]*Ibid.*, para. 114.

[57]*Ibid.*, para. 118.

[58]China's third participant's submission, para. 5.

[59]*Ibid.*, para. 6.

[60]*Ibid.*, para. 7.

terms of reference and has made "such findings as will assist the DSB" within the meaning of Article 11 of the DSU.

35. China asserts that the terms "laws or regulations" in Article XX(d) do not encompass international agreements. China states that Article X of the GATT 1994 provides contextual guidance for the interpretation of Article XX(d). Article X expressly distinguishes between "[l]aws, regulations, judicial decisions and administrative rulings" and "[a]greements … between the government or a governmental agency of any Member and the government or governmental agency of any other Member". China adds that interpreting "laws or regulations" to include international agreements would allow a WTO Member to justify under Article XX(d) its deviation from its WTO obligations in the name of any remedial measure in response to any alleged breach of any non-WTO international agreement. Such a scenario, according to China, is not consistent with the object and purpose of the GATT 1994.

2. European Communities

36. The European Communities submits that the Appellate Body should uphold the Panel's finding that it did not have the discretion to decline to exercise jurisdiction in this case. The European Communities submits that "the functions and obligations of WTO Panels must be established on the basis of the DSU, and particularly Article 11 thereof."[61] On this basis, the European Communities agrees that a panel has an inherent power to establish whether it has jurisdiction, and whether a particular matter is within its jurisdiction. However, the European Communities argues that a panel may not freely, or by "the notion of 'judicial economy'", decide to refrain from exercising its jurisdiction "in a case properly brought before it under the DSU."[62]

37. The European Communities asserts, furthermore, that the Appellate Body should uphold the Panel's finding that only measures made applicable in the domestic legal order of a WTO Member constitute "laws or regulations" within the meaning of Article XX(d). The European Communities disagrees, however, with the Panel's finding that "international agreements, even when incorporated into the domestic law of a WTO Member, can never be regarded as 'laws or regulations' for the purposes of Article XX(d)".[63] In addition, the European Communities takes issue with the Panel's interpretation of the terms "to secure compliance" as requiring a degree of certainty in the results that may be achieved through the measure.

[61]European Communities' third participant's submission, para. 8.

[62]*Ibid.*, paras. 10-11.

[63]*Ibid.*, para. 44.

3. Japan

38. Japan disagrees with the Panel's interpretation of the terms "to secure compliance" in Article XX(d). In this regard, Japan submits that Article XX(d) does not necessarily exclude measures that have, as a purpose, to secure compliance, but are not accompanied by compulsory enforcement. According to Japan, compliance can be secured by a request or a command without being accompanied by any coercion. Japan considers that the Panel erred by indicating that the determination of whether a measure is designed "to secure compliance" should be analyzed based on the degree of certainty of its outcome. Nevertheless, Japan agrees with the Panel's finding that Article XX(d) does not cover international agreements. Japan explains that the terms "laws or regulations", read together with the phrase "to secure compliance", "presuppose a hierarchical structure that is associated with the relation between the state and its subjects"[64] and, therefore, excludes international agreements.

III. Issues Raised in This Appeal

39. The following issues are raised in this appeal:

(a) whether the Panel erred in concluding that a WTO panel "has no discretion to decide whether or not to exercise its jurisdiction in a case properly before it"[65] and, if so, whether the Panel erred in declining to exercise that discretion in the circumstances of this dispute;

(b) whether the Panel erred in concluding that Mexico's measures do not constitute measures "to secure compliance with laws or regulations", within the meaning of Article XX(d) of the GATT 1994[66]; and

(c) whether the Panel failed to make an objective assessment of the facts of the case, as required by Article 11 of the DSU, in concluding that "even if the assumption were to be made in the abstract that international countermeasures are potentially capable of qualifying as measures designed to secure compliance", within the meaning of Article XX(d) of the GATT 1994, "Mexico has not established that its measures contribute to securing compliance in the circumstances of this case."[67]

[64]Japan's third participant's submission, para. 22.

[65]Panel Report, para. 7.18.

[66]*Ibid.*, para. 8.198.

[67]*Ibid.*, para. 8.186.

IV. The Panel's Exercise of Jurisdiction

A. *Introduction*

40. In its first written submission to the Panel, Mexico requested that the Panel decide, as a preliminary matter, to decline to exercise jurisdiction "in favour of an Arbitral Panel under Chapter Twenty of the North American Free Trade Agreement (NAFTA)."[68] In a preliminary ruling, the Panel rejected Mexico's request and found instead that, "under the DSU, it had no discretion to decide whether or not to exercise its jurisdiction in a case properly before it."[69] The Panel added that even if it had such discretion, it "did not consider that there were facts on record that would justify the Panel declining to exercise its jurisdiction in the present case."[70]

41. In its reasoning, the Panel opined that "discretion may be said to exist only if a legal body has the freedom to choose among several options, all of them equally permissible in law."[71] According to the Panel, "such freedom ... would exist within the framework of the DSU only if a complainant did not have a legal right to have a panel decide a case properly before it."[72] Referring to Article 11 of the DSU and to the ruling of the Appellate Body in *Australia – Salmon*, the Panel observed that "the aim of the WTO dispute settlement system is to resolve the matter at issue in particular cases and to secure a positive solution to disputes" and that a panel is required "to address the claims on which a finding is necessary to enable the DSB to make sufficiently precise recommendations or rulings to the parties."[73] From this, the Panel concluded that a WTO panel "would seem therefore not to be in a position to choose freely whether or not to exercise its jurisdiction."[74] Referring to Articles 3.2 and 19.2 of the DSU, the Panel further stated that "[i]f a WTO panel were to decide not to exercise its jurisdiction in a particular case, it would diminish the rights of the complaining Member under the DSU and other WTO covered agreements."[75] The Panel added that Article 23 of the DSU "make[s] it clear that a WTO Member that considers that any of its WTO benefits have been nullified or impaired as a result of a measure adopted by another Member has the right to bring the case before the WTO dispute settlement system."[76]

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[68]Panel Report, para. 7.1.

[69]*Ibid.*

[70]*Ibid.*

[71]*Ibid.*, para. 7.7.

[72]*Ibid.*

[73]*Ibid.*, para. 7.8 (referring to Appellate Body Report, *Australia – Salmon*, para. 223).

[74]*Ibid.*

[75]*Ibid.*, para. 7.9.

[76]*Ibid.*

42. On appeal, Mexico contends that the Panel erred in rejecting Mexico's request that it decline to exercise jurisdiction in the circumstances of the present dispute. Mexico submits that WTO panels, like other international bodies and tribunals, "have certain implied jurisdictional powers that derive from their nature as adjudicative bodies."[77] Such powers include the power to refrain from exercising substantive jurisdiction in circumstances where "the underlying or predominant elements of a dispute derive from rules of international law under which claims cannot be judicially enforced in the WTO, such as the NAFTA provisions" or "when one of the disputing parties refuses to take the matter to the appropriate forum."[78] Mexico argues, in this regard, that the United States' claims under Article III of the GATT 1994 are inextricably linked to a broader dispute[79] regarding access of Mexican sugar to the United States' market under the NAFTA. Mexico further emphasizes that "[t]here is nothing in the DSU ... that explicitly rules out the existence of"[80] a WTO panel's power to decline to exercise validly established jurisdiction and submits that "the Panel should have exercised this power in the circumstances of this dispute."[81]

43. In contrast, the United States argues that, "[t]he Panel's own terms of reference in this dispute instructed the Panel 'to examine ... the matter referred to the DSB by the United States'"[82] and "to make such findings as will assist the DSB" in making the recommendations and rulings provided for under the DSU. China and the European Communities agree with the United States that the Panel had no discretion to decline to exercise jurisdiction. China submits that if a panel declines to exercise jurisdiction over a dispute, such a decision will create legal uncertainty, contrary to the aim of providing security and predictability to the multilateral trading system and the prompt settlement of disputes as provided for in Article 3.3 of the DSU.[83] The European Communities agrees with the Panel's finding that it did not have discretion to decline to exercise jurisdiction in this case, and emphasizes that "the functions and obligations of WTO Panels must be established on the basis of the DSU, and particularly Article 11 thereof."[84]

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[77]Mexico's appellant's submission, para. 65 ("*tienen ciertas facultades implícitas en relación con su competencia, las cuales derivan de su propia naturaleza como órganos jurisdiccionales*").

[78]*Ibid.*, para. 73 ("*los elementos predominantes de una disputa derivan de reglas del derecho internacional, cuyo cumplimiento no puede reclamarse en el marco OMC, por ejemplo las disposiciones del TLCAN*"; "*cuando una de las partes contendientes se rehúsa a someterse al foro adecuado*").

[79]*Ibid*.

[80]*Ibid.*, para. 65 ("*Nada en el ESD ... explícitamente descarta que ... existan*").

[81]*Ibid.*, para. 72 ("*el Grupo Especial debió haber ejercido esa facultad en las circunstancias de esta disputa*").

[82]United States' appellee's submission, para. 125.

[83]China's third participant's submission, para. 6.

[84]European Communities' third participant's submission, para. 8.

B. *Analysis*

44. Before addressing Mexico's arguments, we note that "Mexico does not question that the Panel has jurisdiction to hear the United States' claims."[85] Moreover, Mexico does not claim "that there are legal obligations under the NAFTA or any other international agreement to which Mexico and the United States are both parties, which might raise legal impediments to the Panel hearing this case".[86] Instead, Mexico's position is that, although the Panel had the authority to rule on the merits of the United States' claims, it also had the "implied power" to abstain from ruling on them[87], and "should have exercised this power in the circumstances of this dispute."[88] Hence, the issue before us in this appeal is not whether the Panel was legally precluded from ruling on the United States' claims that were before it, but, rather, whether the Panel could decline, and should have declined, to exercise jurisdiction with respect to the United States' claims under Article III of the GATT 1994 that were before it.

45. Turning to Mexico's arguments on appeal, we note, first, Mexico's argument that WTO panels, like other international bodies and tribunals, "have certain implied jurisdictional powers that derive from their nature as adjudicative bodies"[89], and thus have a basis for declining to exercise jurisdiction. We agree with Mexico that WTO panels have certain powers that are inherent in their

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[85]Mexico's appellant's submission, para. 71 ("*México no discute que el Grupo Especial tiene competencia para resolver la reclamación que Estados Unidos ha interpuesto*") (quoting Mexico's response to Question 35 posed by the Panel; Panel Report, p. C-16). Mexico confirmed this point in response to questioning at the oral hearing.

[86]Panel Report, para. 7.13. In response to questioning at the oral hearing, Mexico argued that the panel in *Argentina – Poultry Anti-Dumping Duties* "at least contemplated the existence of a situation where an impediment found in another agreement might give rise to declining jurisdiction". The panel in *Argentina – Poultry Anti-Dumping Duties* referred to Article 1 of the Protocol of Olivos, which provides that, once a party decides to bring a case under either the MERCOSUR or WTO dispute settlement forum, that party may not bring a subsequent case regarding the same subject-matter in the other forum, and went on to state:

> The Protocol of Olivos ... does not change our assessment, since that Protocol has not yet entered into force, and in any event it does not apply in respect of disputes already decided in accordance with the MERCOSUR Protocol of Brasilia. Indeed, the fact that parties to MERCOSUR saw the need to introduce the Protocol of Olivos suggests to us that they recognised that (in the absence of such Protocol) a MERCOSUR dispute settlement proceeding could be followed by a WTO dispute settlement proceeding in respect of the same measure.

(Panel Report, *Argentina – Poultry Anti-Dumping Duties*, para. 7.38) (footnote omitted)

[87]Thus, Mexico suggested that, in the circumstances of this dispute, it would not have been "appropriate" for the Panel "to issue findings on the merits of the United States' claims." (Panel Report, para. 7.11 (referring to Mexico's first written submission to the Panel, paras. 102-103))

[88]Mexico's appellant's submission, para. 72 ("*debió haber ejercido esa facultad en las circunstancias de esta disputa*").

[89]*Ibid*., para. 65 ("*tienen ciertas facultades implícitas en relación con su competencia, las cuales derivan de su propia naturaleza como órganos jurisdiccionales*").

adjudicative function. Notably, panels have the right to determine whether they have jurisdiction in a given case, as well as to determine the scope of their jurisdiction. In this regard, the Appellate Body has previously stated that "it is a widely accepted rule that an international tribunal is entitled to consider the issue of its own jurisdiction on its own initiative, and to satisfy itself that it has jurisdiction in any case that comes before it."[90] Further, the Appellate Body has also explained that panels have "a margin of discretion to deal, always in accordance with due process, with specific situations that may arise in a particular case and that are not explicitly regulated."[91] For example, panels may exercise judicial economy, that is, refrain from ruling on certain claims, when such rulings are not necessary "to resolve the matter in issue in the dispute".[92] The Appellate Body has cautioned, nevertheless, that "[t]o provide only a partial resolution of the matter at issue would be false judicial economy."[93]

46. In our view, it does not necessarily follow, however, from the existence of these inherent adjudicative powers that, once jurisdiction has been validly established, WTO panels would have the authority to decline to rule on the entirety of the claims that are before them in a dispute. To the contrary, we note that, while recognizing WTO panels' inherent powers, the Appellate Body has previously emphasized that:

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[90]Appellate Body Report, *US – 1916 Act*, footnote 30 to para. 54. See also Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 53. In that dispute, the Appellate Body also stated that:

> … panels have to address and dispose of certain issues of a fundamental nature, even if the parties to the dispute remain silent on those issues. ... [P]anels cannot simply ignore issues which go to the root of their jurisdiction—that is, to their authority to deal with and dispose of matters. Rather, panels must deal with such issues—if necessary, on their own motion—in order to satisfy themselves that they have authority to proceed.

(Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 36)

[91]Appellate Body Report, *EC – Hormones*, footnote 138 to para. 152. See also Appellate Body Report, *US – FSC (Article 21.5 – EC)*, paras. 247-248.

[92]Appellate Body Report, *US – Wool Shirts and Blouses*, p. 19, DSR 1997:I, 323, at 340. Mexico referred, in its appellant's submission, to a panel's discretion to apply judicial economy as "an example of situations where WTO panels have refrained from exercising validly established jurisdiction on certain claims that are before them." (Mexico's appellant's submission, para. 68 ("*un ejemplo de situaciones en las que grupos especiales de la OMC se han abstenido de resolver ciertas reclamaciones sobre las cuales tienen competencia sustantiva validamente establecida*")) Mexico clarified at the oral hearing, however, that "it is clear that in the context of the exercise of judicial economy a panel cannot decline entirely to exercise jurisdiction." The United States noted, in this regard, that the doctrine of judicial economy "does not relieve a panel from its duty to carry out its mandate under Articles 7 and 11 of the DSU to resolve the dispute" before it. (United States' appellee's submission, para. 130)

[93]Appellate Body Report, *Australia – Salmon*, para. 223.

> Although panels enjoy some discretion in establishing their own working procedures, *this discretion does not extend to modifying the substantive provisions of the DSU. … Nothing in the DSU gives a panel the authority either to disregard or to modify ... explicit provisions of the DSU.*[94] (emphasis added)

47. With these considerations in mind, we examine the scope of a panel's jurisdictional power as defined, in particular, in Articles 3.2, 7.1, 7.2, 11, 19.2, and 23 of the DSU. Mexico argues that "[t]here is nothing in the DSU ... that explicitly rules out the existence of"[95] a WTO panel's power to decline to exercise its jurisdiction even in a case that is properly before it.

48. We first address Article 7 of the DSU, which governs the terms of reference of panels. Article 7 of the DSU states, in its first paragraph, that panels shall have the following terms of reference:

> "To examine, in the light of the relevant provisions in (name of the covered agreement(s) cited by the parties to the dispute), the matter referred to the DSB by (name of party) in document … and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in that/those agreement(s)."

The Panel in this dispute was established with standard terms of reference[96], which instructed the Panel to "examine" the United States' claims that were before it and to "make findings" with respect to consistency of the measures at issue with Article III of the GATT 1994.

49. The second paragraph of Article 7 further stipulates that "[p]anels shall address the relevant provisions in any covered agreement or agreements cited by the parties to the dispute." The use of the words "shall address" in Article 7.2 indicates, in our view, that panels are required to address the relevant provisions in any covered agreement or agreements cited by the parties to the dispute.[97]

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[94]Appellate Body Report, *India – Patents (US)*, para. 92.

[95]Mexico's appellant's submission, para. 65 ("*Nada en el ESD ... explícitamente descarta que ... existan*").

[96]The Panel's terms of reference in this dispute were as follows:

> To examine, in the light of the relevant provisions of the covered agreements cited by the United States in document WT/DS308/4, the matter referred to the DSB by the United States in that document, and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements.

(WT/DS308/5/Rev.1, para. 2)

[97]In this regard, we further note the Appellate Body's statement that, "as a matter of due process, and the proper exercise of the judicial function, panels are required to address issues that are put before them by the parties to a dispute." (Appellate Body Report, *Mexico – Corn Syrup (Article 21.5 – US)*, para. 36)

50. We turn next to Article 11 of the DSU, which provides that:

> The function of panels is to assist the DSB in discharging its responsibilities under this Understanding and the covered agreements. Accordingly, 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, 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. …

51. Article 11 of the DSU states that panels *should* make an objective assessment of the matter before them. The Appellate Body has previously held that the word "should" can be used not only "to imply an exhortation, or to state a preference", but also "to express a duty [or] obligation".[98] The Appellate Body has repeatedly ruled that a panel would not fulfil its mandate if it were not to make an objective assessment of the matter.[99] Under Article 11 of the DSU, a panel is, therefore, charged with the *obligation* to "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." Article 11 also requires that a panel "make such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the covered agreements." It is difficult to see how a panel would fulfil that obligation if it declined to exercise validly established jurisdiction and abstained from making any finding on the matter before it.

52. Furthermore, Article 23 of the DSU states that Members of the WTO *shall* have recourse to the rules and procedures of the DSU when they "seek the redress of a violation of obligations ... under the covered agreements". As the Appellate Body has previously explained, "allowing measures to be the subject of dispute settlement proceedings ... is consistent with the comprehensive nature of the right of Members to resort to dispute settlement to 'preserve [their] rights and obligations … under the covered agreements, and to clarify the existing provisions of those agreements'."[100] We also note in this regard that Article 3.3 of the DSU provides that the "prompt settlement of situations in which *a Member considers* that any benefits accruing to it directly or indirectly under the covered agreements are being impaired by measures taken by another Member is essential to the effective

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[98]Appellate Body Report, *Canada – Aircraft*, para. 187 (quoting *The Concise Oxford English Dictionary* (Clarendon Press, 1995), p. 1283).

[99]See, for instance, Appellate Body Report, *EC – Export Subsidies on Sugar*, paras. 329 and 335. See also Appellate Body Report, *Canada – Aircraft*, paras. 187-188; and Appellate Body Report, *EC – Hormones*, para. 133.

[100]Appellate Body Report, *US – Corrosion-Resistant Steel Sunset Review*, para. 89. (footnote omitted)

functioning of the WTO".[101] The fact that a Member may initiate a WTO dispute whenever it considers that "any benefits accruing to [that Member] are being impaired by measures taken by another Member" implies that that Member is *entitled* to a ruling by a WTO panel.

53. A decision by a panel to decline to exercise validly established jurisdiction would seem to "diminish" the right of a complaining Member to "seek the redress of a violation of obligations" within the meaning of Article 23 of the DSU, and to bring a dispute pursuant to Article 3.3 of the DSU. This would not be consistent with a panel's obligations under Articles 3.2 and 19.2 of the DSU.[102] We see no reason, therefore, to disagree with the Panel's statement that a WTO panel "would seem … not to be in a position to choose freely whether or not to exercise its jurisdiction."[103]

54. Mindful of the precise scope of Mexico's appeal[104], we express no view as to whether there may be other circumstances in which legal impediments could exist that would preclude a panel from ruling on the merits of the claims that are before it. In the present case, Mexico argues that the United States' claims under Article III of the GATT 1994 are inextricably linked to a broader dispute[105], and

[101](emphasis added) Thus, the Appellate Body has explained that there is "little in the DSU that explicitly limits the rights of WTO Members to bring an action". (Appellate Body Report, *EC – Export Subsidies on Sugar*, para. 312) In a similar vein, the Appellate Body has also observed that a WTO "Member has broad discretion in deciding whether to bring a case against another Member under the DSU." (Appellate Body Report, *EC – Bananas III*, para. 135) Further, Article 3.7 of the DSU states that "[b]efore bringing a case, a Member shall exercise *its judgement* as to whether action under these procedures would be fruitful." (emphasis added) Finally, Article 3.10 of the DSU stipulates that "if a dispute arises, *all Members will engage* in these procedures *in good faith in an effort to resolve the dispute*." (emphasis added)

[102]Article 3.2 of the DSU provides that "[r]ecommendations and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements."

Article 19.2 of the DSU states that "[i]n accordance with paragraph 2 of Article 3, in their findings and recommendations, the panel and Appellate Body cannot add to or diminish the rights and obligations provided in the covered agreements."

[103]Panel Report, para. 7.8.

[104]See *supra*, para. 44 and footnote 85 thereto.

[105]Mexico's appellant's submission, para. 73.

that only a NAFTA panel could resolve the dispute as a whole.[106] Nevertheless, Mexico does not take issue with the Panel's finding that "neither the subject matter nor the respective positions of the parties are identical in the dispute under the NAFTA ... and the dispute before us."[107] Mexico also stated that it could not identify a legal basis that would allow it to raise, in a WTO dispute settlement proceeding, the market access claims it is pursuing under the NAFTA.[108] It is furthermore undisputed that no NAFTA panel as yet has decided the "broader dispute" to which Mexico has alluded. Finally, we note that Mexico has expressly stated that the so-called "exclusion clause" of Article 2005.6 of the NAFTA[109] had not been "exercised".[110] We do not express any view on whether a legal impediment to

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[106]In its appellant's submission, Mexico explains that, in 1998, it initiated NAFTA dispute settlement proceedings because it was of the view that the United States was acting inconsistently with its obligation under the NAFTA relating to market access for Mexican sugar to the United States market. In 2000, Mexico requested the establishment of a panel under Article 2008 of the NAFTA. Subsequently, according to Mexico, it appointed its panelists to the NAFTA panel; however, the United States failed to appoint its panelists and also instructed the United States' Section of the NAFTA Secretariat not to appoint panelists. (Mexico's appellant's submission, paras. 15-27)

As a result, "[n]o further step could be taken by Mexico to form the NAFTA panel and have its grievance heard." (Mexico's appellant's submission, para. 28 ("*No había otros pasos que México pudiera dar conforme a las disposiciones del tratado para conseguir integrar el panel y que su agravio fuera oído*")) Mexico explains that it subsequently adopted the measures at issue in this dispute "to compel the United States to comply with its obligations and [to] protect [Mexico's] own legal and commercial interests." (*Ibid*., para. 42 ("*para mover a Estados Unidos a cumplir con sus obligaciones, a la vez que protegió [los] legítimos intereses jurídicos y comerciales [de México]*"))

The United States disputes these arguments by Mexico and argues that "the Appellate Body [should not] undertake itself to assess the correctness of Mexico's assertions as to what the NAFTA requires." (United States' appellee's submission, para. 18) It submits that, if the WTO dispute settlement were to "become a forum for WTO Members to ... obtain findings as to the consistency of another Member's measure with any non-WTO agreement", this "would be a departure from the function the WTO dispute settlement system was established to serve". (*Ibid*., para. 41) The United States also submits that "it is in full compliance with its obligations under NAFTA's dispute settlement mechanism." (*Ibid*., para. 84)

While these NAFTA issues have been described by the parties by way of background to the WTO dispute, neither the Panel or the Appellate Body was called upon to examine these issues.

[107]Panel Report, para. 7.14. The Panel noted, in this regard, that:

> [i]n the present case, the complaining party is the United States and the measures in dispute are allegedly imposed by Mexico. In the NAFTA case, the situation appears to be the reverse: the complaining party is Mexico and the measures in dispute are allegedly imposed by the United States. As for the subject matter of the claims, in the present case the United States is alleging discriminatory treatment against its products resulting from internal taxes and other internal measures imposed by Mexico. In the NAFTA case, instead, Mexico is arguing that the United States is violating its market access commitments under the NAFTA.

[108]Mexico's response to questioning at the oral hearing.

[109]Article 2005.6 of the NAFTA provides:

> Once dispute settlement procedures have been initiated under Article 2007 or dispute settlement proceedings have been initiated under the GATT, *the forum selected shall be used to the exclusion of the other, unless a Party makes a request pursuant to paragraph 3 or 4*. (emphasis added)

[110]Mexico's response to questioning at the oral hearing.

the exercise of a panel's jurisdiction would exist in the event that features such as those mentioned above were present.[111] In any event, we see no legal impediments applicable in this case.

55. Finally, as we understand it, Mexico's position is that the "applicability" of its WTO obligations towards the United States would be "call[ed] into question"[112] as a result of the United States having prevented Mexico, by an illegal act (namely, the alleged refusal by the United States to nominate panelists to the NAFTA panel), from having recourse to the NAFTA dispute settlement mechanism to resolve a bilateral dispute between Mexico and the United States regarding trade in sweeteners.[113] Specifically, Mexico refers to the ruling of the Permanent Court of International Justice (the "PCIJ") in the *Factory at Chorzów* case, and "calls into question the 'applicability' of its WTO obligations towards the United States in the context of this dispute".[114]

56. Mexico's arguments, as well as its reliance on the ruling in *Factory at Chorzów*, is misplaced. Even assuming, *arguendo*, that the legal principle reflected in the passage referred to by Mexico is applicable within the WTO dispute settlement system, we note that this would entail a determination whether the United States has acted consistently or inconsistently with its NAFTA obligations.[115] We see no basis in the DSU for panels and the Appellate Body to adjudicate non-WTO disputes. Article 3.2 of the DSU states that the WTO dispute settlement system "serves to preserve the rights and obligations of Members under the *covered agreements*, and to clarify the existing provisions of *those agreements*". (emphasis added) Accepting Mexico's interpretation would imply that the WTO dispute settlement system could be used to determine rights and obligations outside the covered agreements. In light of the above, we do not see how the PCIJ's ruling in *Factory at Chorzów* supports Mexico's position in this case.

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[111]In this context, Mexico has alluded to paragraph 7.38 of the Panel Report in *Argentina – Poultry Anti-Dumping Duties*. See also *supra*, footnote 86.

[112]Mexico's appellant's submission, para. 73 ("*[es] cuestion[able]*").

[113]See Panel Report, para. 7.14.

[114]Mexico's appellant's submission, para. 73 ("*cuestiona que sus obligaciones sean aplicables frente a Estados Unidos a la luz del siguiente principio general del derecho internacional*"). The passage of the ruling that Mexico refers to reads as follows:

> … one party cannot avail himself of the fact that the other has not fulfilled some obligation, or has not had recourse to some means of redress, if the former party has, by some illegal act, prevented the latter from fulfilling the obligation in question, or from having recourse to the tribunal which would have been open to him.

(Permanent Court of International Justice, *Factory at Chorzów (Germany v. Poland)* (Jurisdiction), 1927, PCIJ Series A, No. 9, p. 31) (underlining added by Mexico omitted)

[115]We also note that the ruling of the PCIJ in the *Factory at Chorzów* case relied on by Mexico was made in a situation in which the party objecting to the exercise of jurisdiction by the PCIJ was the party that had committed the act alleged to be illegal. In the present case, the party objecting to the exercise of jurisdiction by the Panel (Mexico) relies instead on an allegedly illegal act committed by the other party (the United States).

57. For all these reasons, we *uphold* the Panel's conclusion, in paragraphs 7.1, 7.18, and 9.1 of the Panel Report, that "under the DSU, it ha[d] no discretion to decline to exercise its jurisdiction in the case that ha[d] been brought before it." Having upheld this conclusion, we *find* it unnecessary to rule in the circumstances of this appeal on the propriety of exercising such discretion.[116]

V. Article XX(d) of the GATT 1994

A. *Introduction*

58. We turn now to Mexico's claim that the Panel erred in finding that the challenged measures are not justified under Article XX(d) of the GATT 1994. Before proceeding, we note that Mexico has not appealed the Panel's conclusion that the challenged measures are inconsistent with Article III of the GATT 1994.[117]

59. Mexico argued before the Panel that its "measures are 'necessary to secure compliance' by the United States with the United States' obligations under the NAFTA, an international agreement that is a law not inconsistent with the provisions of the GATT 1994."[118] The United States responded that "the NAFTA is not a 'law or regulation,' and Mexico's taxes are not 'necessary to secure compliance.'"[119]

60. The Panel began its analysis by looking at the meaning of the terms "to secure compliance". According to the Panel, "to secure compliance" means "to *enforce* compliance".[120] The Panel noted that "the notion of enforcement contains a concept of action within a hierarchical structure that is associated with the relation between the state and its subjects".[121] It further observed that Article XX(d) "is concerned with action at a domestic rather than international level."[122] Based on this reasoning, the Panel concluded that "the phrase 'to secure compliance' in Article XX(d) does not apply to measures taken by a Member in order to induce another Member to comply with obligations owed to it under a non-WTO treaty."[123]

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[116]Panel Report, paras. 7.1 and 7.18.

[117]Therefore, we express no view on the Panel's interpretation of Article III in this case.

[118]Panel Report, para. 8.162 (referring to Mexico's first written submission to the Panel, paras. 117-118 and 125).

[119]*Ibid*., para. 8.163.

[120]*Ibid*., para. 8.175. (emphasis added)

[121]*Ibid*., para. 8.178.

[122]*Ibid*., para. 8.179.

[123]*Ibid*., para. 8.181.

61. Having interpreted the terms "to secure compliance", the Panel proceeded to examine whether Mexico's measures are designed to secure compliance. The Panel explained that "when enforcement action is taken within a Member's legal system there will normally be no doubt, provided the action is pointed at the right target, that it will achieve that target."[124] In contrast, "the outcome of international countermeasures, such as those adopted by Mexico, is inherently unpredictable".[125] Therefore, the Panel reasoned, international countermeasures are "not eligible to be considered as measures 'to secure compliance' within the meaning of Article XX(d)."[126] The Panel added that "even if the assumption were to be made in the abstract that international countermeasures are potentially capable of qualifying as measures designed to secure compliance, the Panel's conclusion would be that Mexico has not established that its measures contribute to securing compliance in the circumstances of this case."[127] Thus, the Panel rejected Mexico's argument that "the challenged tax measures are *designed* to secure compliance by the United States with laws or regulations."[128]

62. The Panel then examined whether the challenged measures would fall within the meaning of the terms "laws or regulations" in Article XX(d). The Panel underscored the link between the terms "to secure compliance" and the terms "laws and regulations" as set out in Article XX(d). It indicated that the same reasoning that applies in determining whether Mexico's measures are measures "to secure compliance" must also apply in determining whether the measures are "laws or regulations" within the meaning of Article XX(d).[129] In the Panel's view, "the conclusion that these words refer to enforcement action within a particular domestic legal system, and that they do not extend to international action of the type taken by Mexico, necessarily applies to both parts of this expression."[130] The Panel further observed that, "even if it were to assume that the expression 'laws or regulations' in Article XX(d) could include international agreements such as the NAFTA, it would in any event conclude that, on the facts of the case, because of the uncertainty of their consequences, the challenged measures are not designed 'to secure compliance with laws or regulations which are not inconsistent with the provisions' of GATT 1994."[131]

63. Therefore, the Panel concluded that "Mexico has not demonstrated that the challenged measures are designed 'to secure compliance with laws or regulations', within the meaning of

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[124]Panel Report, para. 8.185.

[125]*Ibid*., para. 8.186.

[126]*Ibid*.

[127]*Ibid*.

[128]*Ibid*., para. 8.190. (original emphasis)

[129]*Ibid*., para. 8.194.

[130]*Ibid*.

[131]*Ibid*., para. 8.197.

Article XX(d) of the GATT 1994."[132] Having made this finding, the Panel did not consider that it needed to examine whether Mexico's measures are "necessary" within the meaning of Article XX(d)[133], and whether the measures satisfy the requirements set out in the chapeau of Article XX.[134] Consequently, the Panel concluded that "Mexico has not established that the challenged measures are justified under Article XX of the GATT 1994."[135]

64. On appeal, Mexico seeks review of the Panel's conclusion that Mexico's measures are not justified under Article XX(d) of the GATT 1994. According to Mexico, the Panel incorrectly interpreted the terms "to secure compliance" as excluding international countermeasures[136], and this error led the Panel to incorrectly interpret the terms "laws or regulations" in Article XX(d).[137] Mexico argues that the terms "laws or regulations" are "broad enough to include international agreements such as the NAFTA."[138] Mexico points out that "the use of the terms 'laws' and 'regulations' elsewhere in the GATT 1994 and in other WTO agreements does not demonstrate that such terms exclude international law rules."[139]

65. The United States responds that the Panel properly found that Mexico's measures are not justified under Article XX(d). It asserts that "the ordinary meaning of 'laws' and 'regulations' is that these are rules (e.g., in the form of a statute) issued by a government and not obligations under an international agreement."[140] The United States further explains that Mexico's interpretation of Article XX(d) is in conflict with Article 23 of the DSU, by allowing a WTO Member to take action outside the rules of the DSU to secure compliance with another Member's obligations under any international agreement, including the WTO agreements.[141] It would also undermine Article 22 of the DSU by "permit[ting] the suspension of concessions ... without DSB authorization and without any requirement to adhere to the rules established" in that provision.[142]

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[132]Panel Report, para. 8.198.

[133]*Ibid*., para. 8.202.

[134]*Ibid*., para. 8.203.

[135]*Ibid*., para. 8.204.

[136]Mexico's appellant's submission, para. 79 and footnote 49 thereto.

[137]*Ibid*., para. 126.

[138]*Ibid*., para. 129 ("*suficientemente amplia para incluir tratados internacionales, como el TLCAN*").

[139]*Ibid*. ("*el empleo de los términos "leyes" y "reglamentos" en el resto del GATT de 1994 y en otros Acuerdos de la OMC no demuestran que los tales términos excluyen las reglas del derecho internacional*"). (footnote omitted)

[140]United States' appellee's submission, para. 30 (referring to definitions in *Black's Law Dictionary*, (1990), p. 816).

[141]*Ibid*., para. 37.

[142]*Ibid*., para. 38. (footnote omitted)

B. *Analysis*

1. Are Mexico's Measures Justified under Article XX(d)?

66. Article XX(d) of the GATT 1994 reads:

> *General Exceptions*
>
> Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures:
>
> ...
>
> (d) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including those relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the protection of patents, trade marks and copyrights, and the prevention of deceptive practices[.]

67. The Appellate Body explained, in *Korea – Various Measures on Beef*, that two elements must be shown "[f]or a measure, otherwise inconsistent with GATT 1994, to be justified provisionally under paragraph (d) of Article XX".[143] The first element is that "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", and the second is that "the measure must be 'necessary' to secure such compliance."[144] The Appellate Body also explained that "[a] Member who invokes Article XX(d) as a justification has the burden of demonstrating that these two requirements are met."[145]

68. In our view, the central issue raised in this appeal is whether the terms "to secure compliance with laws or regulations" in Article XX(d) of the GATT 1994 encompass WTO-inconsistent measures applied by a WTO Member to secure compliance with another WTO Member's obligations under an international agreement.

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[143]Appellate Body Report, *Korea – Various Measures on Beef*, para. 157.

[144]*Ibid*.

[145]*Ibid*. (referring to Appellate Body Report, *US – Gasoline*, pp. 22-23, DSR 1996:I, 3, at 20-21; Appellate Body Report, *US – Wool Shirts and Blouses*, pp. 14-16, DSR 1997:I, 323, at 335-337; and GATT Panel Report, *US – Section 337*, para. 5.27).

69. In order to answer this question, we consider it more helpful to begin our analysis with the terms "laws or regulations" in Article XX(d) (which we consider to be pivotal here) rather than to begin with the analysis of the terms "to secure compliance", as did the Panel. The terms "laws or regulations" are generally used to refer to domestic laws or regulations. As Mexico and the United States note, previous GATT and WTO disputes in which Article XX(d) has been invoked as a defence have involved domestic measures.[146] Neither disputes that the expression "laws or regulations" encompasses the rules adopted by a WTO Member's legislative or executive branches of government. We agree with the United States that one does not immediately think about international law when confronted with the term "laws" in the plural.[147] Domestic legislative or regulatory acts sometimes may be intended to implement an international agreement. In such situations, the origin of the rule is international, but the implementing instrument is a domestic law or regulation.[148] In our view, the terms "laws or regulations" refer to rules that form part of the domestic legal system of a WTO Member.[149] Thus, the "laws or regulations" with which the Member invoking Article XX(d) may seek to secure compliance do not include obligations of *another* WTO Member under an international agreement.

70. The illustrative list of "laws or regulations" provided in Article XX(d) supports the conclusion that these terms refer to rules that form part of the domestic legal system of a WTO Member.[150] This list includes "[laws or regulations] relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the protection of patents, trade marks and copyrights, and the prevention of deceptive practices". These matters are typically the subject of domestic laws or regulations, even though some of these matters may also be the subject of

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[146]United States' appellee's submission, footnote 62 to para. 39; Mexico's response to questioning at the oral hearing.

[147]Panel Report, footnote 419 to para. 8.193; United States' appellee's submission, para. 31.

[148]In some WTO Members, certain international rules may have direct effect within their domestic legal systems without requiring implementing legislation. In such circumstances, these rules also become part of the domestic law of that Member.

[149]The European Communities notes that:

> [i]t is entirely possible that international agreements may be incorporated into the domestic legal order in such a way that they can be invoked as against individuals, and enforce[d] against them. If this is the case, the international agreement, albeit international in origin, may be regarded as having become an integral part of the domestic legal order of such Member, and thus a law or regulation within the meaning of Article XX (d) [of the] GATT [1994].

(European Communities' third participant's submission, para. 41)

[150]The participants agree that the list in Article XX(d) is not exhaustive. (See Mexico's response to Question 67 posed by the Panel after the second Panel meeting; Panel Report, p. C-61; United States' response to Question 31 posed by the Panel after the first Panel meeting; Panel Report, p. C-42; and United States' response to Question 67 posed by the Panel after the second Panel meeting; Panel Report, pp. C-79-C-80)

international agreements. The matters listed as examples in Article XX(d) involve the regulation by a government of activity undertaken by a variety of economic actors (e.g., private firms and State enterprises), as well as by government agencies. For example, matters "relating to customs enforcement" will generally involve rights and obligations that apply to importers or exporters, and matters relating to "the protection of patents, trade marks and copyrights" will usually regulate the use of these rights by the intellectual property right holders and other private actors.[151] Thus, the illustrative list reinforces the notion that the terms "laws or regulations" refer to rules that form part of the domestic legal system of a WTO Member and do not extend to the international obligations of another WTO Member.[152]

71. Our understanding of the terms "laws or regulations" is consistent with the context of Article XX(d). As the United States points out[153], other provisions of the covered agreements refer expressly to "international obligations" or "international agreements". For example, paragraph (h) of Article XX refers to "obligations under any intergovernmental commodity agreement". The express language of paragraph (h) would seem to contradict Mexico's suggestion that international agreements are implicitly included in the terms "laws or regulations".[154] The United States and China also draw our attention to Article X:1 of the GATT 1994[155], which refers to "[l]aws, regulations, judicial decisions and administrative rulings" and to "[a]greements affecting international trade policy which are in force between a government … of any Member and the government … of any other Member". Thus, a distinction is drawn in the same provision between "laws [and] regulations" and "international agreements". Such a distinction would have been unnecessary if, as Mexico argues, the terms "laws" and "regulations" were to encompass international agreements that have not been incorporated, or do not have direct effect in, the domestic legal system of the respective WTO Member. Thus, Articles X:1 and XX(h) of the GATT 1994 do not lend support to interpreting the terms "laws or

[151]European Communities' third participant's submission, para. 38.

[152]The United States also points out that the terms "laws or regulations" are qualified by the requirement that they not be "inconsistent" with the GATT 1994. The United States explains that the word "inconsistent" appears elsewhere in the GATT 1994 in connection with domestic measures. In contrast, when referring to treaty obligations, the WTO agreements use the word "conflict". (United States' appellee's submission, para. 33) In our view, this distinction supports the position that the terms "laws or regulations" refer to the rules that are part of the domestic legal system of a WTO Member, including international rules that have been incorporated or have direct effect in a particular domestic legal system.

[153]United States' appellee's submission, para. 34.

[154]If an international commodity agreement contains GATT-inconsistent provisions, Article XX(h) would still serve the purpose of justifying such an agreement, even if it could not be justified under Article XX(d).

[155]United States' appellee's submission, para. 35; China's third participant's submission, para. 21.

regulations" in Article XX(d) as including the international obligations of a Member other than that invoking the provision.[156]

72. We turn to the terms "to secure compliance", which were the focus of the Panel's reasoning and are the focus of Mexico's appeal. The terms "to secure compliance" speak to the types of measures that a WTO Member can seek to justify under Article XX(d). They relate to the design of the measures sought to be justified.[157] There is no justification under Article XX(d) for a measure that is not designed "to secure compliance" with a Member's laws or regulations. Thus, the terms "to secure compliance" do not expand the scope of the terms "laws or regulations" to encompass the international obligations of another WTO Member. Rather, the terms "to secure compliance" circumscribe the scope of Article XX(d).

73. Mexico takes issue with several aspects of the Panel's reasoning related to the interpretation of the terms "to secure compliance". We recall that, according to the Panel, "[t]he context in which the expression is used makes clear that 'to secure compliance' is to be read as meaning to enforce compliance."[158] The Panel added that, in contrast to enforcement action taken within a Member's legal system, "the effectiveness of [Mexico's] measures in achieving their stated goal—that of bringing about a change in the behaviour of the United States—seems ... to be inescapably uncertain."[159] Thus, the Panel concluded that "the outcome of international countermeasures, such as those adopted by Mexico, is inherently unpredictable".[160]

74. It is Mexico's submission that the Panel erred in requiring a degree of certainty as to the results achieved by the measure sought to be justified.[161] Mexico also asserts that the Panel, in its reasoning, incorrectly relied on the Appellate Body Report in *US – Gambling*.[162] We agree with

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[156]The Panel noted that there are examples of international "regulations" within the WTO agreements themselves. The Panel cited, as examples, Article VI of the *Marrakesh Agreement Establishing the World Trade Organization* that refers to "regulations" to be adopted by the Ministerial Conference, and Article VII that refers to "financial regulations" to be adopted by the General Council and to the "regulations" of the GATT 1947. (Panel Report, footnotes 423 and 424 to para. 8.195) Article XXIV of the GATT 1994 also uses the term "regulations" when referring to rules applied by free trade areas or customs unions. Nevertheless, we agree with Japan that, in these instances, the context makes it clear that the regulations are international in character. (Japan's third participant's submission, paras. 17-19)

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

[158]Panel Report, para. 8.175.

[159]*Ibid*., para. 8.185.

[160]*Ibid*., para. 8.186. See also Mexico's appellant's submission, paras. 104-116.

[161]The European Communities and Japan agree with Mexico that the Panel erred in implying that whether a measure falls within the meaning of the phrase "to secure compliance" depends on the degree of certainty that the measure will achieve its intended results. (European Communities' third participant's submission, para. 26; Japan's third participant's submission, para. 10)

[162]Panel Report, paras. 8.187-8.188 (referring to Appellate Body Report, *US – Gambling*, para. 317).

Mexico that the *US – Gambling* Report does not support the conclusion that the Panel sought to draw from it. The statement to which the Panel referred was made in the context of the examination of the "necessity" requirement in Article XIV(a) of the *General Agreement on Trade in Services*, and did not relate to the terms "to secure compliance". As the Appellate Body has explained previously, "the contribution made by the compliance measure to the enforcement of the law or regulation at issue"[163] is one of the factors that must be weighed and balanced to determine whether a measure is "necessary" within the meaning of Article XX(d). A measure that is not suitable or capable of securing compliance with the relevant laws or regulations will not meet the "necessity" requirement. We see no reason, however, to derive from the Appellate Body's examination of "necessity", in *US – Gambling*, a requirement of "certainty" applicable to the terms "to secure compliance".[164] In our view, a measure can be said to be designed "to secure compliance" even if the measure cannot be guaranteed to achieve its result with absolute certainty.[165] Nor do we consider that the "use of coercion"[166] is a necessary component of a measure designed "to secure compliance". Rather, Article XX(d) requires that the design of the measure contribute "to secur[ing] compliance with laws or regulations which are not inconsistent with the provisions of" the GATT 1994.

75. Nevertheless, while we agree with Mexico that the Panel's emphasis on "certainty" and "coercion" is misplaced, we consider that Mexico's arguments miss the point. Even if "international countermeasures" could be described as intended "to secure compliance", what they seek "to secure compliance with"—that is, the international obligations of another WTO Member—would be outside the scope of Article XX(d). This is because "laws or regulations" within the meaning of Article XX(d) refer to the rules that form part of the domestic legal order of the WTO Member invoking the provision and do not include the international obligations of *another* WTO Member.

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[163]Appellate Body Report, *Korea – Various Measures on Beef*, para. 164.

[164]We note that, at the request of the United States, the Panel clarified in the interim review phase that:

> … its reasoning does not focus on whether the achievement of Mexico's objective through the measures at issue is certain or uncertain. Rather, the Panel considers that international countermeasures (as the ones allegedly imposed by Mexico) are intrinsically unable to *secure* compliance of laws and regulations. In contrast, national measures are, beyond particular factual considerations, usually in a position to achieve [] that objective, through the use of coercion, if necessary.

(Panel Report, para. 6.12) (original italics; underlining added)

[165]The European Communities notes that "even within the domestic legal order of WTO Members, enforcement of laws and regulations may not simply be taken for granted, but may depend on numerous factors". (European Communities' third participant's submission, para. 28)

[166]Panel Report, para. 8.178.

76. Mexico finds support for its interpretation in the Appellate Body's rulings in *US – Shrimp* and *US – Shrimp (Article 21.5 – Malaysia)*.[167] We fail to see how these rulings support Mexico's position. In those cases, the United States sought to justify its measures under Article XX(g) of the GATT 1994, and the measures at issue were domestic laws and regulations of the United States.[168] The reference to the Inter-American Convention for the Protection and Conservation of Sea Turtles (the "Inter-American Convention") was made in the context of the examination of whether the measures constituted "a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail" for purposes of the chapeau of Article XX.[169] The United States, in those cases, did not argue that its measures were justified under Article XX(d) because they were intended to secure compliance with the obligations of another Member under the Inter-American Convention. In the present case, Mexico seeks to justify its measures under paragraph (d) of Article XX, and not under paragraph (g). Moreover, Mexico not only refers to the NAFTA in relation to the chapeau of Article XX, but also seeks justification for its measures under paragraph (d) on the basis that they are allegedly intended to secure compliance with the United States' NAFTA obligations.

77. We observe, furthermore, that Mexico's interpretation of Article XX(d) disregards the fact that the GATT 1994 and the DSU specify the actions that a WTO Member may take if it considers that another WTO Member has acted inconsistently with its obligations under the GATT 1994 or any of the other covered agreements. As the United States points out[170], Mexico's interpretation of the terms "laws or regulations" as including international obligations of another WTO Member would logically imply that a WTO Member could invoke Article XX(d) to justify also measures designed "to secure compliance" with that other Member's WTO obligations. By the same logic, such action under Article XX(d) would evade the specific and detailed rules that apply when a WTO Member seeks to take countermeasures in response to another Member's failure to comply with rulings and recommendations of the DSB pursuant to Article XXIII:2 of the GATT 1994 and Articles 22 and 23 of the DSU.[171] Mexico's interpretation would allow WTO Members to adopt WTO-inconsistent measures based upon a *unilateral* determination that another Member has breached its WTO obligations, in contradiction with Articles 22 and 23 of the DSU and Article XXIII:2 of the GATT 1994.

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[167]Mexico's appellant's submission, paras. 174-178.

[168]See Appellate Body Report, *US – Shrimp*, paras. 2-6.

[169]See *ibid*., paras. 169-172; and Appellate Body Report, *US – Shrimp (Article 21.5 – Malaysia*), para. 128. See also United States' appellee's submission, para. 108.

[170]United States' appellee's submission, para. 37.

[171]Mexico's interpretation would also undermine the limitations in paragraphs 3 and 4 of Article 22 as to the magnitude and the trade sectors in which such countermeasures could be taken. (*Ibid*., paras. 37-38)

78. Finally, even if the terms "laws or regulations" do not go so far as to encompass the WTO agreements, as Mexico argues[172], Mexico's interpretation would imply that, in order to resolve the case, WTO panels and the Appellate Body would have to assume that there is a violation of the relevant international agreement (such as the NAFTA) by the complaining party, or they would have to assess whether the relevant international agreement has been violated. WTO panels and the Appellate Body would thus become adjudicators of non-WTO disputes.[173] As we noted earlier[174], this is not the function of panels and the Appellate Body as intended by the DSU.[175]

79. For these reasons, we agree with the Panel that Article XX(d) is not available to justify WTO-inconsistent measures that seek "to secure compliance" by another WTO Member with that other Member's international obligations. In sum, while we agree with the Panel's conclusion, several aspects of our reasoning set out above differ from the Panel's own reasoning. First, we conclude that the terms "laws or regulations" cover rules that form part of the domestic legal system of a WTO Member, including rules deriving from international agreements that have been incorporated into the domestic legal system of a WTO Member or have direct effect according to that WTO Member's legal system.[176] Second, we have found that Article XX(d) does not require the "use of coercion" nor that the measure sought to be justified results in securing compliance with absolute certainty. Rather, Article XX(d) requires that the measure be designed "to secure compliance with laws or regulations which are not inconsistent with the provisions of" the GATT 1994.[177] Finally, we do not endorse the Panel's reliance on the Appellate Body's interpretation in *US – Gambling* of the term "necessary" to interpret the terms "to secure compliance" in Article XX(d).[178]

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[172]At the oral hearing, Mexico argued that the terms "laws or regulations" would not include the WTO agreements because the latter are *lex specialis*.

[173]Article 3.2 of the DSU states that the WTO's dispute settlement system "serves to preserve the rights and obligations of Members under the *covered agreements*, and to clarify the existing provisions of *those agreements*". (emphasis added)

[174]See *supra*, para. 56.

[175]We note that, in its analysis, the Panel also referred to the negotiating history of the GATT 1947, and particularly to the rejection of a proposal presented by India during the negotiations on the International Trade Organization (the "ITO") Charter according to which Members would be permitted to justify, on a temporary basis, retaliatory measures under Article XX. (See Panel Report, para. 8.176 (referring to ITO Doc. E/PC/T/180 (19 August 1947), p. 97; and "Havana Charter for an International Trade Organization", United Nations Conference on Trade and Employment, Final Act and Related Documents (Lake Success, New York, April 1948), pp. 33-34)

[176]See *supra*, paras. 69-71.

[177]See *supra*, para. 74.

[178]See *supra*, para. 74.

80. Therefore, we *uphold*, albeit for different reasons, the Panel's conclusion, in paragraph 8.198 of the Panel Report, that Mexico's measures do not constitute measures "to secure compliance with laws or regulations", within the meaning of Article XX(d) of the GATT 1994.

2. Mexico's Request to Complete the Analysis

81. Mexico requests the Appellate Body to complete the analysis by examining whether Mexico's measures are "necessary", within the meaning of Article XX(d) of the GATT 1994, and meet the requirements of the chapeau of that Article.[179] Mexico's request is premised on the Appellate Body reversing the Panel's conclusion that the measures are not designed "to secure compliance with laws or regulations" within the meaning of Article XX(d). We have upheld the Panel's conclusion that Mexico's measures do not constitute measures "to secure compliance with laws or regulations" within the meaning of Article XX(d) of the GATT 1994. Therefore, the premise on which Mexico's request is predicated is not fulfilled and, consequently, it is not necessary for us to complete the analysis as requested by Mexico.[180]

3. Mexico's Claim under Article 11 of the DSU [181]

82. Mexico argues, "separately and in addition"[182] to the previous errors, that the Panel failed to make "an objective assessment of the facts", as required by Article 11 of the DSU, in finding that "Mexico has not established that its measures contribute to securing compliance in the circumstances of this case."[183] Mexico argues that "[t]he evidence on the record demonstrates that the effects of the measures at issue have contributed to securing compliance in the circumstances of this case, by changing the dynamic of the NAFTA dispute and forcing the United States to pay attention to

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[179]Mexico's appellant's submission, para. 138.

[180]See, for example, Appellate Body Report, *Dominican Republic – Import and Sale of Cigarettes*, para. 74.

[181]In its Notice of Appeal, Mexico claimed that the Panel "failed to make an objective assessment of the matter before it, including the facts of the case, inconsistently with its obligation under Article 11 of the DSU, with respect to Mexico's request for determinations of fact, status and relevance of the NAFTA dispute between the parties." (Mexico's Notice of Appeal (attached as Annex I to this Report), para. 4 (referring to Panel Report, paras. 8.231 and 8.232) (footnote omitted)) Mexico also asserted that "in concluding that international countermeasures cannot qualify for consideration as measures designed to 'secure compliance' within the meaning of Article XX(d) of the GATT 1994, the Panel improperly increased the obligations of WTO Members and reduced the rights of Members under the covered agreements." (*Ibid*., para. 5 (referring to Panel Report, paras. 8.181 and 8.186) (footnote omitted)) Mexico did not offer arguments to support these two claims in its appellant's submission. In response to questioning at the oral hearing, Mexico confirmed that it did not intend to pursue these claims further.

[182]Mexico's appellant's submission, heading III.E ("*independiente y adicional*").

[183]Panel Report, paragraph 8.186. See also, Mexico's Notice of Appeal, para. 3.

Mexico's grievances."[184] The United States submits that, contrary to Mexico's contention, the Panel did not "ignore" arguments or evidence submitted by Mexico.[185] The United States further explains that, in any event, Mexico's claim under Article 11 of the DSU "appears to be no more than a reiteration of its legal arguments that its ... measures are designed to 'secure compliance'".[186]

83. In Section B.1 above, we held that Mexico's measures do not constitute measures "to secure compliance with laws or regulations", within the meaning of Article XX(d) of the GATT 1994. Therefore, Mexico's claim under Article 11 of the DSU is predicated on an interpretation of Article XX(d) of the GATT 1994 that we have found to be incorrect. Since Mexico's measures cannot be justified under Article XX(d) as a *matter of law*, we reject Mexico's claim under Article 11 of the DSU.

4. Conclusion

84. For the reasons set out above, we *uphold* the Panel's conclusion, in paragraphs 8.204 and 9.3 of the Panel Report, that "Mexico has not established that the challenged measures are justified under Article XX of the GATT 1994".

VI. Findings and Conclusions

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

(a) upholds the Panel's conclusion, in paragraphs 7.1, 7.18, and 9.1 of the Panel Report, that, "under the DSU, it ha[d] no discretion to decline to exercise its jurisdiction in the case that ha[d] been brought before it";

(b) upholds the Panel's conclusion, in paragraph 8.198 of the Panel Report, that Mexico's measures do not constitute measures "to secure compliance with laws or regulations", within the meaning of Article XX(d) of the GATT 1994;

(c) rejects Mexico's claim that the Panel failed to fulfil its obligations under Article 11 of the DSU, in finding, in paragraph 8.186 of the Panel Report, that "Mexico has not established that its measures contribute to securing compliance in the circumstances of this case"; and

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[184]Mexico's appellant's submission, para. 167 ("*Las pruebas en el expediente demuestran que las medidas en cuestión no están desprovistas de efectos que contribuyen a lograr la observancia en las circunstancias de este caso, cambiando la dinámica en la controversia derivada del TLCAN y forzando a Estados Unidos a prestar atención a los agravios de México*").

[185]United States' appellee's submission, para. 118.

[186]*Ibid*.

(d) as a consequence, upholds the Panel's conclusion, in paragraphs 8.204 and 9.3 of the Panel Report, that "Mexico has not established that the challenged measures are justified under Article XX of the GATT 1994".

86. The Appellate Body recommends that the Dispute Settlement Body request Mexico to bring the measures that were found in the Panel Report to be inconsistent with the *General Agreement on Tariff and Trade 1994* into conformity with its obligations under that Agreement.

Signed in the original in Geneva this 8th day of February 2006 by:

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Yasuhei Taniguchi
Presiding Member

_____ _____

Merit E. Janow
Member

Giorgio Sacerdoti
Member

ANNEX I

WORLD TRADE ORGANIZATION

WT/DS308/10
6 December 2005

(05-5832)

Original: Spanish

MEXICO – TAX MEASURES ON SOFT DRINKS AND OTHER BEVERAGES

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

The following notification dated 6 December 2005, from the delegation of Mexico, is being circulated to Members.

Pursuant to Article 16 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") and Rule 20 of the *Working Procedures for Appellate Review*, Mexico hereby notifies its decision to appeal to the Appellate Body certain issues of law dealt with in the Report of the Panel on *Mexico – Tax Measures on Soft Drinks and Other Beverages* (WT/DS308/R) (the "Panel Report") and certain legal interpretations developed by the Panel in this dispute.

1. Mexico seeks review by the Appellate Body of the Panel's legal conclusion that it has no discretion to decline to exercise jurisdiction in this case and its determination that, even if it had such discretion, the facts in the record do not justify a refusal by the Panel to exercise jurisdiction in this case. This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations concerning Articles 3, 7, 11 and 19 of the DSU and Articles XXII and XXIII of the GATT 1994. These errors are contained, *inter alia*, in paragraphs 7.1 to 7.18, 8.215 to 8.230 and 9.1 of the Panel Report.

2. Mexico seeks review by the Appellate Body of the Panel's legal conclusion that the challenged tax measures are not justified under Article XX of the GATT 1994 as measures necessary to secure United States compliance with laws or regulations which are not inconsistent with the provisions of the GATT 1994. This conclusion is in error and is based on erroneous findings on issues of law and related legal interpretations concerning Article XX of the GATT 1994. Paragraphs 8.168 to 8.204 and 9.3 of the Panel Report, among others, contain such errors, including the following:

(a) The Panel's interpretation and application of the expression "to secure compliance" in Article XX(d) of the GATT 1994 and its conclusion that it does not apply to measures taken by a Member in order to induce another Member to comply with obligations owed to it under a non-WTO treaty.[1]

(b) The Panel's conclusion that the challenged tax measures "are not designed to secure compliance" within the meaning of Article XX(d) of the GATT 1994 and are not eligible for consideration under Article XX(d) of the GATT 1994.[2]

(c) The Panel's interpretation and application of the phrase "laws or regulations" contained in Article XX(d) of the GATT 1994 and its conclusion that this phrase does not cover international treaties such as NAFTA.[3]

(d) The Panel's failure to consider whether the Mexican measures are "necessary" to secure compliance with a law that is not inconsistent with the provisions of the GATT 1994.[4]

3. Mexico seeks review by the Appellate Body, in the light of DSU Article 11, of the Panel's conclusion that "Mexico has not established that its measures contribute to securing compliance in the circumstances of this case".[5] This conclusion does not reflect an objective approach to analysis of the available evidence on the effects of the Mexican measures, and is inconsistent with the treatment given by the Panel to relevant evidence. Accordingly, this conclusion is inconsistent with the Panel's duty to make an objective assessment of the matter before it.

4. Mexico considers that the Panel also failed to make an objective assessment of the matter before it, including the facts of the case, inconsistently with its obligation under Article 11 of the DSU, with respect to Mexico's request for determinations of fact, status and relevance of the NAFTA dispute between the parties.[6]

5. Mexico also considers that, in concluding that international countermeasures cannot qualify for consideration as measures designed to "secure compliance" within the meaning of Article XX(d) of the GATT 1994[7], the Panel improperly increased the obligations of WTO Members and reduced the rights of Members under the covered agreements.

6. In the event that the Appellate Body reverses the Panel's conclusion that Mexico's tax measures are not justified under Article XX(d) of the GATT 1994, Mexico requests that the Appellate Body complete the legal analysis under Article XX of the GATT 1994.

Those provisions of the covered agreements which Mexico considers the Panel to have interpreted or applied erroneously include Articles XX, XXII and XXIII of the GATT 1994 and Articles 3, 7, 11 and 19 of the DSU.

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[1] Panel Report, paragraphs 8.170 to 8.181.

[2] Panel Report, paragraphs 8.182 to 8.190 and 8.197 to 8.198.

[3] Panel Report, paragraphs 8.191 to 8.197.

[4] Panel Report, paragraphs 8.199 to 8.202.

[5] Panel Report, paragraph 8.186.

[6] Panel Report, paragraphs 8.231 and 8.232.

[7] Panel Report, paragraphs 8.181 and 8.186.