

Legal Assessment of Duty-Free Tobacco Regulations under International Trade Laws

P E I - K A N Y A N G *

I. ABSTRACT

Banning duty-free sales of tobacco products is one of the price and tax tobacco control measures that can effectively reduce the demand for tobacco use. The issue of duty-free tobacco has been addressed by the World Health Organization, prescribing relevant rules under the Framework Convention on Tobacco Control (FCTC) and the implementing Guidelines and its Protocol. While health experts tend to support a total ban on duty-free sales of tobacco products as such sales frustrate the effectiveness of tobacco control, the issue of banning duty-free tobacco was hotly debated among delegates to the FCTC, given that it would be a detriment to trade and fiscal interests. In addition to health concerns, a sound policy on duty-free tobacco involves a mixture of considerations regarding the nature of duty-free purchase as a legal tax avoidance instrument, unclear evidence of the extent of smuggling problems caused by duty-free sales and concerns over the compatibility with existing international trade rules. This paper tries to examine trade-related issues of regulating duty-free sales of tobacco products with particular emphasis on its consistency with international trade laws. As for the special concern expressed by the delegates over the legality of such a ban, this paper examines the compatibility of such regulations with relevant trade rules and finds that

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it is unlikely to become an obstacle for Parties to prohibit or restrict duty-free sales and/or importation of tobacco products. The real challenge lies at weighing different interests of multiple stakeholders in the process of domestic policy-making.

Keywords: duty-free sales, tax-free sales, illicit trade, tobacco control, FCTC, WHO, WTO

II. INTRODUCTION

Banning duty-free sales of tobacco products has been considered by the World Health Organization (WHO) as one of the important elements of price and tax measures to reduce the demand for tobacco consumption.¹ Article 6.2(b) of the Framework Convention on Tobacco Control (FCTC), the first treaty negotiated under the auspice of WHO, provides that each Party should “adopt or maintain, as appropriate, measures which may include ... prohibiting or restricting, as appropriate, sales to and/or importations by international travellers of tax- and duty-free tobacco products.”²

In order to further implement Article 6 of the FCTC, Parties to the FCTC reviewed the issue of duty-free tobacco when they negotiated the Protocol to Eliminate Illicit Trade in Tobacco Products (the Protocol)³ and the Guidelines for the Implementation of Article 6 of the WHO FCTC (Article 6 Guidelines).⁴ As a result of intense negotiation, the final text was agreed and prescribed in Article 13 of the Protocol and Section 6 of the Guidelines, adopted by the Conferences of Parties (COP) to the WHO FCTC in November 2012 and October 2014, respectively.

¹ World Health Org., Guidelines for Implementation of Article 6 of the WHO FCTC (Price and tax measures to reduce the demand for tobacco), FCTC/COP6(5), UNWHOOR, (2014) at 13-14.

² WHO Framework Convention on Tobacco Control, June 16, 2003, 2302 UNTS 166 art 6.2 at 8 (entered into force 27 February 2005 whqlibdoc.who.int/publications/2003/9241591013.pdf).

³ WHO Protocol to Eliminate Illicit Trade in Tobacco Products, 10 January 2013, (entered into force Sep 25, 2018).

⁴ WHO Article 6 Guidelines, *supra* note 1.

In the course of negotiation, some representatives were opposed to this ban based on the argument that duty-free sales of tobacco products were not problematic due to the relatively small scale of these sales in tobacco consumption,⁵ and that introducing such a ban caused more concerns over the consistency with existing international conventions.

Since purchasing duty-free tobacco products has been used by consumers as a legal tax avoidance instrument, a policy to prohibit or restrict duty-free sales of tobacco products should consider various aspects of policy interests such as international trade, public health, taxation policy, and customs regulations. Among others, opponents of a total ban on duty-free tobacco are often suspect of the connection between illicit trade and duty-free sales of tobacco products, either casting doubt over the effectiveness of such ban in controlling illicit trade in tobacco products or the existence of a causal relationship between the expansion of the illicit tobacco market and duty-free sales of tobacco products.⁶ Given that this linkage issue needs more empirical evidence to have a better picture of the magnitude of the problem, this paper instead focuses on the issue of potential conflicts of international norms, namely, the legal aspect of skepticism over banning duty-free sales of tobacco products.

To examine trade-related issues of regulating duty-free sales of tobacco products, this paper will explore relevant threshold questions as follows. Firstly, how has the issue of banning duty-free sales of tobacco products been addressed by the representatives of Parties to the FTCT during various stages of developing international norms on tobacco control? Specifically, why has the idea of banning duty-free sales of tobacco products emerged as one of the policy options when Parties to the FCTC negotiated the Protocol to eliminate illicit trade in tobacco products? Secondly, what policy rationales and possible options for regulating duty-free sales of tobacco products had

⁵ This position has been lobbied by the tobacco, travel or retailer industry arguing that the ban on duty free sales has a negligible impact on total tobacco consumption since such sales account for only one percent of total world-wide sales of tobacco. See Peter Freathy, "The WHO and tobacco control: implications for the travel-retail sector" (2004) 32:5 Intl J Retail & Distribution Management 252 at 256 (doi.org/10.1108/09590550410534596).

⁶ See Dermot Davitt, "Powerful industry alliance rejects proposed duty free tobacco ban" (12 March 2010), online: *The Moodie Davitt Report* <www.moodiedavittreport.com/powerful-industry-alliance-rejects-proposed-duty-free-tobacco-ban/> [perma.cc/76W3-K5M7]. See also Melody Ng, "Duty free tobacco ban talks stall during WHO meeting" (22 March 2010), online: *The Moodie Davitt Report* <www.moodiedavittreport.com/duty-free-tobacco-ban-talks-stall-during-who-meeting/> [perma.cc/R3M9-S3ZS].

been discussed or proposed during the process of negotiation or implemented in specific country practices? Put differently, this paper will explore various forms of policy options put forward by delegates to regulate duty-free sales of tobacco products. Finally, will implementing those policy options for regulating duty-free sales of tobacco products would run afoul of any existing international conventions? In other words, are there any existing international norms preventing Parties to the FCTC from implementing regulation of duty-free sales of tobacco products? If so, how could Parties to the FCTC choose or design the policy options to avoid the possible challenges based on international trade norms?

With the above questions in mind, this paper will firstly explore, in Part III, the problems and the historical route of negotiation dealing with the issue of duty-free sales, and examine different viewpoints and concerns over the policy of banning duty-free sales in tobacco products. Then, Part IV seeks to discuss the rationale for regulating duty-free sales of tobacco products, and identify the possible elements of policy options for domestic implementation and enforcement. Part V of this paper analyzes the consistency of banning duty-free sales policies with other existing international conventions, especially for the international rules under the World Trade Organization (WTO) and the World Customs Organization (WCO).⁷ Finally, Part VI concludes this paper.

III. INTERNATIONAL RULE-MAKINGS ON DUTY-FREE TOBACCO UNDER THE WHO/FCTC

A. Negotiation history and a brief overview of the problems of duty-free sales of tobacco products

The problems of duty-free sales of tobacco products mainly lie in the scale of tobacco consumption derived from the duty-free sources, and the impact on effective control of tobacco use. Ever since the first airport duty-free shop was opened at Shannon Airport in 1951, cigarettes and tobacco became one of the major products sold, in addition to liquor and alcohol.⁸

⁷ The WTO and WCO are selected because the multilateral rules concluded therein are related to or will have legal implications on the regulation of duty-free sales of tobacco products.

⁸ See Duty Free World Council, Economic impact of duty free and travel retail in Europe: A report for the Duty Free World Council, by Dr. Harry Bush & Daniel Storey, (March 2016)

According to data compiled by the Duty Free World Council, the global duty-free sale and travel retail reached the amount of 79 billion USD in 2018, of which 9.9% consists of tobacco goods.⁹ In terms of the amount, the global duty-free sales of tobacco products were around eight billion USD in 2018 and the number was rising.¹⁰ The problem also came from the increase of tobacco consumption from a duty-free source.¹¹ Research has indicated that the percentage of smokers consuming tobacco from a duty-free source ranges from below 1% in the US, Canada and Australia, and up to 3.8% and 5.6% in New Zealand and the UK, respectively.¹² It has been pointed out that such a tax anomaly of duty-free sales of tobacco products will reduce tax revenue, foster illicit trade, and undermine public health by encouraging cigarette consumption.¹³

The issue of regulating duty-free sales of tobacco products can be traced back to the WHO's decision to launch the negotiation of the FCTC. In May 1996, the 49th Session of the World Health Assembly (WHA) adopted Resolution WHA 49.17, entitled "International framework convention for tobacco control," requesting the Director-General of the WHO to initiate the development of a Framework Convention on Tobacco Control.¹⁴

Later in June 1997, for the purpose of making preparations for an International Framework Convention on Tobacco Control, representatives from six countries¹⁵ met in Halifax, Nova Scotia, Canada, and recommended

at 13.

⁹ See Duty Free World Council, *Global Travel Retail Change 2018 v 2017*, (Sweden: Generation Research, 2018).

¹⁰ See Chris Lane, "Eliminating Duty-free Tobacco—What Went Wrong?" (4 February 2021), online: Center for Global Development <www.cgdev.org/blog/eliminating-duty-free-tobacco-what-went-wrong> [perma.cc/HQ78-3WYE].

¹¹ See generally A Hyland et al, "Cigarette purchase patterns in four countries and the relationship with cessation: findings from the International Tobacco Control (ITC) Four Country Survey" (2006) 15:3 *Tobacco Control* iii59 (doi:10.1136/tc.2005.012203).

¹² Constantine I Vardavas, Andrew B Seidenberg & Gregory N Connolly, "Regulating duty free sales and tobacco advertising in airports: a call for action" (2011) 9:7 *Tobacco Induced Diseases*.

¹³ See Chris Lane, *supra* note 10 (estimating that the tobacco tax revenues could be reduced by about US \$7 billion per year because of the duty-free sale of tobacco products).

¹⁴ Forty-Ninth World Health Assembly, *International framework convention for tobacco control*, WHA49.17, UNWHAOR, 1996, s 3(1).

¹⁵ The six countries are Canada, Finland, France, Switzerland, Thailand and the United

a Consultative Group be formed to seek expertise on a number of tobacco issues among which the “duty-free sale” of tobacco products was specifically mentioned as one.¹⁶

In 1999, the Working Group on the WHO FCTC also identified “tax-free tobacco products” as one of the key areas for tobacco control when reviewing the possible scope and subject of an international framework convention on tobacco control. The Working Group in its first meeting had clearly stated that “to end all duty-free tobacco would be consistent with WHO health policy targets of reducing tobacco use, as tax-free sale makes cigarettes available cheaply.”¹⁷

In the subsequent phases of negotiation, prohibition of tax-free and duty-free sales of tobacco products continued to be an available option as one of the price and tax measures used to reduce the demand for tobacco. However, some representatives held the opposite position against such a proposal, expressing concerns over the appropriateness and legality of it.¹⁸ In the end, the acceptable solution for Parties appears to have been Article 6.2(b) of the FCTC; this provision is the only textual basis in the FCTC that encourages contracting Parties to adopt measures prohibiting or restricting duty-free sales and importation of tobacco products. Given that the text leaves too many qualifications to have an effective and enforceable implementation, the COP has made its efforts to materialize Article 6.2 of the FCTC through the development of guidelines and/or conclusion of a protocol. There are several ways to enforce this article.

Firstly, the COP, via the reporting mechanism, required Parties to provide information regarding the volumes of duty-free sales of tobacco

States.

¹⁶ See WHO Division of Mental Health and Prevention of Substance Abuse, *Programme on Substance Abuse International Framework Convention on Tobacco Control: Some Initial Preparations*, WHO/MSA/PSA/97.8, UNWHOOR, 1997 at 1.

¹⁷ See First Meeting of the Working Group on the WHO Framework Convention on Tobacco Control, *Subjects of possible protocols and their relation to the framework convention on tobacco control*, A/FCTC/WG1/3, UNWHOOR, 1999 at 1.

¹⁸ For example, representatives of the Dominican Republic held the position that tax- and duty-free sales should not be prohibited. Representatives of Japan expressed concerns over the consistency with other existing international conventions regarding customs and taxation. See World Health Organization, *Summary Records of the Third Session of the Intergovernmental Negotiating Body on the WHO Framework Convention on Tobacco Control*, A/FCTC/INB3/SR, UNWHOOR, 2001 at 110-111.

products and the regulatory measures – if any – adopted either to prohibit or restrict sales to, and/or importation by, international travelers of tax-and duty-free tobacco products. This was done in order to estimate the magnitude of illicit supply of tobacco products.¹⁹

Secondly, the COP, by adopting the Guidelines for implementation of Article 11 of the WHO Framework Convention on Tobacco Control (Article 11 Guidelines), recommended in paragraph 49, that Parties should ensure the equal application of packaging and labelling requirements to all tobacco products within the jurisdiction, including those domestically manufactured, or imported or intended for duty-free sales.²⁰

Despite Article 6.2 of the FCTC entering into force in 2005, it was not until 2010 that the fourth session of the COP decided to establish a working group to develop draft guidelines for implementation of Article 6 of the FCTC (Article 6 Guidelines) in which Section 6 recommended Parties should consider prohibiting or restricting the tax- or duty-free sales of tobacco products.²¹

While these provisions address the issue of duty-free tobacco products, they are not legally binding obligations imposed on contracting Parties. Nonetheless, this paper considers that such soft norms reflect the common understanding of the contracting Parties and can be introduced by the parties if they so wish.

Long before the working group was established to develop Article 6 Guidelines, the COP, at its second session in 2007,²² decided to establish an open-ended Intergovernmental Negotiating Body (INB) to develop a draft protocol on illicit trade in tobacco products.²³ In the first session INB held

¹⁹ See Conference of the Parties to the WHO Framework Convention on Tobacco Control, *Decisions and Ancillary Documents*, COP/1/2006/CD, UNWWHOOR, 1st sess, (2006) at 48-49.

²⁰ See World Health Organization, *Guidelines for implementation of Article 11 of the WHO Framework Convention on Tobacco Control (Packaging and labelling of tobacco products)*, FCTC/COP3(10), UNWWHOOR, 3rd sess, (2008) at 8.

²¹ See Conference of the Parties to the WHO Framework Convention on Tobacco Control, *Draft guidelines for the implementation of Article 6 of the WHO Framework Convention on Tobacco Control: Report of the working group*, FCTC/COP/5/8, UNWWHOOR, 5th sess, (2012) at 18.

²² See Conference of the Parties to the WHO Framework Convention on Tobacco Control, *Decisions and Ancillary Documents*, FCTC/COP2(12), UNWWHOOR, 2nd sess, (2007) at 28.

²³ Illicit trade or smuggling of tobacco products were considered as possible topics for future

in 2008, representatives of the Parties vigorously supported reconsidering the issue of duty-free sales and including it in the relevant provision of the Protocol,²⁴ although the issue had never been addressed in the original template²⁵ for the protocol on illicit trade drafted by the Expert Group.²⁶ The issue of duty-free sales was hotly debated and negotiated in the following five sessions of the INB,²⁷ and accordingly the text was revised and amended

protocols during the fifth and sixth sessions of the Negotiating Body. See Second Meeting of the Working Group on the WHO Framework Convention on Tobacco Control, Possible subjects of initial protocols: Elaboration of technical components of three possible protocols, A/FCTC/WG2/4, UNWHAOR, 2000 at 8-11. See also Conference of the Parties to the WHO Framework Convention on Tobacco Control, Additional matters identified in the Convention for consideration by the Conference of the Parties: Elaboration of guidelines for implementation of Article 7 and Article 9 and Elaboration of protocols - Note by the Secretariat, A/FCTC/COP/1/INF.DOC./3, UNWHAOR, 1st sess, (2006) at 4.

²⁴ In INB 1, when discussing the Internet sales of cigarettes, representative of Philippines suggested that “if the protocol made reference to Internet sales, it should also include a provision relating to duty-free sales.” Such proposal was later endorsed by representatives from Nigeria, Palau, and Saudi Arabia. Representative of Saudi Arabia even suggested that “a new subparagraph should be added ... stating that tobacco products should not be sold in tax-free or duty-free zones or on aircraft, since they might be smuggled or resold illicitly.” See Conference of the Parties Intergovernmental Negotiating Body on a Protocol on Illicit Trade in Tobacco Products, Summary Records, FCTC/INB-IT/1/REC/1, UNWHAOR, 1st sess, (2008) at 25, 46.

²⁵ The most relevant parts in the Template are paragraphs 27 and 28 which address the issue of Internet sales. The Expert Group recommended prescribing Internet sales in the future protocol because tobacco products were often sold via the Internet to avoid tax or other regulations. These are also the provisions that the representatives of the INB proposed to reconsider the issue of duty-free sales to be included in the Protocol (this sentence is unclear please rephrase). See Conference of the Parties Intergovernmental Negotiating Body on a Protocol on Illicit Trade in Tobacco Products, Drafting and negotiation of a protocol on illicit trade in tobacco products: Template for a protocol on illicit trade in tobacco products, as proposed by the expert group convened in accordance with decision FCTC/COP1(16) of the Conference of the Parties, FCTC/COP/INB-IT/1/4, UNWHAOR, 1st sess, (2007) at 11.

²⁶ The First Session of the COP held in February 2006 requested the Convention Secretariat under the direction of the Bureau to form a group of experts and prepare a template for the protocol on illicit trade in tobacco products. The Group developed the template and submitted it to the Second Session of the COP held in July 2007 in Bangkok. The decision of the COP1, See COP 2006, *supra* note 19 at 57.

²⁷ The negotiation history of the Protocol, see “Annex 2: History of the Negotiations of the Protocol to Eliminate Illicit Trade in Tobacco Products”, WHO Protocol, *supra* note 4 at

several times through different versions of the draft Protocol.²⁸ The final result appeared in Article 13 of the draft Protocol along with the draft Article 6 Guidelines, both of which were finally adopted by the COP in November 2012 and October 2014 respectively.

B. Debates over the legality and necessity of rules on duty-free tobacco products

While the Protocol underwent five rounds of negotiations, the provision regulating duty-free sales of tobacco products was not included in the draft Protocol until the Revised Chairperson's text for the Protocol²⁹ was prepared at the end of the second session of the INB.³⁰ Although the proposal of prohibiting or restricting duty-free sales of tobacco products gained a lot of support throughout the whole process of negotiation,³¹ it is worth noting

53-55.

²⁸ Article 13 of the Protocol, titled "Duty free sales," provides that "1. Each Party shall implement effective measures to subject any duty-free sales to all relevant provisions of this Protocol, taking into consideration Article 6 of the WHO Framework Convention on Tobacco Control. 2. No later than five years following the entry into force of this Protocol, the Meeting of the Parties shall ensure at its next session that evidence-based research is conducted to ascertain the extent of illicit trade in tobacco products related to duty free sales of such products. On the basis of such research, the Meeting of the Parties shall consider appropriate further action." WHO Protocol, *supra* note 3 at 21.

²⁹ Article 11 of the Revised Chairperson's text, titled "free-trade areas and duty-free sales," provides that "[e]ach Party shall, within three years of the entry into force of this Protocol for that Party, implement effective measures to prohibit any tax, regulatory or other advantages that apply in free-trade areas from applying to tobacco, tobacco products or manufacturing equipment used in the manufacture of tobacco products, including tax-reduced and duty-free sales to individual customers." See Conference of the Parties Intergovernmental Negotiating Body on a Protocol on Illicit Trade in Tobacco Products, *Revised Chairperson's text for a protocol on illicit trade in tobacco products*, FCTC/COP/INB-IT/3/3, UNWHOOR, 3rd sess, (2009) at 16.

³⁰ In the Chairperson's text for the Protocol, Parties are required to share information regarding "import, export, transit, tax-paid and duty-free sales" of tobacco products, but are not specifically encouraged to prohibit or restrict duty-free sales of tobacco products. See Conference of the Parties Intergovernmental Negotiating Body on a Protocol on Illicit Trade in Tobacco Products, *Chairperson's text for a protocol on illicit trade in tobacco products*, FCTC/COP/INB-IT/2/3, UNWHOOR, 2nd sess, (2008) at 18.

³¹ For example, the representatives of Philippines were firm supporters of a ban on duty-free sales of tobacco products, proposing, in INB 2, new wording with the title "Duty-free, Internet and other analogous modes of sale," to read: "in order to prevent diversion and potential sources of illicit trade, each Party shall implement effective measures to prohibit

that not every representative supported the proposal to include a provision banning duty-free sales of tobacco products in the Protocol. Some commentators cast doubts about the necessity of including such provision in the Protocol dealing with illicit trade in tobacco products³² and were worried about the feasibility of implementing such provision in domestic law.³³ Others argued that Parties should be given the discretion and flexibility in shaping their tax policy, including how to deal with duty-free sales of tobacco products, rather than a rigid mandate.³⁴

Based on the discussion during the negotiation process, this paper finds that there are two major concerns, normative and positive, expressed by participants over the proposal of banning duty-free sales of tobacco products. With respect to the first concern, the representatives of the INB have demanded legal advice concerning the issue of consistency of banning duty-free sales of tobacco products with other existing international conventions. With respect to the second concern, a compromise was reached which requires evidence-based research to be conducted on the extent of the linkage between duty-free sales and illicit trade of tobacco products before further actions or policy-making decisions are taken.

duty-free, Internet and sales in free zones of tobacco and other tobacco products.” This proposal of a ban on sales of tobacco products through duty-free outlets was also supported by the representative of Myanmar and Swaziland. The International Union against Cancer also spoke in favour of a ban on Internet and duty-free sales of tobacco products. See Conference of the Parties Intergovernmental Negotiating Body on a Protocol on Illicit trade in Tobacco Products, *Summary Records*, FCTC/COP/INB-IT/2/REC/1, UNWHAOR, 2nd sess, (2008) at 9-10.

³² For example, in INB 2, the representative of Norway held the position that her delegation could not support the inclusion of a provision to ban duty-free sales of tobacco products in the paragraph under discussion. Moreover, the representative of India, who spoke on behalf of the Parties in the WHO South-East Asia Region, had doubts about whether the reference to the sale of duty-free tobacco products should be included in that provision. See *ibid* at 10, 41-42.

³³ The Representative of Japan, in INB 2, said that Japan “needed time to look into the feasibility of implementing them in its jurisdiction. It therefore reserved its position on the section.” See *ibid* at 42.

³⁴ For example, the Representative of Barbados said that, “to give countries like her own some flexibility for determining their taxation policies, the words ‘should’ or ‘shall endeavour’ should be inserted in the proposal on prohibition of duty-free sales of tobacco products.” See *ibid* at 42.

On the first issue, the INB (at its second session) requested the Chairperson and the Convention Secretariat to seek expert reviews on a number of elements of the Protocol, including the legal ramifications of a possible ban on duty-free sales of tobacco products with a particular focus on international trade law.³⁵ In regard to the second issue, the INB decided to postpone it by including a new second paragraph in Article 13 of the Protocol. Paragraph 2 of Article 13 now mandates Meeting of the Parties to conduct evidence-based research on the extent of illicit trade in tobacco products related to duty-free sales of such products no later than five years from the entry into force of this Protocol.³⁶ Based on this provision, the Meeting of the Parties adopted the Timelines for evidence-based research at its first session in August 2018.³⁷

While these two aspects of concerns are both essential elements that will ultimately affect the Parties' policy choices toward duty-free sales of tobacco products, this paper focuses instead on the normative issue regarding the legality of such regulation – specifically in terms of the compatibility of duty-free rules with international trade laws – and addresses the scientific evidence only to the extent necessary to demonstrate the rationale for such regulations.

³⁵ See Conference of the Parties Intergovernmental Negotiating Body on a Protocol on Illicit trade in Tobacco Products, Revised Chairperson's text for a protocol on illicit trade in tobacco products and general debate: Expert review on a possible ban on duty-free sales of tobacco products, FCTC/COP/INB-IT/3/INF.DOC./3, UNWHOOR, 3rd sess, (2009).

³⁶ See Article 13.2 of the Conference of the Parties to the WHO Framework Convention on Tobacco Control, Draft protocol to eliminate illicit trade in tobacco products, FCTC/COP/5/6, UNWHOOR, 5th sess, (2012) at 16. Originally, the idea was proposed by the Informal Working Group (IWG), mandated by the COP 4 to narrow the issue and submit the draft of the Protocol to the INB 5. The IWG stated that in order to reach consensus on the text of the articles, they agreed to include new provisions – namely a new paragraph 2 of Article 11b is, and a new paragraph 5 of Article 5 – which require the Meeting of the Parties (MOP) to consider appropriate action in respect of duty free sales and key inputs, respectively, after having performed evidence-based research five years after the entry into force of the protocol. See Conference of the Parties Intergovernmental Negotiating Body on a Protocol on Illicit trade in Tobacco Products, Informal working group on the draft protocol to eliminate illicit trade in tobacco products: Outcome of the two meetings of the working group, FCTC/COP/INB-IT/5/3, UNWHOOR, 5th sess, (2011).

³⁷ See Meeting of the Parties to the Protocol to Eliminate Illicit Trade in Tobacco Products, Timelines for evidence-based research (Articles 6.5 and 13.2), FCTC/MOP/1/11, UNWHOOR, 5th sess, (2018).

C. Current rules of duty-free sales of tobacco products and their problems

So far in the FCTC and its guidelines and protocols, there are four legal provisions that clearly address the issue of duty-free sales of tobacco products: Article 6.2 of the FCTC, paragraph 49 of Article 11 Guidelines, Article 13 of the Protocol, and Section 6 of Article 6 Guidelines. This paper briefly analyzes these rules and their related problems in order to create a better understanding of the current state of duty-free sale regulations under the FCTC and their related legal instruments.

1. Article 6.2 of the FCTC

Article 6.2 is the only provision which prescribes duty-free sales of tobacco products in the original text of the FCTC. Article 6.2 provides, in relevant parts, that:

[w]ithout prejudice to the sovereign right of the Parties to determine and establish their taxation policies, each Party should take account of its national health objectives concerning tobacco control and adopt or maintain, as appropriate, measures which may include: ... (b) prohibiting or restricting, as appropriate, sales to and/or importations by international travellers of tax- and duty-free tobacco products.³⁸

It is noteworthy that pursuant to this provision, the FCTC formally recognizes that tax- and duty-free tobacco products should be prescribed to make tobacco control more effective and comprehensive. However, this provision has too many qualifications to have an effective or enforceable implementation by the Parties. The term “should” and “take account” used in the text indicate a weaker mandate imposed on the Parties. In addition, the word “may” and the recognition of “sovereign right on taxation policy” denotes that Parties have the discretion to decide if or how duty-free sales of tobacco products should be prohibited or restricted within their jurisdiction. All of these terms weaken the legal strength of this provision. If a more effective implementation is desired, a collective action from the Parties is necessary to adopt a clear guideline, providing specific ways of implementing this provision. To achieve this end, the COP established a working group to develop draft guidelines and finally adopted it at its sixth session in October 2014.

³⁸ FCTC, *supra* note 2 at 8.

2. Paragraph 49 of the Guidelines implementing Article 11 of the FCTC

The COP, at its third session, in dealing with the issue of packaging and labeling of tobacco products, adopted the Guidelines for implementation of Article 11 (Packaging and labelling of tobacco products) of the FCTC. The term “duty-free sales” is mentioned paragraph 49 of the Guidelines, which provides that “Parties should ensure that the packaging and labelling provisions related to Article 11 of the Convention apply equally to all tobacco products sold within the jurisdiction and that no distinction is made between products that are manufactured domestically or imported or intended for duty-free sale within a Party’s jurisdiction.”³⁹

Despite the term “duty-free sales” being used in Article 11 of the Guidelines, paragraph 49 does not directly prescribe the banning of duty-free sales in tobacco products. Rather, it simply recommends that Parties should ensure the packaging and labelling provisions apply equally to all tobacco products without making any distinction between products that are manufactured domestically or imported or intended for “duty-free sale.”

This paragraph has a limited scope of application to address only one type of the tobacco-control measures associated with duty-free sales – namely the packaging and labelling requirements. Nonetheless, it at least indicates that the COP holds the regulatory principle that tobacco products intended for duty-free sales should be treated equally to those of other regular ones. In other words, the duty-free tobacco products will not enjoy more lenient standards of regulatory treatment than duty-paid tobacco products. This provision could serve as a useful guidance for interpretation as a general principle of law despite its limited scope of application.

3. Article 13 of the Protocol to eliminate illicit trade in tobacco products

The issue of duty-free tobacco reappeared during the negotiation of the Illicit Trade Protocol. Despite the intense debate over the necessity of such provision, the current text of Article 13 embodies the acceptable compromise, which provides in the first paragraph that

[e]ach Party shall implement effective measures to subject any duty free sales to all relevant provisions of this Protocol, taking into consideration Article 6 of the WHO Framework Convention on Tobacco Control.⁴⁰

³⁹ See WHO Guidelines for implementation of Article 11 of the WHO FCTC (Packaging and labelling of tobacco products), *supra* note 20 at para 49.

⁴⁰ WHO Protocol, *supra* note 3 at 21.

The Parties then added the second paragraph, which mandates that the Meeting of the Parties shall ensure the evidence-based research be conducted “to ascertain the extent of illicit trade in tobacco products related to duty free sales of such products”, and “on the basis of such research ... [shall consider] ... appropriate further action.”⁴¹

The result mainly reflects two major concerns that arose during the negotiation. The first paragraph deals with the legal aspect concerning the acceptable approach towards regulations of duty-free sales of tobacco products. As for the second paragraph, it addresses the scientific inquiry about the connection between duty-free sales and illicit trade in tobacco products.

With respect to the regulatory approach, negotiators seem to have adopted a regulatory strategy in Article 13 of the Protocol similar to that of the Article 11 Guidelines – a more lenient approach that could embody a common ground among delegates. Instead of indicating a preference for a complete ban on duty-free sales, Article 13.1 of the Protocol subjects any duty-free sales to all relevant provisions of the Protocol, thereby avoiding controversy over which regulatory direction should be pursued.

According to Article 13.1 of the Protocol, relevant provisions under this Protocol such as requirement of license, track and tracing and due diligence that applies to tax-paid tobacco products should also apply to duty-free tobacco products. Such approach is similar to the principle indicated in Article 11 of the Guidelines, which provides that tobacco control rules should equally apply to all kinds of tobacco products, no matter whether they are intended for duty-free sales or purchased from duty-free stores.

Despite being the most acceptable compromise among delegates, this paper finds several potential problems with the interpretation and implementation of this provision. Firstly, the phrase “all relevant provisions” is too vague to have an effective and meaningful implementation. It seems unclear which provisions in the Protocol are considered to be relevant, and who is able or has the authority to decide. Thus, clarification is needed with regard to the scope of specific provisions being considered as “relevant” to the regulation of duty-free sales of tobacco products. Without such clarification, it may provide a potential loophole for manipulating qualifications for the relevancy of applicable provisions that in turn can weaken the effectiveness of this provision.

⁴¹ See *ibid* at 21.

With respect to the scientific research, Article 13.2 of the Protocol provides a timeline of five years for conducting evidence-based research beginning from the date of entry into force of this Protocol.⁴² This paper suggests that the Meeting of the Parties should respond and act swiftly to avoid the expansion of damage caused by duty-free sales as soon as sufficient evidence can be shown to prove the linkage between duty-free sales and the increase of illicit trade in tobacco products. Moreover, this provision fails to indicate the possible elements or scope of such research, let alone the ways and means of conducting the research. While the goal is to ascertain the extent or magnitude of illicit trade caused by duty-free sales, it may be worth exploring this issue from a regulatory perspective. In other words, the research may need to examine the nature of different duty-free mechanisms as one of the parameters to evaluate the extent of such a problem.

4. Section 6 of the Guidelines implementing Article 6 of the FCTC

Unlike previous rules, the Guidelines implementing Article 6 of the FCTC is the legal instrument clearly prescribing the duty-free sales of tobacco products. Section 6 of this Guideline provides that:

[p]arties should consider prohibiting or restricting the tax- or duty-free sales of tobacco products. They should monitor the extent to which tax- or duty-free products contribute to illicit trade and take the necessary measures if such a link is ascertained.⁴³

Pursuant to this provision, a position was unequivocally held by the COP towards the prohibition or restriction of the duty-free sales of tobacco product.

Unlike a more conservative approach taken under the Protocol, this Guideline clearly recommends the preferred policy choices of either prohibiting or restricting the tax- or duty-free sales of tobacco products. In addition to the textual difference, the significant discrepancy lies at the regulatory policy proclaimed towards different directions. Section 6 states that duty-free sales of tobacco products should be prohibited or restricted, while Article 13 of the Protocol simply requires them to be subjected to the provisions regulating regular tobacco products without denouncing the duty-free sales of tobacco products altogether.

⁴² See *ibid* at 21.

⁴³ WHO Article 6 Guidelines, *supra* note 1 at 13-14.

The reason for the different approaches taken between the Guidelines and the Protocol lies in the different legal ramifications that are to be derived from these two instruments. The Guidelines provide non-binding recommendations relying on voluntary implementation by each Party, while the Protocol prescribes legally binding obligations on the Parties who ratify the Protocol. Therefore, it was reasonable that the Parties took different textual approaches to regulate duty-free sales of tobacco products, considering the different legal ramifications under the two legal instruments. Parties were more willing to accept stronger wording in non-binding instruments than in binding ones.

Nonetheless, this paper finds that such different approaches may create a false impression that Parties to the FCTC held blurred, if not contradictory, positions on the duty-free sales of tobacco products, an issue derived from the potential conflicting message prescribed under the Guidelines and the Protocol. Given that Section 6 of the Guidelines aims to implement Article 6.2(b) of the FCTC, it can be problematic if the FCTC holds different regulatory approaches on the issue of duty-free sales of tobacco products under the Protocol. Inconsistent policy approaches taken across various legal instruments may weaken the FCTC's efforts of tobacco control, and cause uncertainty for implementation and enforcement. It may be worth reviewing if the regulatory differences evident in the Guidelines and the Protocol may cause any obstacles for effective implementation of tobacco control measures, or draw any concern over the potential lack of harmony in policy choices under the FCTC.

IV. REGULATORY RATIONALE AND POLICY OPTIONS FOR RULES ON DUTY-FREE SALES OF TOBACCO PRODUCTS

A. Regulatory rationales of duty-free sales of tobacco products

Before identifying the possible policy options for regulations of duty-free sales of tobacco products, it is necessary to explore the rationales and the competing interests involved in such regulations. This paper finds that there are three policy interests that are the most relevant and have inter-related considerations that lay out the foundations for duty-free sales regulation. These interests are public health, fiscal or taxation, and international trade.

1. Public health interests

The pursuit of public health interests and concerns over the potential health impact remains the major regulatory rationale for prohibiting or restricting duty-free tobacco products. Raising tobacco taxes to elevate the market price for tobacco products has been considered one of the effective measures to reduce tobacco consumption, especially for youth or the poor. However, if the sale of duty-free tobacco products is permitted by law, it can have a potential impact on the price of tobacco products, as the price of duty-free products will be lower than those on which duty has been paid or tax imposed. This amounts to an encouragement for tobacco consumption if duty-free tobacco products are widely and easily available for existing or potential smokers.⁴⁴

Since allowing the sales of duty-free tobacco products makes cheaper tobacco products more readily available for consumption, this not only defeats the taxation policy originally designed to control tobacco demand, but also harms public health by encouraging personal consumption of tobacco products.⁴⁵ In other words, allowing duty-free tobacco sales weakens the effectiveness of tax and price measures designed to reduce the demand of tobacco consumption. Purchasing duty-free cigarettes frustrates the public health purpose because the increase of tobacco consumption is well expected due the availability of cheaper and more affordable cigarettes than those that are taxed or duty-paid.

2. Fiscal or taxation considerations

In addition to public-health concerns, the regulation of duty-free tobacco products must take into account fiscal considerations, including the legitimacy of taxation policy. Apparently, imposing or increasing tobacco taxes can have fiscal effects of increasing governmental revenues, which is one of the reasons why the government maintains higher tobacco taxes than

⁴⁴ Given that the duty-free tobacco products are sold mainly at the airport for travelers, it has been argued that allowing duty-free sales of tobacco products provides a large regressive subsidy to consumption of a product that is known to be harmful to consumers. Moreover, the subsidy largely benefits high-income individuals who travel far more than low-income individuals. See Chris Lane, *supra* note 10.

⁴⁵ See World Health Organization, "WHO Technical Manual on Tobacco Tax Administration" (2010) at 78, online (pdf): <apps.who.int/iris/bitstream/handle/10665/44316/9789241563994_eng.pdf;jsessionid=7BAC68C7996531FA180367AFD27A3552?sequence=1> [perma.cc/95SM-ANEN].

taxes on other products. Given the fact that the demand for tobacco products is inelastic and the share of tax in cigarette prices is low in many countries, significant increases in governmental revenues can be generated through increasing tobacco taxes.⁴⁶ Therefore, allowing duty-free sales of tobacco products directly contradicts the benefits of governmental revenues since no taxes or duties are collected from those products.

On the other hand, purchasing duty-free products is a legal method used by consumers to avoid taxation. The original rationale for duty-free sales lies in the fact that those products are intended for personal consumption abroad or purchased in transit for personal use. Since tobacco products are not consumed within the border of a state and normally considered as goods carried by the travelers for personal use, the state authority arguably lacks a legitimate basis to impose taxes on those products, and will normally exempt them from customs duties, excises tax and value added tax (VAT). Occasionally, some states will also exempt taxes or surcharges especially earmarked for the expense of tobacco control.⁴⁷

Nonetheless, if tobacco taxes or duties are waived, making duty-free tobacco products more easily available could have the fiscal implications, in that less governmental revenue could be raised and used for the implementation or enforcement of tobacco control policies, especially when the earmarked taxes or health-related surcharges are also waived.

3. Implications on international trade

Regulating duty-free tobacco products also needs to address the concern over licit and illicit trade in tobacco products. Despite higher tobacco taxes being effective on tobacco control, the high margin of price differences between tax-paid and tax-free tobacco products provides lucrative incentives for smugglers engaging in illicit trade of tobacco products. Moreover, research has shown that there is some evidence that the availability of duty-free sales of tobacco products facilitates the illicit trade in tobacco products in many countries.⁴⁸ It has been suggested that “[c]igarettes marked for duty-

⁴⁶ See *ibid* at 18.

⁴⁷ See Conference of the Parties to the WHO Framework Convention on Tobacco Control WHO, *supra* note 36 at 3.

⁴⁸ See WHO, *supra* note 30 at 81. See also J Collin et al, “Complicity in contraband: British American Tobacco and cigarette smuggling in Asia” (2004) 13 (Suppl II) Tobacco Control ii104.

free sales may end up as contraband, often diverted into illegal distribution channels prior to even reaching duty-free stores.”⁴⁹ Thus, duty-free sales of tobacco products provide a loophole for possible illicit supplies of tobacco products to consumers.

On the other hand, the duty-free system has legitimate purposes to facilitate international trade or accommodate the personal need for international travelers. Banning duty-free sales may adversely affect legitimate trade at the border in duty-free shops. Moreover, duty-free retailers and industry associations have emphasized that their supply chain of duty-free sales is “one of the most secure in the world with processes and technologies in place to provide for verification of registration, compliance, certification, review, and audit;”⁵⁰ thereby refuting the argument that the tobacco products sold at the duty-free shops originate from illicit trade in tobacco products. As such, competing trade implications may need to be taken into account when examining the consistency of the regulations of duty-free sales of tobacco products with relevant international trade rules.

B. Policy options for regulating duty-free sales of tobacco products

Based on the rationales for regulating duty-free sales of tobacco products, this paper identifies a possible regulatory scope and available policy tools for such regulations before analyzing the issue of legality.

1. Scope and object of regulations

As Article 6.2 of the FCTC indicates, the scope of duty-free regulations covers the “sale” to and the “importation” by international travelers of duty-free tobacco products.⁵¹ Article 6.2 seems to treat these two activities similarly situated so as to apply the same regulatory approach to prohibit or restrict the sales and/or importations of tobacco products on a duty-free basis. However, this paper argues that these two activities should be

⁴⁹ See WHO, *supra* note 30 at 81.

⁵⁰ See Duty Free World Council, “DFWC Industry Position Paper: Duty free industry supports the WHO Protocol to Eliminate Illicit Trade in Tobacco Products – duty free retailers are not part of the problem” (14 March 2018) at 1, online (pdf): <dfworldcouncil.com/wp-content/uploads/2018/08/DFWC-ITP-Position-Paper.pdf> [perma.cc/524Y-PV4U].

⁵¹ FCTC, *supra* note 2 at 8.

examined separately in light of the different functions or purposes they are designed to achieve.

Specifically, duty-free trade is a general term which includes three types of transactions that occur at the border of a customs territory, i.e., purchasing duty-free products for the purpose of “exportation,” “in transit use” or “importation.” The concept of “duty-free sales” refers to the former two types of trade while “duty-free importation” refers to the latter. The original rationale for allowing duty-free transactions lies in the fact that the purchased products are intended for consumption abroad or personal use “in transit,” which is considered as “exportation” of such products by the international travellers.

This “exportation” rationale should not apply to the “importation” of duty-free products by international travellers. Instead, the reason for allowing importation of duty-free products falls under the main consideration of personal use by international travellers. Therefore, a certain amount of allowance is normally permitted for personal carriage of such products. Nonetheless, regulating “sales” of duty-free products seems easier and more feasible than regulating “importation” of such products because of the difficulty in monitoring activities of importation by international travellers.⁵²

2. Prohibition on duty-free sales of tobacco products

The first policy option proposed by the WHO is to impose a total ban on duty-free sales of tobacco products as indicated in Article 6.2 of the FCTC, and Section 6 of the Article 6 Guideline.⁵³ However, the phrase “prohibiting” is left undefined, causing the potential ambiguity about whether tobacco products may not be sold legally in duty-free stores or in the transportation vehicles because of such outright ban.

But such a strict definition does not seem to be the common understanding among the representatives of the negotiating Parties. Instead, the real understanding is to prohibit sales of tobacco products on a duty-free basis while still allowing tobacco products that are being traded at the border or in transit at the duty-free stores. In other words, the sale of legal tobacco products at duty-free stores is permitted so long as the tax or duty charged on them is equivalent to regular duty-paid tobacco products. However, the

⁵² See WHO, *supra* note 30 at 3.

⁵³ FCTC, *supra* note 2 at 8. WHO Article 6 Guidelines, *supra* note 1 at 13-14.

privilege for sales on a duty-free basis has to be eliminated based on the proposed prohibition approach.

3. Restrictions in variant forms on duty-free sales of tobacco products

Instead of a total elimination of duty-free privilege, imposing a series of restrictive measures can be an alternative policy choice to regulate duty-free sales of tobacco products. This approach is more lenient than a total ban on the duty-free sales of tobacco products. Unlike the first option, this approach could be more practically feasible and politically acceptable for countries whose delegates express concerns over the impact of duty-free regulations on international trade, as it provides more flexibility for domestic implementation. The compromise text in Article 13.1 of the Illicit Trade Protocol is a perfect example of such a preferred approach, which requires subjecting duty-free sales of tobacco products to the relevant provisions in this Protocol instead of banning these sales completely.⁵⁴ Therefore, the compromise approach leaves the Parties a certain level of regulatory latitude in shaping the duty-free policy for tobacco products.

Specifically, there may be various forms of restrictions that a Party can implement to effectively regulate duty-free sales of tobacco products. These include: (i) imposing age limits on buying duty-free cigarettes; (ii) prescribing an allowance for personal imports of duty-free cigarettes; (iii) and applying excise taxes on tobacco products sold in tax- or duty-free stores, among others. Such restrictive measures can take the form of qualitative or quantitative restrictions, or a combination of both.

i. Qualitative approach

Qualitative restrictions refer to various forms of “non-price regulations” on the control over duty-free sales of tobacco products, which includes things such as packaging, labeling and age limitations for cigarette buyers, and the like. For example, Article 11 Guidelines recommends that the same packaging and labeling requirements of regular tobacco products should also apply to duty-free ones.⁵⁵ Moreover, the ban on sales to minors also applies to minors purchasing duty-free tobacco products in many countries. The issue of non-price restrictions on duty-free sales of tobacco products is less controversial because it basically shares the same regulatory standards with

⁵⁴ WHO Protocol, *supra* note 3 at 21.

⁵⁵ WHO Article 11 Guidelines, *supra* note 20 at 8.

regular duty-paid tobacco products.⁵⁶ These non-price measures are scientifically proven to be effective tobacco control policies that have been adopted by the FCTC.⁵⁷ Nonetheless, it is still arguable to what extent this regulatory approach could extend to dealing with the issue of illicit trade in duty-free tobacco products due to the unclear scope of the “relevant provisions” provided in Article 13.1 of the Protocol.

ii. Quantitative approach

Quantitative restrictions refer to the tobacco control measures associated with price or quantity. They can be in the form of either (i) restricting the allowance for travellers’ import of duty-free tobacco products or (ii) imposing excise taxes on tobacco products sold at duty-free stores. Limiting the travellers’ allowance for importing duty-free tobacco products is considered a price-related measure because it will, more or less, affect the price of tobacco products in regular markets based on the economic principle of supply and demand. Limiting the amount of allowance aims at ensuring that the purpose of personal use is properly served, and becomes a common regulatory approach adopted without much controversy in many countries.

Nonetheless, there is a vigorous debate over the way in which to apply excise or other forms of taxes on duty-free tobacco products at the duty-free stores. While banning duty-free tobacco products eliminates all forms of duty-free privileges originally offered, this policy option only eliminates some but not all types of duty-free privileges. Despite being less effective and comprehensive, imposing some taxes or duties can be a stepping-stone towards a total abolition of all duty-free privileges of selling tobacco products at duty-free stores. Unlike “duty-free” sales, this has been called “duty-reduced” sales of tobacco products.

Normally, duty-free tobacco products are sold without charging any taxes or duties, such as customs duties, excises, VAT and other surcharges. As for “duty-reduced” tobacco products, the taxes charged are less than full duty-paid tobacco products, but more than duty-free tobacco products. Parties

⁵⁶ Despite this, a commentator argued that duty-free sale of tobacco undermine public-health goals because duty-free sales are less regulated than duty-paid sales in terms of product packaging and product promotion. See Chris Lane, *supra* note 10. Moreover, one observer remarks that “airports may represent one of the last remaining havens for the tobacco industry.” See Constantine I Vardavas et al, *supra* note 12 at 1.

⁵⁷ FCTC, *supra* note 2 at 8 (Article 7 of the FCTC prescribes non-price measures to reduce the demand for tobacco).

may also choose the types of tax to apply to duty-reduced tobacco products. Some apply excise taxes to tobacco products while others apply welfare surcharges to tobacco products sold at duty-free shops. In any event, the taxes imposed on tobacco products sold at duty-free stores are moderately increased as compared to duty-free tobacco products in order to reduce the incentive of purchasing duty-free tobacco products. This is due to narrowing the margin of price differences between duty-paid and duty-free tobacco products.

V. LEGAL ASSESSMENT OF DUTY-FREE TOBACCO REGULATIONS UNDER INTERNATIONAL TRADE-RELATED LAWS

The proposal of banning duty-free sales of tobacco products has been highly discussed and supported in the course of negotiations of the Illicit Trade Protocol. However, representatives expressed serious concerns over the legality of adopting such measures, and requested expert opinions on the consistency of banning duty-free sales proposed in the Protocol with other existing international instruments in order to clarify the relationship between them.⁵⁸ To address these concerns, the Convention Secretariat sought expert opinions on the legal ramifications of a possible ban on duty-free sales of tobacco products, and concluded that “restricting or eliminating duty-free sales of tobacco products to departing travellers is unlikely to breach any international obligation.”⁵⁹

Despite a positive conclusion being reached, this paper finds that some of the key issues are not well-articulated in the expert’s report and are worth pondering before reaching a conclusion. This paper will discuss this legal issue by addressing the following questions in turn: (1) Are there any international instruments positively requiring Parties to provide duty-free sales/importation of tobacco products? If so, what do these obligations really require? If no, (2) will Parties be liable for violations of any international instruments particularly those regarding international trade if they decide to regulate, prohibit or restrict, duty-free sales of tobacco products? If yes, what

⁵⁸ See Conference of the Parties to the WHO Framework Convention on Tobacco Control, Report of the Intergovernmental Negotiating Body to the Third session of the Conference of the Parties on the progress of its work, FCTC/COP/3/4, UNWHOOR, 3rd sess, (2008) at 4-5.

⁵⁹ See Conference of the Parties to the WHO Framework Convention on Tobacco Control, *supra* note 36 at 8-9.

kinds of regulations can prevent Parties from violating international instruments? Finally, if it is difficult to circumvent, (3) are there any available exemptions provided in international instruments for Parties to justify such violations so that they can still regulate duty-free tobacco products for the benefit of public health?

A. International obligations to allow duty-free sales of tobacco products

In principle, each Party has the sovereign right to establish its taxation policy within its jurisdiction unless it agrees to hand over its sovereign rights by committing to international obligations. Therefore, each Party should be able to decide whether to prohibit or restrict duty-free sales of tobacco products at its discretion so long as no international instrument to which the Party is a member state requires otherwise.

However, as mentioned in the expert's report⁶⁰, the Convention Concerning Customs Facilities for Touring⁶¹ (Convention for Touring) and the International Convention on the Simplification and Harmonization of Customs Procedures⁶² (Kyoto Convention) are the most relevant international instruments that may require their Contracting States to allow duty-free sales of tobacco products.

This paper examines these two international conventions to see if there is any provision requiring its Contracting States to provide duty-free sales of tobacco products before further assessing possible violations of relevant international trade rules under the General Agreement on Tariff and Trade⁶³ (GATT) and the General Agreement on Trade in Service⁶⁴ (GATS).

⁶⁰ *Ibid* at 7-8.

⁶¹ Economic Commission for Europe Inland Transport Committee, Convention Concerning Customs Facilities for Touring, 276 UNTS 191 (signed New York, 4 June 1954, entered into force 11 September 1957, amended 6 June 1967) [Convention for Touring].

⁶² International Convention on the Simplification and Harmonization of Customs Procedure, 18 May 1973, 950 UNTS 269 (entered into force 25 September 1974) [Kyoto Convention].

⁶³ *The General Agreement on Tariffs and Trade*, 30 October 1947, 814 UNTS 61 arts 11, 55 [GATT 1947].

⁶⁴ *Marrakesh Agreement Establishing the World Trade Organization*, 15 April 1994, Annex 1B, 1869 UNTS 183, 33 ILM 1167 (entered into force 1 June 1995) [GATS 1994].

1. *Convention for Touring*

Article 3 of this Convention requires its Contracting States to allow tourists⁶⁵ to import a certain amount of tobacco products “free of import duties and import taxes”⁶⁶ provided that these tobacco products “are carried on the person of or in the hand luggage accompanying the tourist” and “there is no reason to fear abuse.”⁶⁷ The amount is set for 200 cigarettes, or 50 cigars, or 250 grams of tobacco, or an assortment of these products, provided that the total weight does not exceed 250 grams.⁶⁸ Given the term “shall admit” used in Article 3, Contracting States are legally obliged to allow tourists to import tobacco products free of import duties and import taxes.⁶⁹ If a Party to the FCTC happens to be a Contracting State to this Convention, this provision will limit the ability of the Party to prevent duty-free tobacco imports by tourists below the above threshold.⁷⁰

On the contrary, this paper finds that Article 3 does not heavily constrain the ability of Parties to regulate duty-free tobacco products through several latitudes embedded in this provision. Firstly, it is worth noting that Article 3 simply prevents Contracting States from imposing import taxes and import duties, but does not prohibit States from imposing excises taxes, welfare surcharges and other internal taxes on tobacco products sold to the tourists, if the transaction occurs at the duty-free stores within its territory. Therefore, Parties are free to apply excise taxes or other welfare surcharges on tobacco products sold at duty-free stores without contradicting Article 3 of this Convention.

⁶⁵ According to Article 1(b) of the Convention, the term “tourist” has been defined as “any person without distinction as to race, sex, language, religion, who enters the territory of a Contracting State other than that in which that person normally resides and remains there for not less than twenty-four hours and not more than six months in the course of any twelve-month period, for legitimate non-immigrant purposes, such as touring, recreation, sports, health, family reasons, study, religious pilgrimages or business.” *Convention for Touring*, *supra* note 61 at 232.

⁶⁶ According to Article 1(a) of the Convention, the term “import duties and import taxes” is defined to include “not only Customs duties but also all duties and taxes whatever chargeable by reason of importation.” *Ibid* at 230.

⁶⁷ See *Convention for Touring*, *supra* note 61, art 3.

⁶⁸ *Ibid.*

⁶⁹ *Ibid.*

⁷⁰ See WHO, *supra* note 30 at 7.

Moreover, Article 3 does not prevent States from imposing taxes or duties on tobacco products sold to tourists at duty-free stores for the purpose of “exportation” or use “in transit.” As such, Parties may decide to prohibit duty-free “sales” of tobacco products at the duty-free stores without violating Article 3 of the Convention for Touring because this provision only prescribes the activities of “importation” by tourists. In other words, banning duty-free “importation” of tobacco products may be inconsistent with Article 3 but banning duty-free “sales” (including exportation or in transit use) of tobacco products – as long as they are not imported by tourists – won’t be against this rule.

Finally, Parties may also be free to impose import duties and taxes on tobacco products for the amount carried by the tourist beyond the allowance threshold, and to prohibit the tourist from importing duty-free tobacco products below the threshold if such importation is proven to be abusive or intended for commercial use. In addition, if the Parties can prove that the tobacco products imported by the tourist are intended for commercial use (e.g. for resale purposes), import taxes and duties can then be imposed on those carry-on tobacco products even if the amount is within the permitted threshold. Although the authorities may have difficulty in monitoring the volume and adjudging the purpose of every importation by tourists, this paper argues that Article 3 has limited negative effects on duty-free regulations.⁷¹

2. *Kyoto Convention*

The Revised Kyoto Convention⁷² has a similar provision – Article 16 in Specific Annex J, Chapter 1 (Travellers) – that allows a certain amount of tobacco products to be imported by travellers free of import duties and taxes.⁷³ Unlike Article 3 of the Convention for Touring, Article 16 of the

⁷¹ It is worth noting that states may refer to Article 9 of the Convention providing that any prohibitions or restrictions on imports of duty-free tobacco products shall apply only in so far as they are based on other non-economic considerations – such as public health. This will be discussed in Section C of this Part.

⁷² *Kyoto Convention as amended by the Protocol of Amendment to the International Convention on the simplification and harmonization of Customs procedures* (signed 26 June 1999, entered into force 3 February 2006), 2370 UNTS 27 at 11 (Revised Kyoto Convention).

⁷³ It provides: “The quantities of tobacco goods, wine, spirits and perfume allowed to be imported free of import duties and taxes by travellers should be not less than: (1) 200 cigarettes or 50 cigars or 250 grams of tobacco, or an assortment of these products of a total weight not exceeding 250 grams; ...The facilities provided for tobacco goods and alcoholic

Revised Kyoto Convention is less likely to limit the ability of the Parties to regulate duty-free sales of tobacco products for at least two reasons.

Firstly, Article 16, a provision in the Specific Annex guidelines, does not impose an obligation on Parties unless Parties decide to accept this provision. Instead, the revised provision serves as “recommended practices”⁷⁴ without imposing any legally binding force upon Parties. Thus, this provision cannot prevent Parties from adopting measures to prohibit or restrict duty-free tobacco products unless they accept the provision contained in Specific Annex J, Chapter 1 of the Kyoto Convention.⁷⁵ Secondly, even if the Parties accept this provision, they may also make reservations against this particular recommended practice to avoid binding effects imposed upon them.⁷⁶ Therefore, this paper finds that the Kyoto Convention is unlikely to limit the ability of the Parties to prohibit or restrict duty-free tobacco products.

B. Legality of duty-free tobacco regulations under international trade laws

In addition to international conventions on tourism and customs, duty-free sales of tobacco products remain controversial among delegates mainly because of their concerns over the potential frustration of trade facilitation or the failure to comply with international trade rules.

Unlike conventions on tourism or customs, there are no international trade rules positively requiring Parties to allow duty-free sales of tobacco

beverages may, however, be restricted to persons who have reached a certain age and may not be granted, or may be granted in reduced quantities only, to persons who cross the border frequently or who have been out of the country for less than 24 hours.” *Ibid*, J.1/5.

⁷⁴ Article 1(c) of the Revised Kyoto Convention defines the “recommended practice” as “a provision in a Specific Annex which is recognized as constituting progress towards the harmonization and the simplification of Customs procedures and practices, the widest possible application of which is considered to be desirable.” *Ibid* at 2.

⁷⁵ Article 3 of the Revised Kyoto Convention clarifies the legal effect of such recommended practice, and provides that “The provisions of this Convention shall not preclude the application of national legislation with regard to either prohibitions or restrictions on goods which are subject to Customs control.” *Ibid* at 3.

⁷⁶ Article 9.2 of the Revised Kyoto Convention provides: “Any Contracting Party which accepts a Specific Annex or Chapter therein shall be bound by any amendments to the Recommended Practices contained therein, which have entered into force at the date on which it notifies its acceptance to the depositary, unless it enters reservations against one or more of those Recommended Practices in accordance with Article 12 of this Convention.” *Ibid* at 7.

products within their jurisdictions. Nonetheless, this paper examines whether WTO Members will be liable for possible violations of relevant international trade rules if they decide to prohibit or restrict duty-free sales and/or importations of tobacco products in their customs territory.

1. Characterization of duty-free regulations as trade policy measures

Before further examining the consistency issue, it is necessary to deal with the issue of characterization. Based on the possible policy options mentioned above, this paper characterizes the nature of various regulatory measures on duty-free tobacco products in light of different types of trade-policy tools, so that the issue of its compliance with trade rules can be examined accordingly.

The scope of duty-free regulations includes the “sales” and “importation” of duty-free tobacco products. Regulations targeting the “sales” of duty-free tobacco products may be characterized as either “border measures” or “internal measures” depending on where a measure is enforced or implemented. If the “sales” of duty-free tobacco products are prohibited at the border, such prohibition may be viewed as a tariff measure. When the “sales” of tax-free tobacco products are prohibited within the customs territory, it may be viewed as an internal taxation measure. In contrast, if the “sales” of duty-free tobacco products are simply restricted rather than an outright ban within the customs territory, such a restrictive measure can be categorized as an “internal measure.” If a measure prescribes the amount of tax to be paid, it is characterized as an “internal taxation” measure. If a measure prescribes other regulatory requirements to be fulfilled such as marketing, it can be considered as an “internal regulation” under the context of the GATT.

As for regulations targeting the “importation” of duty-free tobacco products, it can only be considered as “border measures”, given that such regulatory activity occurs at the border. While a state may choose to prohibit or restrict the importation of duty-free tobacco products, a measure targeting the importation of duty-free tobacco product is characterized as a tariff measure rather than a measure imposing “quantitative restrictions.” Given that a ban on the importation of duty-free tobacco products simply removes the privilege of duty-free benefits from the imported tobacco products, the tobacco products are still allowed to be imported without any quantitative restrictions so long as a full duty has been paid. Such regulations are tariffs in nature. This initial characterization of these duty-free regulations serves as

the basis for further analysis of the applicability of, and their compatibility with, international trade rules.

Characterization of Duty-Free Regulations

| Tobacco Control Measures | Trade Policy Tools & International Trade Rules | |
|---|---|--|
| | Border Measures | Internal Measures |
| <p>Duty-Free “Sales” Regulation</p> <p>(at duty-free stores or in transportation vehicles)</p> | <p>Prohibition:</p> <p>Impose “customs duties” on tobacco products (not meant to prohibit the sales of tobacco products)</p> <p>GATT Art. XI: ✗ GATT Art. V:</p> <p>Goods in transit: ✓ Goods not in transit: ?</p> | <p>Prohibition:</p> <p>Imposing all “internal taxes” as usual <u>duty-paid tobacco products</u></p> <p>GATT Art. III:2: ✓ GATT Art. V: ✗</p> <p>Restriction:</p> <p><u>Tax-reduction</u>: apply some “internal taxes” (e.g. excises, VAT, or welfare surcharge)</p> <p>GATT Art. III:2: ✓</p> <p><u>Non-price regulation</u>: subject to “internal regulation” or “TBT” (e.g. packaging & labeling or age limit)</p> <p>GATT Art. III:4: ✓</p> <p>TBT Agreement: ✓</p> |
| <p>Duty-free “Importation” Regulation</p> <p>(carry-on by individual)</p> | <p>Prohibition:</p> <p>Imposing “customs duties” (within the limit of tariff binding)</p> <p>GATT Art. XI: ✗</p> | <p>N/A</p> |

| | | |
|---|---|--|
| travellers entering into the territory) | <p>GATT Art. II: ✓</p> <p>Restriction: <u>Duty-free allowance</u> (free of customs duties)</p> <p>GATT Art. XI: ✕</p> <p>GATT Art. I: ✓</p> | |
|---|---|--|

2. Prohibition and/or restriction on duty-free importation of tobacco products and its consistency with international trade rules on border measures

Article XI:1 of the GATT provides: “[n]o prohibitions or restrictions other than duties, taxes or other charges ... shall be instituted or maintained by any Member on the importation of any product.”⁷⁷ An outright ban on importation of tobacco products will superficially run against this provision because prohibition is one of the most serious types of quantitative restrictions. In other words, if such a ban is understood as a categorical prohibition from importing or purchasing any amount of tobacco products, it will definitely be considered as a “quantitative restriction” under Article XI of the GATT.

However, this is not how such a ban is understood. The proposed duty-free regulation is not to prohibit the “transaction” of tobacco products at all; instead, it simply aims at eliminating “duty-free” privileges of tobacco products, which remain legally traded goods under the current multilateral trade system. In other words, what has been regulated is not the prohibition of import or export of tobacco products (goods) but the duty-free privilege attached to such products (duties). Since there is no prohibition or restriction on the quantity of importation, Article XI of the GATT is unlikely to constitute an obstacle to prevent Members from abolishing “duty-free”

⁷⁷ Article XI:1 of the GATT provides: “No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences or other measures, shall be instituted or maintained by any Member on the importation of any product of the territory of any other Member or on the exportation or sale for export of any product destined for the territory of any other Member.” *GATT*, *supra* note 63 at 224, 226.

tobacco products within their jurisdiction. Therefore, the nature of banning “duty-free” tobacco products is a type of taxation measure, which is allowed to be adopted under Article XI of the GATT.

Despite this, it is noteworthy that a Member must not impose customs duties or other charges on imported tobacco products in excess of their “bounded rate” as provided in the individual tariff schedule according to Article II:1 of the GATT.⁷⁸

Moreover, if a Member regulates duty-free tobacco products by providing a certain amount of allowance for international travellers, such a restrictive measure may be considered superficially as a measure of quantitative restriction because the rule only prescribes a certain amount of tobacco products legally allowed to be imported free of customs duties. By the same token, this rule is not designed to prohibit importation of tobacco products; instead, it only restricts the amount of tobacco products that can be imported free of any import duties or taxes. Basically, travellers are free to import as much as they can so long as they notify the customs personnel and pay the required import duties and taxes. Even if the amount of allowance does prescribe quantitative numbers, this rule is designed to fulfill the purpose of personal use for international travelers rather than serving the function of a trade policy tool. Therefore, the duty-free allowance regulation is unlikely to contradict Article XI:1 of the GATT, for the same as prohibition on the importation of duty-free tobacco products does not.

It should be noted that according to Article I of the GATT, Members must accord any “advantage, favour, privilege or immunity” granted to products imported from or exported to any other country, to like products imported from or exported to all WTO Members.⁷⁹ This most-favored-nation provision still applies to the duty-free regulations with respect to tobacco products. Therefore, the duty-free allowance regulation should be applied in a non-discriminatory manner, and cannot vary with the travellers’ country of origin or destination.⁸⁰ Otherwise, if a discriminatory duty-free allowance scheme is allowed, it will likely be in violation of the most-favored-nation obligation prescribed under Article I of the GATT.

⁷⁸ Article II: of the GATT provides: “Each Member shall accord to the commerce of the other Member treatment no less favourable than that provided for in the appropriate Part of the appropriate Schedule annexed to this Agreement.” *Ibid* at 200.

⁷⁹ GATT article I, *supra* note 63 at 196, 198.

⁸⁰ See WHO, *supra* note 23 at 5.

3. Prohibition of duty-free sales of tobacco products and its consistency with international trade rules on border measures

The measure prohibiting duty-free “sales” of tobacco products may need to be examined in accordance with trade rules governing either border or internal measures depending on the types of taxes or duties being imposed. For those tobacco products sold at the duty-free stores, a total ban on “duty-free” tobacco must eliminate all types of duty-free privileges including customs duties. Since the customs duties are being withdrawn at the duty-free shops, the legal issues over Articles XI and II of the GATT are similar to those involved with the “importation” of duty-free tobacco products as discussed in previous paragraphs. It should not be violative of Article XI or II of the GATT if states decide to adopt the duty-free regulations on the sales of tobacco products at the duty-free shops. However, in banning duty-free sales of tobacco products, special attention should be paid to the issue of the applicability of Article V of the GATT, which prescribes the freedom of transit.⁸¹

Article V:3 of the GATT⁸² could be the provision preventing WTO Members from prohibiting duty-free sales of tobacco products because it requires them to exempt customs duties on goods for travellers’ use in transit. It provides that “traffic in transit through its territory ... shall be exempt from customs duties.”⁸³ Article V:1 further defines the “traffic in transit” and provides that “goods (including baggage)” are deemed to be in transit “when the passage across such territory ... is only a portion of a complete journey beginning and terminating beyond the frontier of the Member.”⁸⁴ This provision may thus limit the ability of Parties to impose customs duties on tobacco products sold at duty-free stores in airports or transportation vehicles.

⁸¹ GATT, *supra* note 63 at 208.

⁸² Article V:3 of the GATT provides: “Any contracting party may require that traffic in transit through its territory be entered at the proper customs house, but, except in cases of failure to comply with applicable customs laws and regulations, such traffic coming from or going to the territory of other contracting parties shall not be subject to any unnecessary delays or restrictions and shall be exempt from customs duties and from all transit duties or other charges imposed in respect of transit, except charges for transportation or those commensurate with administrative expenses entailed by transit or with the cost of services rendered.” *Ibid* at 210.

⁸³ *Ibid*.

⁸⁴ See Article V:1 of the GATT, *ibid* at 208.

While the Convention for Touring obliges Contracting States to allow “importation” of tobacco products free of import duties and taxes by the tourists entering into their territory, Article V:3 of the GATT requires Members not to impose customs duties on goods (including baggage) “in transit,” passing through the territory of the Member.⁸⁵ In other words, a WTO Member cannot impose customs duties on the tobacco products carried onto its territory by international travellers who are in transit to a foreign country.

However, it is arguable whether this provision could really prevent a Member from imposing customs duties on tobacco products sold at the duty-free stores within its territory. If a traveler purchases a pack of cigarettes at the duty-free store but does not carry it on during their journey, will the tobacco products purchased with the intention to be consumed in the home country be considered as “goods used in transit”? It is not clear if Article V of the GATT can apply to this situation. The problem lies in the interpretation of “traffic in transit.” What if the goods are not “in transit” and purchased by international travellers who are in transit to another country? Would “traffic in transit” also include the beginning of travellers’ journey where it is “within” instead of “beyond” the territory of the Member? This paper argues that “traffic in transit” should be narrowly interpreted and Article V should not apply to the above situation for two reasons.

Firstly, as for the lexicon used in Article V of the GATT, the “traffic in transit” should refer to the transportation of goods that are shipped or transferred during voyage. If the goods are purchased within a Member’s territory, such goods are difficult to interpret as being “in transit” because the passage of such goods is not literally “a portion of a complete journey beginning and terminating beyond the frontier of the Member”; instead, it is purchased at either the beginning or the termination of the journey – not in transit. Moreover, such goods are not “passed or carried-on” by travellers entering the customs of the Member and “waiting for transfer to another country” if they are bought at the duty-free stores within the Member’s territory.

Secondly, such narrow interpretation of “traffic in transit” avails the WTO Member of more latitude to adopt effective tobacco-control measures regulating duty-free tobacco products. If as suggested, this provision only applies to a limited scope of tobacco products that are transported “in

⁸⁵ See WHO, *supra* note 23 at 5.

transit”, each Member may impose customs duties on tobacco products offered for sale at the duty-free stores within its own territory without violating Article V of the GATT. This is because tobacco products sold at the duty-free stores are not those “in transit” or “carried-on” by travellers even if the travellers themselves are in transit to a foreign country.

Lastly, it is noteworthy that Article V of the GATT does not preclude Members from imposing “excise taxes or other internal taxes” on goods in transit. This may not be as problematic because it is practically difficult for a Member to impose those internal taxes on goods in transit. However, this finding may be important if this provision is not narrowly interpreted and aims to cover the situation identified in the previous paragraphs. In other words, if Article V of the GATT, broadly interpreted, can prevent a Member from imposing customs duties on tobacco products sold at the duty-free stores within its territory, this provision still cannot prevent a Member from imposing excise taxes or other internal taxes on those tobacco products. Therefore, Parties to the FCTC can still restrict duty-free tobacco products by imposing excises taxes without violating Article V of the GATT.

4. Regulation of duty-free sales of tobacco products and its consistency with international trade rules on internal measures

If a WTO Member adopts the most stringent policy to prohibit duty-free sales of tobacco products, all tobacco products sold within its jurisdiction will have all internal taxes imposed on them, or be charged as usual duty-paid or tax-paid tobacco products without any privileges of tax- and duty-free exemptions. Members adopting such policy are required to comply with the national treatment obligation under Article III:2 of the GATT – the trade rule prohibiting discrimination between imported and domestically produced goods with respect to internal taxation or other government regulation. This national treatment obligation also applies to the less stringent approach of restricting duty-free sales of tobacco products if a Member chooses to adopt a tax-reduced or duty-reduced policy of tobacco products rather than a total ban on duty-free tobacco products.

Under Article III:2 of the GATT, Members may not subject imported products to “internal taxes or other internal charges of any kind in excess of those applied ... to like domestic products.”⁸⁶ In other words, Members

⁸⁶ Article III:2 of the GATT provides: “The products of the territory of any Member imported into the territory of any other Member shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly,

cannot impose higher internal taxes or other charges (e.g. welfare surcharges) on imported tobacco products than on those domestically manufactured. In compliance with Article III:2 of the GATT, Members should consistently and comprehensively apply all internal taxes or other internal charges to tobacco products sold at the duty-free stores and implement this in a non-discriminatory manner irrespective of whether the tobacco is being imported or domestically manufactured.

With respect to the non-price regulations that restrict “duty-free” sales of tobacco products (packaging, labeling and age limit), these measures may be either internal regulations or technical barriers to trade (TBT) subject to Article III:4 of the GATT⁸⁷ or relevant provisions under the TBT Agreement. The legality of such non-price measures is not as difficult to assess compared to the price-related measures examined above, such as duty-free allowance and duty-reduced tobacco products. These non-price regulations are less problematic as long as they are applied in a non-discriminatory manner and based on appropriate risk assessments or relevant international standards.

5. Potential issues of applicability under the GATS

With respect to the issues under the GATS, the WHO expert report does not specifically address the potential legal ramifications of the duty-free regulation under the GATS. It has been examined in light of the market access obligations under the GATS, and concluded that “a total ban on tobacco sales in duty-free stores would be a market access restriction under the GATS” if a Member “has unlimited commitments for retail distribution services.”⁸⁸ Moreover, the argument goes on to stress that the ban on duty-free sales of tobacco or reduced duty-free allowance is “potentially

to like domestic products ...” GATT, *supra* note 63 at 206.

⁸⁷ Article III:4 of the GATT provides: “The products of the territory of any Member imported into the territory of any other Member shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use...” *Ibid*.

⁸⁸ See Jane Kelsey, “International Trade Law and Tobacco Control: Trade and investment law issues relating to proposed tobacco control policies to achieve an essentially smokefree Aotearoa New Zealand by 2025”, (May 2012) at 35, 66-67, online (pdf): cpath.org <www.cpath.org/sitebuildercontent/sitebuilderfiles/jkelseyfinalreportjktobacco.pdf> [perma.cc/CGR5-ZRDJ].

problematic” because of potential violations of market access commitments under the GATS.⁸⁹

Such legal assessment seems to use a stricter understanding of banning duty-free sales of tobacco products as the basis of its analysis, i.e., to prohibit tobacco products sold at the duty-free stores altogether. However, this paper argues that such a stringent approach is not what the FCTC exclusively aims to prescribe. In actuality, the FCTC only prescribes the elimination of “duty-free” privilege of tobacco products sold at the duty-free stores.⁹⁰ Therefore, as long as tobacco products can still be sold at the duty-free stores, it is unlikely to contradict the market access commitments under the GATS even if those products are sold without bearing any duty-free privileges.

Article II:1 of the GATS provides that “this Agreement applies to measures by Members affecting trade in services.”⁹¹ Article II:2 further defines four modes of service supply: cross-border supply, consumption abroad, commercial presence and movement of natural person.⁹² For the GATS to apply, the duty-free regulations have to be measures affecting trade in service and categorized into one of the four modes of service supply. Thus, the problem begins with a proper characterization of the duty-free regulations in various forms as different modes of service supply.

It has been argued that the most significant “modes” are the supply of services across the border and through foreign investment (e.g. the commercial presence).⁹³ However, this paper finds these two modes are actually unlikely to be applicable to duty-free regulations.

For the first mode, trade in services is defined as “the supply of a service from the territory of one Member into the territory of any other Member.”⁹⁴ Providing duty-free tobacco products is difficult to consider as a cross-border supply of service. The duty-free tobacco products are purchased by international travellers elsewhere beyond the border and carried with them into the territory of the Member. There is no service supplied crossing the

⁸⁹ See *ibid.*

⁹⁰ FCTC art. 6.2, *supra* note 2 at 8.

⁹¹ GATS, *supra* note 64 at 186.

⁹² *Ibid* at 185-186.

⁹³ See Jane Kelsey, *supra* note 88 at 36.

⁹⁴ GATS, *supra* note 64 at 185.

border; instead, it is the tobacco products (goods) being transferred and imported across the border by the travellers themselves.

For mode three, it could be viewed as a commercial presence if a Member allows the duty-free stores to be owned by foreign companies according to its Schedule of Specific Commitments.⁹⁵ However, the proposed duty-free regulation has nothing to do with the issue of limitation on the ownership of duty-free stores. These proposed regulations target the tobacco products sold at the duty-free stores, not the ownership of the duty-free stores. This paper finds that it is unlikely to fit into mode three of service supply. Therefore, the regulation of duty-free sales of tobacco products is not likely to face legal difficulty under the GATS.

C. Available exemptions for a justifiable cause

As for potential challenges for trade violations, Members or Parties may wish to resort to relevant exemptions available in the international conventions if they are determined to adopt the policy of either prohibiting or restricting duty-free sales/importation of tobacco products. This paper identifies two available exemptions as the legal defense to justify possible violations.

1. Article 9 of the Convention for Touring

Article 9 of the Convention for Touring provides that:

“[e]ach of the Contracting States recognizes that any prohibitions which that State imposes on the importation or exportation of articles which benefit under this Convention shall apply only in so far as they are based on considerations other than economic in character, for example, of public morality, public security, public health, hygiene, veterinary or phyto-pathological considerations.”⁹⁶

According to this provision, Parties are free to impose any prohibitions as long as they are enacted on the basis of public health considerations. As indicated, Article 9 of the Convention for Touring requires fewer legal thresholds than Article XX of the GATT. It seems that Article 9 requires Contracting States to demonstrate that the regulatory objective is rooted in public health considerations and such prohibitive measures shall apply “only in so far as” they are based on the afore-mentioned objective. This provision allows the state to adopt a ban on the duty-free tobacco products so long as

⁹⁵ *Ibid.*

⁹⁶ *Convention for Touring, supra* note 61 at 236.

it is based on the public health considerations. Unlike the necessity test under Article XX of the GATT, Article 9 of the Convention for Tarring applies a more reasonable standard of rational connection between the policy goals and the adopted measure, rather than the more stringent necessity test, which requires adopting the least trade restrictive measure. Such interpretation of Article 9 will provide Parties the legal grounds for the adoption of policy either prohibiting or restricting duty-free sales of tobacco products, since such policy aims to promote public-health interests by abolishing duty-free sales of tobacco products. Therefore, even if Parties decide to abolish duty-allowance rules, it may not run afoul of Article 3 of the Convention for Tarring so long as the public-health objective and its reasonable connection can be well demonstrated by the state.

2. *Article XX of the GATT*

Article XX of the GATT, titled “General Exception”, provides an important exception for a WTO Member trying to adopt duty-free regulations. It states that:

“[s]ubject 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: (a) necessary to protect public morals; (b) necessary to protect human, animal or plant life or health; ... (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.”⁹⁷

To justify a duty-free regulation under the general exception provision, the government would need to show the ban was “necessary” and was the least trade-restrictive measure available to achieve the policy goals of either preventing illicit trade, reducing tobacco consumption or enforcing customs laws.

The major problem in applying this exception lies at the insufficient scientific evidence on the effectiveness of banning duty-free sales of tobacco products and the linkage between illicit trade and duty-free sales of tobacco products. Given the ban on duty-free sales/importation is only a part of multi-faceted tobacco control regulations, strong evidence may be needed to

⁹⁷ GATT, *supra* note 63 at 262.

show its effectiveness and the significance of its contribution to attaining the alleged policy objectives.

Despite this, the WTO jurisprudence adopted a weighing and balancing test to examine whether a specific measure at issue is necessary to achieve the policy objectives alleged by the state.⁹⁸ Unlike a more rigid “least trade restrictiveness” standard, Members are given more leeway to tilt a ruling in favor of duty-free regulations when applying the weighing and balancing test. Firstly, a Member can stress the importance of its policy objective given that the public health is at stake. Moreover, prohibiting or restricting duty-free tobacco does not prevent tobacco products from trading or being purchased by consumers. Such regulations do not negate the legal status of tobacco as a tradable commodity. It can be argued that such regulations have fewer trade-restrictive effects on tobacco products, and would be more likely to pass the necessity test under Article XX of the GATT so long as such regulations are applied in an even-handed manner.

VI. CONCLUSION

Combating the global tobacco epidemic is an endless task for the international community. The difficulty of adopting an effective tobacco control policy comes with the involvement of competing interests, different stakeholders and various policy considerations. The controversy over how to regulate duty-free tobacco products is one of the incidences of this regulatory dilemma.

A strong pro-health statement can be delivered when the WHO FCTC calls for a ban (or restriction) on the sale and import by international travellers of tax and duty-free tobacco products. Such regulations will not only enhance the effectiveness of tobacco taxation by reducing consumption, but also will eliminate duty-free sales of tobacco products and thus reduce opportunities for tax avoidance. However, it is inevitable to face difficulties

⁹⁸ See Appellate Body Reports: Brazil – Measures Affecting Imports of Retreaded Tyres (Complaint by the European Communities) (2007), WTO Doc WT/DS332/AB/R at para 156 (Appellate Body Report); China – Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products (Complaint by the United States) (2009), WTO Doc WT/DS363/AB/R at paras 239 and 242 (Appellate Body Report); India – Certain Measures Relating to Solar Cells and Solar Modules (Complaint by the United States) (2016), ¶ 5.59, WTO Doc WT/DS456/AB/R at paras 5-59 (Appellate Body Report).

in carrying out the full-fledged duty-free regulations recommended by the WHO FCTC as different stakeholders and multiple policy interests are involved. A vivid example was the negotiation of Article 13 of the Protocol, a result reflecting more out of a political compromise than the pure public health consideration.

With respect to the concern over the legal compatibility of such regulations with other international conventions, this paper finds that it is unlikely to become an obstacle for Parties to prohibit or restrict duty-free sales or importation of tobacco products. Some problems still remain, such as how to weigh the different interests of multiple stakeholders in the process of domestic policy-making, or how to adopt an effective and feasible approach to regulate duty-free sales and importation of tobacco products. Nevertheless, following the WHO's recommendation to implement a ban on the sale and import of tax and duty-free tobacco products would be a great first step.