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Addressing global environmental concerns through trade: extraterritoriality under WTO law from a comparative perspective

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Citation

Cooreman, B. E. E. M. (2016, June 14). *Addressing global environmental concerns through trade: extraterritoriality under WTO law from a comparative perspective*. Meijers Research Institute and Graduate School of the Leiden Law School of Leiden University, Leiden. Retrieved from https://hdl.handle.net/1887/40164

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Note: To cite this publication please use the final published version (if applicable).

Cover Page

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Title: Addressing global environmental concerns through trade measures : extraterritoriality under WTO law from a comparative perspective
Issue Date: 2016-06-14

2 Product or process – outlining the scope of trade law

2.1 INTRODUCTION

A number of policy tools are available in order to promote environmental policy through trade, such as price-based measures (e.g. taxes, subsidies, higher or lower tariffs) or non-price-based measures (e.g. standards, labeling, production requirements). Price-based measures can either be imposed on imported products only (and might be allowed if scheduled in accordance with Article II GATT) or can take the form of an internal tax (and might be allowed under Article III:2 GATT if non-discriminatory). Non-price-based measures can either be addressed under Article XI GATT if they are imposed at the border and have the form of quantitative barriers to trade, or can be addressed under Article III:4 GATT when imposed both on domestic and imported products. If an adopted trade measure were to violate substantive obligations under GATT, the general exceptions of Article XX foresee in limited environmental justification grounds. Non-tariff barriers can also be addressed under the Agreement on Technical Barriers to Trade (TBT Agreement) of the Agreement on Sanitary and Phytosanitary Measures (SPS Agreement).

As explained in the introductory chapter, trade measures with an environmental objective often aim at the production process rather than at the product itself, as the production process can pose a heavier burden on the environment than the actual product does so targeting production is more effective from an environmental perspective.[1] Measures aiming at the process and production methods are called PPMs, which can either have an impact on the physical characteristics of the final product whereby the environmental effects manifest themselves during distribution/marketing/consumption,[2] the so-called product-related PPMs (pr-PPMs, such as the use of pesticides on vegetables, or production with asbestos fibers that lead to a higher health risk); or can be unrelated to the end product, the so-called non-product-related PPMs (npr-PPMs, such as production of cement in a environmental-friendly factory with lower-than-average emission levels). There has been much debate on whether PPMs can be accepted under WTO law. Traditionally, trade law is concerned

1 Also called the rectification-at-source principle. See Puth(2003), 363.
2 OECD, *Processes and Production Methods (PPMs): Conceptual Framework and Considerations On Use of PPM-based Trade Measures* (1997) 10.

with the treatment of the end product on the market, which include pr-PPMs.[3] The question that needs to be clarified is whether a government can restrict imports of products based on their production processes that leave no trace in the final product (e.g. the use of dolphin-friendly fishing nets or the use of clean energy technologies); or whether in those cases governments are seen to impermissibly influence processes that occur beyond its territory.

This thesis seeks to analyse whether WTO law allows environmental trade measures aimed at protecting concerns outside their territory. In other words, what is the jurisdictional scope of WTO law with regard to the possible extra-territorial effect of npr-PPMs? The 'extraterritorial' nature and reach of npr-PPMs will be examined in chapter 3. The current chapter will outline the general legal framework for npr-PPMs: how can they be challenged under WTO law, and more specifically under the GATT. First, an overview of the trade-environment debate will be given. Second, after putting the development of the WTO and the rise of environmental concerns in their historical perspective, the relevant WTO rules will be elaborated upon. Those provisions that have been invoked in disputes on PPMs will be discussed. The relationship between Article III and Article XI GATT with respect to npr-PPMs will be analyzed, followed by the possible justifications under Article XX GATT.

2.2 The trade and environment debate

Trade and environment are indisputably linked, for instance, in the case of trade in natural resources (such as oil or valuable minerals), trade in products that contain natural resources (such as computer chips), trade in polluting end products (such car with high combustion engines), trade in goods with energy-intensive production (such as steel production), or lower tariffs for environmental-friendly products. States regulate the import of goods to their domestic market through bi-and multilateral trade agreements and unilateral trade measures. National environmental policies that regulate domestic production and set standards for domestic products on the market can be applicable to imports as well, possibly leading to trade restrictions.

The trade-environment relationship has been embedded in the GATT 1947, the predecessor to the current WTO agreements in the post-war global trading system. Article XX GATT 1947 included exceptions to the substantive GATT obligations, allowing Members to adopt measures 'necessary to protect human, animal or plant life'[4] or 'relating to the conservation of exhaustible natural resources'.[5] These measures, however, should not be protectionist or disguised

3 See e.g. WTO, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products* AB Report 2001, WT/DS135/AB/R; AB Report *US-Gasoline* 1996. See also chapter 2.
4 Article XX(b) of GATT.
5 Article XX(g) of GATT.

restrictions on international trade, as stated in the *chapeau* of Article XX. Article XX served to balance WTO Members' obligations not to discriminate between domestic and imported products and their right to regulatory autonomy, and has played an important role in the trade-environment debate.[6] The next reference to environmental protection in a GATT Agreement came with the conclusion of the Standards Code (the current TBT Agreement[7]), concluded during the Tokyo Round of the GATT (1973-79), after discussions on trade-related technical regulations and standards implemented for environmental purposes. Apart from references in these trade agreements, environmental concerns also found their way into multilateral environmental agreements (MEAs) starting from the mid '70s, such as the 1975 CITES[8] (mandating a system of trade bans and restrictions on trade in endangered species), the 1987 Montreal Protocol[9] (trade restrictions for ozone-depleting substances) and the 1989 Basel Convention[10] (on hazardous wastes).[11]

The beginning of the '90s was an important mark for the trade-environment debate. In 1992 the UN convened a landmark conference in Rio de Janeiro, the United Nations Conference on Environment and Development (UNCED, known as the '92 Rio Earth Summit), to set the tone and ambitions for global policy on development and environment. Leaders in Rio recognized the substantive links between international trade and environment by agreeing to strive for mutually supportive policies in favour of sustainable development.[12] It was

6 Hugo Cameron, 'The Evolution of the Trade and Environment Debate at the WTO' in Adil Najam, Mark Halle and Ricardo Melendez-Ortiz (eds), *Trade and Environment: A Resource Book* (International Institute for Sustainable Development, International Centre for Trade and Sustainable Development, The Regional and International Networking Group 2007) 3. Article XX will be discussed in further detail below at 1.4.2.

7 Article 2.2 TBT.

8 Convention on International Trade in Endangered Species of Wild Fauna and Flora, 99 3 UNTS 243, 1973.

9 Montreal Protocol on Substances that Deplete the Ozone Layer, 1522 UNTS 3, 1987.

10 Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal, 1673 UNTS 126; 28 ILM 657, 1989.

11 As different subsystems under international law, there is no hierarchy in norms between trade law and environmental law. Within the WTO dispute settlement, jurisdiction is li mited to the WTO Agreements, but MEAs can serve as interpretative means to the Agreements (and in particular to Article XX GATT), as was held by the AB in *US-Gasoline*, referring to Article 3.2 DSU.

12 Rio Declaration on Environment and Development 1992, A/CONF.151/26 (Vol. I). See in particular principle 12 stating that 'States should cooperate to promote a supportive and open international economic system that would lead to economic growth and sustainable development in all countries, to better address the problems of environmental degradation. Trade policy measures for environmental purposes should not constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade. Unilateral actions to deal with environmental challenges outside the jurisdiction of the importing country should be avoided. Environmental measures addressing transboundary or global environmental problems should, as far as possible, be based on an international consensus'.

acknowledged that international trade is a key component of sustainable development, through a more efficient allocation of scarce resources and easier access for countries to, for instance, environmental goods and technologies.[13]

In the meantime, the *Tuna-Dolphin* cases under the GATT[14] affirmed the fear of environmentalists that the global trading system was not sufficiently open to non-trade-concerns. At issue was a US measure differentiating tuna caught in a manner that harmed dolphins from tuna caught without harming dolphins. The US measure entailed that the import of tuna was only allowed when dolphin-friendly fishing nets were used. In order to have access to the US market, other states had to prove that they protected dolphins through systems comparable to the US system. The US measure was rejected by the first and the second GATT panel, as it was found that import bans could only protect concerns within the jurisdiction of the regulating state, that unilateral measures such as the one at issue were a threat to the multilateral trading system, and that the measure was to coercive towards other countries.[15]

The unadopted reports generated diverging reactions: on the one hand, developing countries favoured the panels' rejection, as it was feared that the imposition of such environmental standards would lead to green protectionism and would constrain development. Many NGOs and developed countries on the other hand, emphasized the need for a possible justification of trade-restrictive measures based on legitimate and necessary environmental protection measures.[16] The fact that the Marrakesh Agreement establishing the WTO (adopted after the conclusion of the Uruguay Round in 1994) recognized the need for trade to be consistent with the goal of sustainable development,[17] was in large part due to the public pressure from NGOs following the *Tuna-Dolphin* cases as well as the results of the 1992 Rio Summit.[18] The Marrakesh Agreement highlighted that trade liberalization should go hand in hand with environmental and social objectives.

This debate in the early 1990s raised further awareness about the link between trade and environment and public activism stimulated a continuing attempt at conciliating both interests. In a 1994 Decision on Trade and Environment, WTO Members acknowledged the outcomes of Rio and emphasized again the link between trade, environmental protection and sustainable develop-

13 WTO, *Harnessing Trade for Sustainable Development and a Green Economy*' (2011) 1.
14 GATT Panel *US-Tuna (Mexico)* 1991; GATT panel *US-Tuna (EEC)* 1994.
15 See *infra* at 4.1 for a further discussion of the legal analysis of the *US-Tuna* cases with respect to Article III and Article XI GATT, as well as chapter 2.4.2 for a discussion with respect to their extraterritorial nature.
16 Howard Mann and Yvonne Apea, 'Issues and Debates: Dispute Resolution' in Adil Najam, Mark Halle and Ricardo Melendez-Ortiz (eds), *Trade and Environment: A Resource Book* (International Institute for Sustainable Development, International Centre for Trade and Sustainable Development, The Regional and International Networking Group 2007) 6 8.
17 Marrakesh Agreement, 1994, preamble.
18 Mann and Apea(2007), 68.

ment.[19] They decided to establish a WTO Committee on Trade and Environment, dedicated to dialogue between governments on the impact of trade policies on the environment and of environmental policies on trade. The WTO dispute settlement system furthermore played a pivotal role in the debate. The first case filed after the creation of the WTO was an environmental dispute concerning the import of reformulated gasoline from Venezuela into the US.[20] The AB held that WTO law must be understood within the context of the broader body of international law, including MEAs[21] and emphasized that 'in the preamble to the WTO Agreement and in the Decision on Trade and Environment, there is specific acknowledgement to be found about the importance of coordinating policies on trade and the environment'.[22]

In 1997 the *US-Shrimp* case marked a milestone in the shift towards a more innovative and integrated approach to trade and environment in the light of Article XX GATT.[23] The dispute was launched by India, Pakistan, Thailand and Malaysia against the US, and concerned a US regulation banning the import of shrimp that was not harvested in a way that was certified as complying with US standards to protect endangered sea turtle. The AB emphasized the need to balance between the rights of WTO Members to market access and 'free' trade,[24] and the right to take measures relating to, for instance, the conservation of exhaustible natural resources under Article XX(g) of GATT.[25] It was confirmed that WTO Members have the right to adopt environmental policies, also when those have an impact on trade, whereby WTO law serves to limit the exercise of governmental discretion as agreed upon by the sovereign Members in order to guard that balance between trade and non-trade concerns.[26]

Since *US-Shrimp*, reconciling trade liberalization and environmental objectives has proven to be a challenging task. To further this end, the WTO Members launched trade and environment negotiations in the ongoing Doha Development Round.[27] Under the WTO principle of single undertaking, 'nothing has been agreed upon unless everything has been agreed upon', and as long as the Doha round is ongoing, the effect of such negotiations is limited. One of the issues on the agenda is strengthening the cooperation between the WTO

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19 Ministerial Decision on Trade and Environment, Marrakesh, 15 April 1994.
20 WTO, *United States-Standards for Reformulated and Conventional Gasoline* Panel Report 1996, WT/DS2/R.
21 Referring to Article 3.2 DSU.
22 AB Report *US-Gasoline* 1996, p.30.
23 AB Report *US-Shrimp* 1998. For a closer discussion of the legal analysis, see chapter 2.4.2.
24 What is meant with free trade is not unrestricted trade, but trade consistent with the substantive obligations in the WTO agreements.
25 Mann and Apea(2007), 69.
26 Petros C. Mavroidis, 'Trade and Environment after the *Shrimps-Turtles* Litigation' 2000, 34 Journal of World Trade 73, 74. See for a further discussion of the case law, chapter 2.
27 Doha Ministerial Declaration, para.6; see also UNEP and WTO, *Trade and Climate Change: WTO-UNEP Report* (2009) xvi.

and MEAs. Also on the Doha Agenda is the liberalization of environmental goods and services. The negotiations call for 'the reduction, or as appropriate, elimination of tariff and non-tariff barriers to environmental goods and services'.[28] The Committee on Trade and Environment acts as a forum within the Doha Development Round to debate environmental aspects of the negotiations.[29] While the discussion of PPMs is not on the agenda, PPMs have received a lot of scholarly attention as a possible means or alternative to address environmental concerns.[30] The central question of this thesis, the extraterritorial nature of PPMs, has largely been ignored in the literature. Before examining that issue in greater detail in the following chapter, the next section will outline the main characteristics of npr-PPMs and review the Article XI/III debate.

2.3 PRODUCT OR PROCESS

2.3.1 PPMs defined

An important question for environmental measures is: are we regulating the product or the process? Whereas product regulations regulate the design, characteristics, and uses of particular products, environmental PPMs regulate the production process and can 'seek to mitigate the environmental effects of private activities by specifying the conditions under which those activities must be carried out'.[31] Even though products themselves can also have an environmental impact (e.g. a polluting car), the production process will often have a greater environmental impact than the actual product. Examples are plenty: energy-intensive industries with high emissions, protection of plant life (e.g. forests, crops) or animal life (e.g. dolphins, sea turtles). PPMs can be formulated either by prescribing defined technologies, or by, for instance, specifying emissions or performance effects that need to be avoided or achieved.[32]

In general, two types of PPMs are distinguished: product-related PPMs (pr-PPMs) and non-product-related PPMs (npr-PPMs). Pr-PPMs are within the scope

28 Doha Ministerial Declaration, para. 31(iii); see also paras. 32, 33 and 51 which set out the 'environmental mandate'.
29 For more information see the homepage of the WTO Committee on Trade and Environment at http://www.wto.org/english/tratop_e/envir_e/wrk_committee_e.htm.
30 See among others Vranes(2009); Conrad(2011); Howse and Regan (2000); Horn and Mavroidis (2008); Charnovitz (2002).
31 Sanford E. Gaines, 'Processes and Production Methods: How to Produce Sound Policy for Environmental PPM-Based Trade Measures?' 2002, 27 Columbia Journal of Environmental Law 383, 394.
32 OECD (1997), 9.

of the TBT Agreement,[33] the SPS Agreement[34] as well as the GATT[35] and are not considered controversial. Food safety offers a good pr-PPM example of how regulators rely on process-based sanitary rules (e.g. pesticides on tomatoes).[36] Npr-PPMs on the other hand have no impact on the physical characteristics of the end product, but focus on, for example, the environmental effects during the production stage (production externalities).[37]

The division between product-related and non-product-related is arguably oversimplified. Consumers may have moral and ecological concerns, which might lead to a preference for goods produced in an animal-friendly or environmental-friendly manner, even if a blindfolded consumer will not be able to distinguish the products. In that way, for the consumer, these processes *are related* to the end product. Howse has argued that the definitions of pr-PPMs and npr-PPMs are incorrect: pr-PPMs do not necessarily relate to the physical characteristics of a product, but rather include all elements that determine a product's position on the market. The market position is strongly influenced by consumer preferences, and hence even those processes that do not change the characteristics of the end product *in se* are pr-PPMs.[38]

In EC-*Seal Products*, the panel and the AB had the opportunity to explore the issue of pr-PPMs under the first sentence of Annex 1.1 TBT. The EU imposed an import ban on all seal products due to public moral concerns with respect to the inhumane killing of seals, with exceptions for seal products from seals hunted by indigenous communities, from seals from hunts conducted for the sustainable management of marine resources, and seal products purchased by travellers. The panel found that the EU measure laid down product characteristics, without analyzing whether the measure might in the alternative also *relate* to product characteristics.[39] The AB reversed the panel's finding that the measure laid down product characteristics, but was unable to complete the legal analysis with regard to *related* PPMs due to a lack of arguments made

33 Annex 1.1 of the TBT Agreement does contain an explicit reference to *related* PPMs, without defining them, see below at 2.4.3 for a further discussion.

34 Sanitary rules are addressed under the SPS Agreement, which refers to end products as well as processes and production methods. Only measures seeking to prevent risks *within* the territory of the importing country fall within the scope of the SPS, and most likely due the nature of sanitary and phytosanitary measures most likely PPMs that do not have an impact on the physical end product would be excluded. See Annex 1 to the SPS Agreement.

35 See for instance AB Report *EC-Asbestos* 2001.

36 Charnovitz (2002), 65; Gabrielle Marceau and Joel P. Trachtman, 'The Technical Barriers to Trade Agreement, the Sanitary and Phytosanitary Measures Agreement, and the General Agreement on Tariffs and Trade: *A Map of the World Trade Organization Law of Domestic Regulation of Goods*.' 2002, 36 Journal of World Trade 811, 865.

37 OECD (1997), 10.

38 Robert Howse, 'Seals Hearing, Day I (part I)', International Economic Law Blog, 18 March 2014; See also Meredith A. Crowley and Robert Howse, '*Tuna-Dolphin II*: A Legal and Economic Analysis Of The Appellate Body Report' 2014, 13 World Trade Review 321, 327.

39 WTO, *European Communities – Measures Prohibiting the Importation and Marketing of Seal Products* Panel Report 2013, WT/DS401/R, para.7.106;7.112.

by the parties and an insufficient exploration by the panel of the relevant issues.[40] The AB did recognize that the distinction between related and non-related PPMs raises systemic issues.[41] It found that product characteristics include objectively definable 'features', 'qualities', 'attributes' or other 'distinguishing marks' of a product;[42] and stated that it must be examined whether the prescribed PPM has 'a sufficient nexus to the characteristics of a product in order to be considered *related* to those characteristics'.[43] While it found the exceptions of the EU Seals regime (the indigenous exception, the travellers exception and the marine resources exception) to not lay down product characteristics, the AB did not clarify whether the identity of the hunter, the type of hunt, or the purpose of the hunt could be seen as *related* to product characteristics.[44] Thus, without clarifying what the 'sufficient nexus' could consist of, it remains unclear whether related PPMs must thus have a physical impact on the end product. If a moral concern about the environmental impact of the production process is to considered 'a sufficient nexus to the characteristics', the traditional distinction between pr- and npr-PPM based purely on physical characteristics should be reviewed.

However, in light of the lacking guidance by the AB on the matter, this thesis will use the distinction between pr-PPMs and npr-PPMs based on the physical characteristics, focusing on those PPMs that have no impact on the physical characteristics of a product (npr-PPMs), as they do not fall within the traditional trade premise that focuses on end products. For the purpose of this research even a general reference to PPMs is to be equated with npr-PPMs.

2.3.2 PPMs as policy tools

Governments can impose npr-PPMs for a number of reasons:[45] as a true incentive for better environmental protection,[46] as a response to consumers' desire for information, or to address economic competitiveness concerns to level the playing field between domestic and imported products, where domestic production processes are subject to stringent environmental regulations.[47] If states cannot impose requirements related to the production of imports, the

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40 WTO, *European Communities – Measures Prohibiting the Importation and Marketing of Seal Products* AB Report 2014, WT/DS401/AB/R, para.5.69.

41 Ibid para.5.173.

42 Ibid para.5.11.

43 Ibid para.5.12.

44 Ibid para.5.45.

45 See for an overview of considerations on the motivation, feasibility, effectiveness and efficiency: OECD (1997), 23.

46 See for instance James Bacchus, *Global Rules for Mutually Supportive and Reinforcing Trade and Climate Regimes – E15 Expert Group on Measures to Address Climate Change and the Trade System* (2016).

47 Charnovitz (2002), 62.

efficiency of (domestic) environmental policy could be undermined, as this could lead to a race to the bottom,[48] whereby countries with the least stringent environmental regimes could specialize in the most polluting or least environmental-friendly industries. PPMs can be seen as attempts 'to prevent foreign producers from reaping the benefits of lower human rights, labor, environmental, or other standards'.[49]

While not explicitly prohibited nor allowed under the WTO Agreements, the use of npr-PPMs is controversial. They can restrict trade and make it harder and costlier for an exporter to supply a foreign market.[50] Differing product standards in different export markets may limit the exporter's ability to access several markets.[51] Furthermore, imposing environmental practices to other countries through npr-PPMs can create resistance in the exporting country and can be considered as interference with the exporting country's sovereignty.[52] The acceptance of environmental npr-PPM standards could also open doors to human rights or labour rights npr-PPMs, which is met with some resistance from developing countries in particular.[53] PPMs imposed by developed countries targeting developing countries may be seen as tools of eco-imperialism.[54] It is inherent to trade measures that a 'popular' export market is in a more powerful position to require compliance, in contrast to smaller export markets.[55] In order to prevent abuse, it is thus important to install sufficient safeguards to ensure the legitimacy of the imposed npr-PPMs.[56] However, in the current absence of binding international agreements on important environmental concerns such as climate change, npr-PPMs can as well be a means to 'incentivize' all trading partners, developed and developing, to adhere to higher environmental standards. As long as non-protectionist trade requirements are coupled with other initiatives to ensure environmental protection, such as, for instance, the transfer of know-how on green technologies and financial assistance, environmental-friendly policies could lead to

48 However, empirical evidence is limited and the effect seems to be overestimated – see Bradford (2012).
49 Ankersmit, Lawrence and Davies (2012), 31.
50 OECD (1997), 14.
51 Johannes Norpoth, 'Mysteries of the TBT Agreement Resolved? Lessons to Learn for Climate Policies and Developing Country Exporters from Recent TBT Disputes' 2013, 47 Journal of World Trade 575, 578.
52 Charnovitz (2002), 62.
53 Tom Rotherham, 'Issues and Debates: Standards and Labelling' in Adil Najam, Mark Halle and Ricardo Melendez-Ortiz (eds), *Trade and Environment: A Resource Book* (International Institute for Sustainable Development, International Centre for Trade and Sustainable Development, The Regional and International Networking Group 2007) 184.
54 Shaffer (2000), 624; Voon (2000), 100; Charnovitz (2002); Eric Neumayer, *Greening Trade and Investment: Environmental Protection Without Protectionism* (Earthscan 2001) 15.
55 See for an interesting discussion of powerful markets: Grewal(2008).
56 Gaines (2002), 427.

global benefits, both for developed and developing countries.[57] From a WTO law perspective, the challenge lies in determining the legitimacy and non-protectionist intention of npr-PPMs, thus distinguishing acceptable from unacceptable npr-PPMs.

2.4 LEGAL ANALYSIS OF NON-PRODUCT-RELATED PPMS

2.4.1 The violation: Article XI v Article III GATT

The idea that npr-PPMs are always infringing a WTO rule stems from the non-adopted *Tuna-Dolphin* GATT panel reports.[58] The first case dealt with an import ban by the US on tuna originating in Mexico: by not using special dolphin-friendly fishing nets, Mexican fishermen accidentally killed dolphins. The GATT panel held that the US regulations did not apply to the products as such and thus could not fall within the scope of Article III GATT on national treatment. Therefore, the regulation had to be seen as an import ban, to be dealt with under Article XI GATT on quantitative restrictions.[59] Under Article XI GATT the US regulations were considered illegal, and therefore prohibited, unless justified under the Article XX exceptions. The GATT panel found that measures addressing concerns outside their jurisdiction (the safety of dolphins) could not be justified under Article XX.[60] The second GATT panel (with this time the EEC as complainant) held that 'likeness' of products should be determined based on the physical characteristics of a product and not on the manner in which they are processed or produced. Again the US regulation was treated as an import ban rather than an internal regulation.[61] With regard to Article XX GATT, the panel did not find a valid ground as to why policies should be limited to the conservation of resources within the territory of a Member.[62] It did find, however, that measures taken so as to coerce other countries to change their policies were not allowed.[63]

It has been a persistent conviction ever since among many trade observers that npr-PPMs are not allowed under WTO, a view that I believe to be incorrect. Five years after the first *Tuna-Dolphin*, the AB came back to the issue of npr-

57 See chapter 7.4 and 7.6 for a further discussion of market power and safeguards under the chapeau of Article XX GATT.

58 GATT Panel *US-Tuna (Mexico)* 1991; GATT panel *US-Tuna (EEC)* 1994; Mann and Apea(2007), 74.; Joost Pauwelyn, 'Recent Books on Trade and Environment: GATT Phantoms Still Haunt the WTO' 2004, 15 European Journal of International Law 575, 585.; For a further discussion of the cases, see below as well as chapter 2.

59 GATT Panel *US-Tuna (Mexico)* 1991, para.5.14. See infra for a discussion of Article III and XI GATT.

60 Ibid paras.5.26;5.31.

61 Ibid para.5.11.; GATT panel *US-Tuna (EEC)* 1994, para.5.8.

62 GATT panel *US-Tuna (EEC)* 1994, para.5.20.

63 Ibid para.5.27.

PPMs in *US-Shrimp*. The facts were similar, only that this time shrimp and sea turtles were concerned, instead of tuna and dolphins. In this case a violation of GATT law (Article III or Article XI) was assumed and not contested by the US; hence both the panel and the AB focused on Article XX GATT in their analysis. The AB took a different stance than the GATT panels in the first *Tuna-Dolphin* case: the AB held that the conservation measures at issue did fall within the scope of Article XX,[64] implying there is thus no principled prohibition on npr-PPMs.[65] However, as the US did not defend itself either under Article III or Article XI, the AB could not examine whether npr-PPMs could possibly be compatible with Article III.

The relationship between the Article III and Article XI GATT is partly addressed in the Interpretative Note Ad Article III. The Ad Note appears to exclude a simultaneous application of both provisions.[66] According to the Ad Note, two conditions must be met for a measure to fall under Article III: firstly, the measure must apply to imported and like domestic products; and secondly, the measure must be enforced at the time or point of importation of the imported product. Domestic measures, even if applicable at the border, remain covered by Article III.[67] If a measure is applied exclusively to imported products and is solely a border measure, then the relevant provision is Article XI. Different aspects of a measure may be scrutinized under both articles, however.[68] Once a panel (or the AB) has found that a particular measure violates one GATT obligation, it does not need to investigate whether the same measure violates other GATT obligations as well.[69] Also, neither a panel nor the AB can address a provision *ex officio* when that provision has not been invoked by either complainant or defendant. For instance, in *US-Shrimp*, the US did not raise Article III in its defense, which led to the reports being focused on the justifications under Article XX GATT.

For the purpose of this chapter, the relation between Article XI and Article III is of particular interest, as measures falling under Article III can still be found to be consistent with the national treatment obligation. Under Article III a measure is only inconsistent when discriminatory, and differentiation based on production methods may not be deemed discriminatory if the products at issue are unlike or if the differentiation is not deemed to be protect-

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64 AB Report *US-Shrimp* 1998, para.121.

65 For a further discussion of these cases with a particular focus on the extraterritorial location of concerns to be protected, see chapter 3.

66 See also WTO, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products* Panel Report 2001, WT/DS135/R, paras.8.91.

67 Peter C. Mavroidis, *Trade in Goods: The GATT and the Other WTO Agreements Regulating Trade in Goods* (2nd edn, Oxfor University Press 2012) 66.

68 WTO, *India – Measures Affecting the Automotive Sector* Panel Report 2001, WT/DS146/R, para.7.224.

69 WTO, *US-Measures Affecting Imports of Woven Wool Shirts and Blouses from India* AB Report 1997, WT/DS33/AB/R, 18.

ive of domestic products. There is no similar opportunity under Article XI, as all border measures that are capable of restricting imports will infringe this provision. Measures that are inconsistent with either provision can be justified under Article XX if they are in compliance with the conditions of both the paragraphs and the *chapeau*.

2.4.1.1 Issues under Article XI GATT

Article XI:1 GATT reads

> '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 contracting party on the importation of any product on the territory of any other contracting party or on the exportation or sale for export of any product destined for the territory of any other contracting party.'

Article XI GATT entails a prohibition on quantitative restrictions. In principle import and export quantitative restrictions are prohibited irrespective of their rationale. As soon as a restriction falls within the scope of Article XI, a violation can be found and no discriminatory effect needs to be established. Duties, taxes and other charges are excluded from the scope of Article XI, as they are addressed under Articles I, II and III:2 GATT. Article III:4 also covers internal measures applied at the time of importation, according to the above-cited Ad Note.

The first *Tuna-Dolphin* GATT panel considered that the production method (the method of fishing tuna) could not fall under Article III GATT as the US regulation did not apply to the products as such.[70] Instead the measure was considered inconsistent with Article XI, as a prohibition or import restriction on tuna caught by dolphin-harming fishing nets.[71] That decision to address PPMs under Article XI supported a strictly territorial view: if the production method does not take place within the domestic market but in the exporting Member, a WTO Member cannot regulate those production methods.[72] The panel's approach can be criticized because the regulations in question did apply to imported and domestic products and did serve a policy purpose. Once a restriction is dealt with under Article XI the violation is easily established, and the analysis will turn to Article XX GATT.

70 GATT Panel *US-Tuna (Mexico)* 1991, para. 5.15.
71 Ibid para.5.18.
72 Marceau and Trachtman (2002), 858.

2.4.1.2 Issues under Article III GATT

Whereas a violation under Article XI GATT is straightforward, the legal analysis of PPMs under Article III is less obvious. If a PPM measure would be dealt with under Article III there are several conditions that need to be fulfilled in order to establish a violation. Article III GATT lays down the national treatment obligation, or the obligation to treat imported products no less favourably than domestic products. National treatment prohibits discrimination against imported products once the imported product has entered the domestic market.

The relevant paragraphs of Article III GATT read

> '1. The contracting parties recognize that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products, and internal quantitative regulations requiring the mixture, processing or use of products in specified amounts or proportions, should not be applied to imported or domestic products so as to afford protection to domestic production.
> 2. The products of the territory of any contracting party imported into the territory of any other contracting party 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, to like domestic products. Moreover, no contracting party shall otherwise apply internal taxes or other internal charges to imported or domestic products in a manner contrary to the principles set forth in paragraph 1.
> (…)
> 4. The products of the territory of any contracting party imported into the territory of any other contracting party 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. The provisions of this paragraph shall not prevent the application of differential internal transportation charges which are based exclusively on the economic operation of the means of transport and not on the nationality of the product.'

Article III contains disciplines on domestic taxation and regulation. Article III:2 requires that imported products shall not be subject to (internal) taxes of any kind in excess of those applied to like domestic products. Article III:4 requires that imported products shall be accorded treatment no less favourable than that accorded to like domestic products in respect of laws and regulations affecting among others their sale and transportation. Article III:1 adds the general principle that none of the above shall be applied in a manner so as to afford protection to domestic production.[73] In *Korea-Alcoholic Beverages* the AB identified the objectives of Article III as 'avoiding protectionism, requiring equality of competitive conditions and protecting expectations of equal com-

73 WTO, *Japan-Taxes on Alcoholic Beverages* AB Report 1996, WT/DS8/AB/R, para. 111.

petitive relationships'.[74] The current analysis will focus on Article III:4 GATT as the centre of gravity for the legal analysis of regulatory npr-PPMs. Whereas environmental measures in the form of fiscal measures, such as border tax adjustments (BTAs) or border carbon adjustments (BCAs) have received considerable scholarly attention,[75] this thesis will focus on regulatory schemes rather than fiscal measures as the latter pose particular question beyond the focus of this thesis, which is the extraterritorial nature of npr-PPMs.

Article III establishes a three-tier test of consistency: first, the measure at issue must be an internal tax or charge (Article III:2) or an internal regulation (Article III:4); second, the products concerned must be like; and third, the like imported products must not be treated less favourably than domestic products (so as to afford protection to domestic products). Article III does not only cover 'in law' or *de jure* discrimination, but also covers 'in fact' or *de facto* discrimination.[76] Whereas *de jure* discrimination is judged on the wording of the measure – an explicit distinction made based on origin –, in order to find *de facto* discrimination, an origin-neutral measure must differentiate between imported and domestic products, imposing a burden on the imported products that is

74 WTO, *Korea – Taxes on Alcoholic Beverages* AB Report 1999, WT/DS75/AB/R, para. 120.

75 BTAs are fiscal measures that charge imported products a tax similar to what domestic products are being charged, in order to level the playing field (*GATT: Report of the Working Party on Border Tax Adjustments* (1970) para. 4.). The aim of a BCA is to level the playing field by imposing a similar constraint on the carbon emissions of the imported and domestic goods. Jean Foure, Houssein Guimbard and Stephanie Monjon, 'Border Carbon Ajustment in Europe and Trade Retaliation: What would be the Cost for European Union?' 2013, 34 CEPII Working Paper; Henrik Horn and Peter C. Mavroidis, 'To B(TA) or not to B(TA)? On the Legality and Desirability of Border Tax Adjustments From a Trade Perspective'34 The World Economy 1911; Javier de Cendra, 'Can Emissions Trading Schemes be Coupled with Border Tax Adjustments? An Analysis vis-a-vis WTO Law' 2006, 15 Review of European Community & International Environmental Law 131; Kati Kulovesi, 'Climate Change and Trade: At the Intersection of Two Interacting Legal Regimes' in Erkki Hollo, Kati Kulovesi and Michael Mehling (eds), *Climate Change and the Law* (Springer 2013) 435; Reinhard Quick, 'The Debate Continues: Are Border Adjustments of Emission Trading Schemes a Means to Protect the Climate or Are They 'Naked' Protectionism?' in Inge Govaere, Reinhard Quick and Marco C.E.J. Bronckers (eds), *Trade and Competition Law in the EU and Beyond* (Edward Elgar 2011); Roland Ismer and Karsten Neuhoff, 'Border Tax Adjustment: A Feasible Way to Support Stringent Emission Trading' 2007, 24 European Journal of Law and Economics 137; Patrick Low, Gabrielle Marceau and Julia Reinaud, 'The Interface between the Trade and Climate Change Regimes: Scoping the Issues' 2011, WTO Staff Working Paper; Joost Pauwelyn, 'Carbon Leakage Measures and Border Tax Adjustments under WTO Law' in Denise Prevost and Geert Van Calster (eds), *Research Handbook on Environment, Health and the WTO* (Edward Elgar 2012).

76 A measure discriminates *de jure* when it is clear from reading the text of the law or regulation that it is discriminatory. If on the face the measure does not seem to discriminate, a measure can still be *de facto* discriminatory if on reviewing of the facts, it becomes clear that it discriminates in practice.; see James Flett, 'WTO Space for National Regulation: Requiem for a Diagonal Vector Test' 2013, 16 Journal of International Economic Law 37, 20.

considered illegitimate.[77] Regulatory distinctions can be of particular relevance when dealing with *de facto* discriminatory measures.

From an environmental perspective, it would be much more beneficial to consider PPM measures under Article III than under Article XI, as this would allow WTO Members to make regulatory distinctions between two physically similar goods and consider them unlike because of their production method, based on, for instance, consumer preferences. Alternatively, regulatory purposes could be considered when examining whether distinctions relate to the foreign origin of imported goods. If the products would be considered unlike because of a different production method, or no discrimination related to the foreign origin of the goods could be detected, there would be no inconsistency with Article III and no recourse to Article XX would be needed.

2.4.1.2.1 Determining likeness

The concept of like products is not defined in the GATT, even though likeness recurs in a number of provisions, and has thus been subject to much debate and jurisprudence. It is agreed that the concept of 'like products' has a different meaning in the different contexts where it is used. In *Japan-Alcoholic Beverages II* the AB used the image of an accordion which 'stretches and squeezes' in different provisions. The AB stated that

> 'the width of the accordion in any one of those places must be determined by the particular provision in which the term 'like' is encountered as well as by the context and the circumstances that prevail in any given case to which that provision may apply.'[78]

In general, the criteria of the GATT Working Party on Border Tax Adjustments are relied on to determine likeness. These encompass (i) physical characteristics of a product, such as the products' properties, nature and quality; (ii) consumers' tastes and habits; and (iii) the products' end-uses in a given market.[79] In *Spain – Unroasted Coffee*, the GATT panel also considered the tariff classifications of the products.[80] Products do not need to be identical, but they need to be similar.[81] For instance, likeness under the first sentence of Article III:2 should be interpreted narrowly, because the second sentence of Article III:2 bears on products that are 'directly competitive or substitutable products'.[82] The second sentence is based on a more general criterion, namely the protective

77 Robert E. Hudec, 'GATT/WTO Constraints on National Regulation: Requiem for an "Aim and Effects" Test' 1998, 32 International Lawyer 619, 623.
78 AB Report *Japan-Alcoholic Beverages II* 1996, para. 114.
79 (1970), para. 18.
80 GATT, *Spain – Tariff Treatment of Unroasted Coffee* GATT Panel Report 1981, BISD 28S/102, paras. 4.6.
81 AB Report *Japan-Alcoholic Beverages II* 1996, para. 113.
82 Annex I to the GATT, Note *Ad* Article III, paragraph 2

nature of the system of internal taxation and therefore applies only if the imported and domestic products are not like products.[83] In *Korea-Alcoholic Beverages,* the AB explained that by definition all 'like' products are 'directly competitive or substitutable', but not vice versa.[84] According to the AB, 'directly competitive or substitutable' refers to a competitive relationship in the marketplace, determined from the consumer's perspective. Cross-price elasticity of demand in the relevant market can be a helpful tool.[85] Products that do not compete cannot be like products, and like products are in an especially close competitive relationship.

Article III:4, establishing national treatment for internal regulations, has been interpreted broadly, to include all measures that may modify the conditions of competition.[86] The non-discrimination obligation applies to 'like' products. In *EC-Asbestos* the AB observed that where Article III:2 consists of two separate sentences with distinct obligations, narrowing the scope of 'likeness' in the first sentence, Article III:4 by contrast only applies to 'like products'.[87] The accordion of likeness hence stretches differently in both paragraphs. In light of the general principle of non-protectionism in Article III:1, 'like products' must be in a competitive relationship. The AB clarified that not '*all* products which are in *some* competitive relationship are "like products" under Article III:4'.[88] While likeness under Article III:4 has a broader scope than under the first sentence of Article III:2, that scope is not broader than the two sentences of Article III:2 combined. The nature and extent of the competitive relationship need to be determined on a case-by-case basis, based on the known criteria of physical properties, end-use, consumer preferences and tariff classification.[89] The AB thereby emphasized that all relevant evidence needs to be taken into account, such as for instance the health risk posed by asbestos, as constituting a defining aspect of the physical properties.[90]

If likeness is determined through a competitive relationship, it may well be that physically identical products may nevertheless not be 'like' when consumer preferences point to the contrary.[91] It is ultimately the consumer

83 AB Report *Japan-Alcoholic Beverages II* 1996, paras. 112.
84 AB Report *Korea-Alcoholic Beverages* 1999, para. 118.
85 Ibid para. 121.
86 GATT, *Italian Discrimination Against Imported Agricultural Machinery* GATT Panel Report 1958, BISD 7S/60, para. 12.
87 AB Report *EC-Asbestos* 2001, para. 94.
88 Ibid para. 99.
89 Ibid para. 101.
90 Ibid para. 115.
91 Reinhard Quick and Christian Lau, 'Environmentally Motivated Tax Distinctions and WTO Law: The European Commission's Green Paper on Integrated Product Policy in Light of the 'Like Product-' and 'PPM-' Debates' 2003, 6 Journal of International Economic Law 419, 431.; Marco C.E.J. Bronckers and Natalie McNelis, 'Rethinking the 'Like Product' Definition in GATT 1994: Anti-Dumping and Environmental Protection' in Marco C.E.J. Bronckers (ed), *A Cross-Section of WTO Law* (Cameron May 2000); Donald Regan, 'Regulatory

who determines whether a competitive relationship between products exists.[92] What if consumers have such a strong preference for green products, or for goods produced under fair and healthy labor conditions, to the extent that the less-green or unfairly manufactured shirt is no longer an alternative option? Only a very weak competitive relationship might then exist between two physically like products. To this date, no case has yet been adjudicated where products were found to be unlike because of consumer preferences, if they were otherwise found to have the same characteristics.[93]

For npr-PPMs consumer preferences could be the decisive element in a likeness determination. Nevertheless, non-likeness, or the non-existence of a competitive relationship based on consumer preferences, seems very difficult to prove.[94] Identical products are usually in a competitive relationship because they at least potentially compete with each other as substitutable products.[95] A market-based analysis requires an economic analysis of consumer preferences on a case-by-case, country-by-country basis.[96] Only if consumers are willing to pay a higher price for a product that has been produced in a different way, and where the other products is not considered a viable alternative, can the competitive relationship between identical products be ruled out.[97] Consumer preferences as determinant factor in a likeness analysis do not guarantee an environmental-friendlier outcome. Notwithstanding good intentions, in most markets consumers are primarily guided by the price of products and less by, for instance, the environmental conditions of production. Even with well-informed consumers it is not clear whether a sufficiently large group of consumers would indeed change their preferences purely based on environmental grounds. That does not necessarily mean that people do not care about the environmental concerns, but studies have shown that people express different preferences as a voter/citizen than as a consumer.[98] Price awareness is even

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Purpose and 'Like Products' in Article III:4 of the GATT (With Additional Remarks on Article III:2)' 2002, 36 Journal of World Trade 443, 447.

92 Pauwelyn (2004), 586. Consumer preferences play an important role in a market-based approach, see also Conrad(2011), 222. See also Won-Mog Choi, *'Like Products' in International Trade law. Towards a Consistent GATT/WTO Jurisprudence* (Oxford University Press 2003) chapter II.3.

93 Note that in *EC-Asbestos* the AB considered the fibres in question as 'physically very different' because of its health risks, which would in turn influence consumers' tastes.

94 Quick and Lau (2003), 431.

95 Ibid 432.

96 Bronckers and McNelis(2000), 50.

97 Conrad(2011), 227.

98 Cass Sunstein, 'Endogenous Preferences, Environmental Law' 1993, 22 Journal of Legal Studies 217, 242., explaining why some concerns may be highly valued by political participants, who are simultaneously not willing to back up that valuation as consumers on te market; Daphna Lewinsohn-Zamir, 'Consumer Preferences, Citizen Preferences, and the Provision of Public Goods' 1998, 108 Yale Law Journal 377, 379., arguing that consumers may perceive a sense of 'hopelessness' that is absent in political settings; Deborah Guber, *The Grassroots of a Green Revolution: Polling America on the Environment* (Cambridge: MIT

more determinant for poor consumers: wealthier consumers could more easily choose between products according to their general preferences, while poor consumers need to give more consideration to the price. Following this logic, the same measure that might be considered legal in wealthy countries, could be found illegal in poor countries.[99] A market-based approach through consumer preferences thus raises challenges with regard to environmental concerns.

2.4.1.2.2 Treatment no less favourable

Treatment no less favourable requires effective equality of opportunities for imported products to compete with like domestic products.[100] A distinction in treatment can be *de jure* or *de facto*,[101] but any determination of treatment no less favourable requires an assessment of the implications of the measure at issue for the group of imported products and the group of domestic products.[102] Article III:4 does not require the *identical* treatment of imported and like domestic products, but rather the *equality of competitive conditions* between these like products.[103] A mere distinction based on origin is not sufficient but a detrimental impact on the conditions of competition for like imported products must be shown.[104] There is no *de minimis* standard for treatment less favourable,[105] but there must be a 'genuine relationship' between the measure at issue and the adverse impact on competitive opportunities for imported products.[106]

The AB has held that Members can draw regulatory distinctions without this necessarily leading to discrimination.[107] The tipping point seems to be where the regulatory distinctions distort the conditions of competition to the detriment of imported products.[108] However, should the assessment of treatment less favourable not go beyond a mere consideration of a detrimental effect on competitive opportunities, but rather consider whether these detrimental

Press, 2002), 155, noting that a critical component of an individual's willingness to engage in activity designed to support environmental causes or other public goods hinges upon the perceived efficacy of that activity.

99 Conrad(2011), 234.

100 Panel Report *US-Gasoline* 1996, para.6.10.

101 Lothar Ehring, '*De Facto* Discrimination in World Trade Law: National and Most-Favoured-Nation Treatment – or Equal Treatment?' 2002, 36 Journal of World Trade 921.

102 AB Report *EC-Seal Products* 2014, para.5.101.

103 Ibid para.5.108.

104 WTO, *Korea-Measures Affecting Imports of Fresh, Chilled and Frozen Beef* AB Report 2000, WT/DS161/AB/R, para.135.

105 WTO, *China-Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment* Panel Report 2009, WT/DS363/R, para.7.1537.

106 AB Report *EC-Seal Products* 2014, para.5.101.

107 AB Report *EC-Asbestos* 2001, para.100.

108 WTO, *Thailand-Customs and Fiscal Measures on Cigarettes from the Philippines* AB Report 2011, WT/DS371/AB/R, para.128.

effects are really related to the foreign origin of the measure? The question whether to apply purportedly objective 'economic' or competition-oriented tests, on the one hand, and more subjective tests that look at the sincerity of the measure's regulatory purposes, on the other hand, has been a returning matter of debate.[109] This crucial issue will be further discussed in the following section on the inclusion of legitimate regulatory purposes in the national treatment analysis.

2.4.1.2.3 Aims and effects or the inclusion of regulatory purposes

Differentiation between like imported and domestic products does not necessarily mean that there is also discrimination. States might have legitimate reasons to impose differential treatment on domestic and imported products. Whether these reasons and regulatory purposes should be included in a national treatment analysis (or in a likeness analysis)[110] has been much debated over the years,[111] and has revived after the 2012 TBT cases. Should legitimate regulatory purposes be excluded from the Article III GATT analysis altogether and be left to Article XX; should they be considered when determining likeness; or rather when assessing treatment less favourable?

In the traditional technical analysis of likeness as discussed above, regulatory objectives are not taken into account and the focus is limited to the conditions of competition. The text of Article III, however, is hardly unequivocal on the correct analysis of likeness.[112] It has been argued that regulatory choices should be included into the analysis of origin-neutral measures under Article III.[113] This would bring a review of national law in line with the basic objective of the GATT – banning protectionism –, while leaving governments with the necessary policy space to address legitimate non-trade concerns. In the 1992 *US-Malt Beverages* case, the GATT panel considered policy objectives in determining likeness. According to the panel the words 'so as to afford

109 Tomer Broude and Philip I. Levy, 'Do You Mind If I Don't Smoke? Products, Purpose and Indeterminacy in *US-Measures Affecting The Production And Sale of Clove Cigarettes*' 2014, 13 World Trade Review 357, 359.

110 Regan (2002).

111 See for instance Hudec (1998); Michael Ming Du, 'The Rise of National Regulatory Autonomy in the GATT/WTO Regime' 2011, 14 Journal of International Economic Law 639; Flett (2013).

112 For an interesting analysis of the institutional constraints of the WTO, see Ming Du (2011). He argues that the WTO agreements are inherently vague and indeterminate due to the single undertaking-principle in the negotiations between very heterogeneous Members. The WTO tribunals interpret the texts with little democratic legitimacy, and their interpretations have differed over time. "Not only has the line been repeatedly drawn, shifted, and erased in academic discourse, the jurisprudence also echoed this uncertainty by evolving, reaffirming the link between the horizontal trade/non-trade debate and the vertical institutional struggle between Members and the WTO adjudicate bodies."(p.655)

113 Conrad(2011), 207; Regan (2002); Donald H. Regan, 'Further Thoughts on the Role of Regulatory Purpose under Article III of the General Agreement on Tariffs and Trade' 2003, 37 Journal of World Trade 737.

protection to domestic production' in Article III:1 do not prevent contracting parties from differentiating between different product categories for *bona fide* policy purposes, *in casu* public health concerns.[114] The panel's approach to look at the regulatory purpose and the effect on conditions of competition would become known as the 'aims and effects' test.[115] The GATT panel in *US-Taxes on Automobiles* further developed this test.[116] Rather than only looking at the competitive opportunities, the aim of a measure should be examined as well:

> 'A measure could be said to have the aim of affording protection if an analysis of the circumstances (…) demonstrated that a change in competitive opportunities in favor of domestic products was a *desired outcome* and not merely an incidental consequence of the pursuit of a legitimate policy goal.'[117]

The advantages of the test were that firstly, a violation was no longer based on a purely technical analysis of likeness but on the trade effects of a measure; and secondly, justification for legitimate regulatory purposes was no longer limited to Article XX, consisting of an exhaustive list of justification grounds and a strictly interpreted chapeau. This new approach was also in line with the one-stage test of violation of the new Standards Code and SPS Code (current Article 2.1-2.2 TBT and Article 2 SPS).[118]

However, the test also raised certain problems. Firstly, neither Article III:2 first sentence nor Article III:4 contain a textual reference to Article III:1, upon which the aim and effects-test was based.[119] Secondly, the burden of proof would become much heavier on the complainant, who would also have to show the aim of the measure.[120] Thirdly, Article XX could become redundant if the regulatory purpose is already taken into account under Article III.[121] The AB in *Japan-Alcoholic Beverages II* rejected the aims and effects-test by stressing that the intent of legislators or regulators was irrelevant when determining likeness.[122] The AB did recognize that an additional element had to be taken into account to discuss the 'protective application of a measure' and stated:

114 , *United States – Measures Affecting Alcoholic and Malt Beverages* GATT Panel 1992, DS23/R – 39S/206, para.5.25.
115 Hudec (1998), 627.
116 The report remains unadopted, as the EU (complainant) blocked the adoption of the report. The EU challenged the aim and effects-test in the first WTO case dealing with the issue, *Japan –Alcoholic Beverages II.*
117 , *United States – Taxes on Automobiles* GATT panel 1994, DS31/R, para.5.10.
118 Hudec (1998), 628.
119 WTO, *Japan – Taxes on Alcoholic Beverages II* panel report 1996, WT/DS8/R, para.6.16.
120 Ibid.
121 Ibid para.6.17.
122 WTO, *Japan – Taxes on Alcoholic Beverages II* AB 1996, WT/DS8/AB/R, p.27.

> '[w]e believe it is possible to examine objectively the underlying criteria used in a particular tax measure, its structure, and its overall application to ascertain whether it is applied in a way that affords protection to domestic products.'[123]

Although it is true that the aim of a measure may not be easily ascertained, nevertheless its protective application can most often be discerned from the design, the architecture, and the revealing structure of a measure. The distinction between the aim and effects-test and this new 'protective application' test was not very clear, and was very much based on the specifics of Article III:2. The AB later rejected any protective application-analysis with respect to Article III:4 in *EC-Bananas III*, stating that there is no reference to Article III:1 in Article III:4.[124] In *Chile-Alcoholic Beverages,* though the AB found the products to be 'directly competitive or substitutable products' and found dissimilar taxation, it then proceeded to assess whether the measure was 'applied so as to afford protection' to domestic production. The AB observed that the stated objectives of a government may be relevant in evaluating the design of a measure by noting:

> '[w]e consider that a measure's purposes, objectively manifested in the design, architecture and structure of the measure, *are* intensely pertinent to the task of evaluating whether or not that measure is applied so as to afford protection to domestic production.'[125]

In *EC-Asbestos* the AB seemed to indicate that rather than under likeness, regulatory purpose might be considered under 'treatment less favourable'. The AB seems to retreat from its previous position in *EC-Bananas* by stating that

> 'the term 'less favourable treatment' expresses the general principle in Article III:1. If there is 'less favourable treatment' of the group of like imported products, there is, conversely, protection of the group of like domestic products. However, a Member may draw distinctions between products which have been found to be 'like', without, for this reason alone, according to the group of like imported products less favourable treatment than that accorded to the group of like domestic products.'[126]

It seems logical that in evaluating regulatory distinctions, one should not only look at the effect on competition, but especially consider whether the distinc-

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123 Ibid p.29.
124 WTO, *European Communities – Regime for the Importation, Sale and Distribution of Bananas III* AB 1997, WT/DS27/AB/R, para.216.
125 WTO, *Canada-Certain Measures Affecting the Automotive Industry* AB Report 2000, WT/DS139/AB/R, para.62.
126 AB Report *EC-Asbestos* 2001, para.100.

tion is related to the origin of the products. In *Dominican Republic-Cigarettes*, the AB stated that

> 'the existence of a detrimental effect on a given imported product resulting from a measure does not necessarily imply that this measure accords less favorable treatment to imports *if the detrimental effect is explained by factors or circumstances unrelated to the foreign origin of the product*.'[127]

Thus, even if a measure has a detrimental effect on imports as opposed to like domestic products, that effect alone may not be sufficient proof of less favourable treatment: rather, a non-protectionist objective may demonstrate that the measure is not *de facto* discriminatory based on origin.[128] In *EC-Biotech* the panel assumed biotech and non-biotech products to be like, but found that the EC treated all biotech products alike irrespective of origin, and equally treated all non-biotech products alike irrespective of origin. As Argentina had 'not adduced argument and evidence sufficient to raise a presumption that the alleged less favourable treatment is explained by the foreign origin of the relevant biotech products', the panel was unable to find a national treatment violation.[129]

Pauwelyn, who argues that the focal point of a national treatment analysis should lie with determining whether or not imported products are discriminated based on their origin, supports this approach. *De jure* discrimination based on origin is easily found (and may still be justified under exceptions), but the important question under Article III is how to define *de facto* discrimination?[130] According to Pauwelyn, the test for *de facto* discrimination for measures that seem origin-neutral should be seen as a weighing exercising including consideration of both the objective purpose of the regulation and its effects.[131] He argues that rather than focusing on likeness (criteria upon which it is permissible to distinguish) panels and the AB should focus on the one *impermissible* feature, which is national origin.[132] Thus if a national

127 WTO, *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes* AB 2005, WT/DS302/AB/R, 96. In that case, both importers and domestic producers of cigarettes had to pay a bond of five million pesos, which imposed a higher burden on an imported cigarette as compared to a domestic cigarette, because importers sell fewer cigarettes in the Dominican Republic than domestic producers. The AB found that the detrimental effect was thus explained by factors such as market share, but was not related to the foreign origin of the product, and thus no treatment less favourable under Article III:4 could be established.

128 Joost Pauwelyn, 'Comment: The Unbearable Lightness of Likeness' in Marion Panizzon, Nicole Pohl and Pierre Sauvé (eds), *GATS and the Regulation of International Trade in Services* (Cambridge University Press 2008) 365.

129 Panel report *EC-Biotech* 2006, para.7.2514.

130 See also for an overview of earlier WTO jurisprudence, Ehring (2002).

131 Pauwelyn(2008), 358.

132 Ibid 363.

measure distinguishes between products based on genuine features that are not origin-based (such as physical characteristics, consumer tastes or legitimate objectives such as environmental protection), the measure would be permissible.[133]

In the recent TBT case law, – where Articles 2.1 and 2.2 TBT were interpreted, relying extensively on the jurisprudence of Article III GATT -,[134] regulatory objectives were considered for the analysis of less favourable treatment. In both *US-Clove Cigarettes*[135] and *US-Tuna II,*[136] the AB explicitly considered the policy objectives of the measures in determining less favourable treatment under Article 2.1 TBT (the national treatment provision). In *US-COOL*[137] the policy objective was only considered shortly under Article 2.1 TBT.[138]

US-Clove Cigarettes concerned a US measure prohibiting cigarettes with characterizing flavour, other than tobacco or menthol. Indonesia, the biggest exporter of clove cigarettes claimed that the measure was in breach of the TBT as it accorded treatment less favourable to like imported products. Clove cigarettes were found to be like domestic cigarettes. The AB stated with regard to the less favourable treatment analysis under Article 2.1 TBT that

> '[a] panel must further analyze whether the detrimental impact on imports stems exclusively from a legitimate regulatory distinction rather than reflecting discrimination against the group of imported products. In making this determination, a panel must carefully scrutinize the particular circumstances of the case, that is, the design, architecture, revealing structure, operation, and application of the technical regulation at issue, and, in particular, whether that technical regulation is even-handed, in order to determine whether it discriminates against the group of imported products.'[139]

133 Ibid.

134 Article 2.1 TBT contains the national treatment and MFN obligation, requiring no less favourable treatment for imported products than that accorded to domestic or other imported like products). Article 2.2 TBT ensures that regulations are not more trade restrictive than necessary in order to fulfill a legitimate objective (non-exhaustive list). Protection of the environment is one of the grounds listed.

135 WTO, *United States – Measures Affecting the Production and Sale of Clove Cigarettes* AB Report 2012, WT/DS406/AB/R.

136 WTO, United States – Measures Concerning the Importation, Marketing and Sale of Tuna and Tuna Products AB Report 2012, WT/DS381/AB/R.

137 WTO, United States-Certain Country of Origin Labelling (COOL) Requirements AB Report 2012, WT/DS384/AB/R.

138 The AB's methodology has been criticized for its 'lock, stock and barrel' export of GATT solutions into the TBT, see among others Petros C. Mavroidis, 'Driftin' too far from shore – Why the Test for Compliance with the TBT Agreement Developed by the WTO Appellate Body is Wrong, and What Should the AB Have Done Instead' 2013, 12 World Trade Review 509.

139 AB Report *US-Clove Cigarettes* 2012, para.182. This was confirmed by the AB in AB Report *US-COOL* 2012, para.271.

Although considering the objective of reducing youth smoking, the AB held that this objective could not justify the measure, as menthol cigarettes would equally increase the attractiveness of tobacco to youth.[140]

In *US-Tuna II*, the US established criteria according to which tuna products sold in the US could carry a 'dolphin-safe' label. The US distinguished between the area where tuna was harvested (inside or outside the Eastern Tropical Pacific Ocean) and the technique used in tuna fishing (with or without the use of special nets). Mexico claimed both a national treatment and a most-favoured nation violation under Article 2.1 TBT. The AB found that the US measure treated Mexican tuna *de facto* less favourably than US tuna and recalled that the treatment less favourable analysis should include whether the disparate impact of a measure stemmed exclusively from a legitimate regulatory distinction.[141] That was not (fully) the case here.[142]

A US measure imposing country of origin labeling (COOL) requirements on livestock of domestic, foreign and mixed origin was at issue in *US-COOL*. After having found a detrimental impact on Canadian and Mexican livestock, the AB proceeded to check under Article 2.1 TBT whether the measure was applied in an even-handed manner. The specifics of the COOL measure made compliance with its requirements least costly for producers if they relied exclusively on domestic livestock, and in that way the measure had a detrimental impact on the competitive opportunities of imported livestock. The expensive recordkeeping and verification requirements regarding the countries where the livestock were born, raised and slaughtered, were not necessarily conveyed to consumers through the prescribed labels, and thus the detrimental impact did not stem exclusively from a legitimate regulatory distinction (the objective of informing consumers).[143] Under Article 2.2 TBT the AB agreed with the panel that the objective was legitimate, however, it did not complete the analysis on the necessity of the measure due to a lack of relevant factual findings by the panel and insufficient undisputed facts on the record.[144]

In the light of these recent TBT cases, it is being proposed to include national regulatory autonomy in the analysis under Article III GATT as well, rather than limit it to Article XX, so as to ensure a consistent and coherent interpretation and application of both agreements.[145] Should the TBT approach of considering whether a detrimental impact is attributable to a legitimate regulatory distinction apply *mutatis mutandis* to Article III:4 GATT? As Flett noted, 'respect for regulatory autonomy should not be rendered ineffective by an excessively

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140 AB Report *US-Clove Cigarettes* 2012, para.225.
141 AB Report *US-Tuna II* 2012, para.216.
142 Ibid paras.251; 288.
143 AB Report *US-COOL* 2012, 349.
144 Ibid 491. See also for a further discussion of the case Petros C. Mavroidis and Kamal Saggi, 'What Is Not So Cool About *US-Cool* Regulations? A Critical Analysis Of The Appellate Body's Rulings on *US-Cool*' 2014, 13 World Trade Review 299.
145 Flett (2013), 27; Crowley and Howse (2014), 322; Broude and Levy (2014), 391.

rigid interpretation and application of Article III:4'.[146] When permitting a modification of the conditions of competition if it stems from a legitimate regulatory distinction under Article 2.1 TBT, the AB referred to the 'context' of Article 2.1 requiring such interpretation.[147] Such support could also be found in the context of Article III:4 GATT – specifically as supplied by Article III:1.[148] Even though in contrast to the TBT, the GATT contains a general exceptions clause, according to Crowley and Howse, there is

> 'no reason why a responding Member could not argue under Article III GATT that, despite features of the design and structure of its measure appearing to be non-evenhanded in their impact on competing imported products, these features can in fact be fully explained by a legitimate regulatory distinction.'[149]

Including regulatory distinctions in the analysis of Article III GATT would allow WTO Members to go beyond the closed list of exception grounds in Article XX GATT. The list of Article XX was drafted in 1947, based on concerns of that time. The TBT already contains an open list of legitimate objectives, which allows a reflection of current circumstances. Including regulatory purpose in the analysis of Article III GATT does not imply Article XX would become void, as there is considerable overlap between both provisions.[150] Any testing of all the facts under Article III would imply the suitability and the necessity of a measure, a proportionality test comparable to Article XX.[151] This 'new' aims and effects-test would broaden the space for regulatory autonomy for facially neutral measures with legitimate objectives. Any explicit justification grounds (for sure for *de jure* discrimination, and for doubtful cases of *de facto* discrimination) would still be dealt with under Article XX. The burden of proof would lie with the complainant to show that the differential treatment under Article

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146 Flett (2013), 53.

147 That context includes Article 2.2 TBT as well as the preamble of the TBT Agreement. AB Report *US-Tuna II* 2012, para.213; WTO, *United States – Measures Affecting the Production and Sale of Clove Cigarettes* AB Report 2012, AB/DS406/AB/R, para.182; AB Report *US-COOL* 2012, para.240.

148 William J. Davey and Keith E. Maskus, '*Thailand-Cigarettes (Philippines)*: A More Serious Role for the 'Less Favourable Treatment' Standard of Article III:4' 2013, 12 World Trade Review 163, 180.

149 Crowley and Howse (2014), 332.

150 The AB commented on this point in AB Report *EC-Asbestos* 2001, para.115., noting that considering evidence relating to health risks under Article III:4 do not render Article XX redundant; The AB stated that 'the fact that that interpretation of Article III:4 implies a less frequent recourse to Article XX(b) does not deprive the exception in Article XX(b) of *effet utile*'.

151 See Weihuan Zhou, '*US-Clove Cigarettes* and *US-Tuna II (Mexico)*: Implications for the Role of Regulatory Purpose under Article III:4 of the GATT' 2012, 15 Journal of International Economic Law 1075.; Federico Ortino, 'From 'Non-Discrimination' to 'Reasonableness': A Paradigm Shift in International Economic Law?' 2004, 01/05 Jean Monnet Working Paper NYU School of Law.

III is based on the foreign origin of the products. The respondent will need to demonstrate the non-protectionist purpose of the measure, and show a genuine link between that purpose and the measure. When a distinction originates from a legitimate regulatory objective, a measure would not need to seek justification under Article XX, as no violation would be found in the first place. The hurdles of Article XX have proven extremely hard to overcome, even for non-protectionist measures. As has been noted, this

> 'norm-justification dichotomy between Article III and Article XX raises a troubling question of constitutional identity, the way a society wants to understand its internal hierarchy of values. There is no reason to believe that liberalized trade should prevail over the competing values, such as human health and safety and protection of the environment.'[152]

Despite strong arguments to be made in favour of adopting a similar TBT test for consideration of legitimate regulatory purposes under Article III GATT, it seems that in *EC-Seal Products* the AB rejected such approach, by distinguishing between the justification provisions under the TBT and the GATT.[153] The AB pointed to Article XX GATT to support its position that the balance under Article 2 TBT between right to regulate and non-discrimination requires an examination of regulatory purpose, whereas under the GATT Article XX serves to counterweigh the non-discrimination obligations. According to the AB, 'a panel is not required to examine whether the detrimental impact of a measure on competitive opportunities for like imported products stems exclusively from a legitimate regulatory distinction'.[154] Note the AB's particular wording of 'not required to' rather than 'should not' or 'cannot'. The AB indicated that it is sufficient to establish a distinction in the competitive opportunities to the detriment of imported products, for which it does not matter whether that distinction is protectionist or whether it stems from a legitimate regulatory distinction. However, the AB did not say that *if* indeed such distinction stems from a legitimate regulatory purpose, that that would be irrelevant. Seen the previous turns the AB has taken in this matter, further confirmation of this approach is to be awaited.[155] In the recent *Argentina-Financial Services* GATS case, the panel did rely on the TBT case law to include regulatory distinctions

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152 Ming Du (2011), 671.

153 AB Report *EC-Seal Products* 2014; Michael Ming Du, ''Treatment No Less Favourable' and the Future of National Treatment Obligation in GATT Article III:4 after *EC-Seal Products*' 2016, 15 World Trade Review 139.

154 AB Report *EC-Seal Products* 2014, para.5.117.

155 See also Ming Du (2016), 155.

to determine likeness under Article II:1 GATS,[156] however, that approach was rejected by the AB.[157]

If regulatory distinctions were included in the analysis of Article III, the extraterritorial effect of measures would also need to be taken into account in that analysis. In light of the AB's findings in *EC-Seal Products*, the main analysis will focus on assessing extraterritoriality within the framework of Article XX. Chapter 7, introducing the extraterritoriality decision tree, will in addition to Article XX also address the application of the tree to Article III GATT.

2.4.2 The justification: Article XX GATT

If a particular npr-PPM is found to violate either Article III or Article XI, the question arises whether that violation could still be justified under the general exceptions of Article XX GATT. In order to protect and promote societal values and interests, governments frequently adopt legislation or take measures that might constitute barriers to trade, and might hence be inconsistent with the non-discrimination principles or other rules of WTO law. WTO law provides for a set of exceptions to reconcile trade liberalization with the pursuit of other societal interests. While only the general exceptions of Article XX GATT will be discussed here, the WTO covered agreements also offer security exceptions,[158] economic emergency exceptions,[159] regional integration exceptions,[160] balance of payment exceptions[161] and economic development exceptions,[162] the discussion of which is of less relevance to this thesis on environmental trade measures with an extraterritorial effect.

Article XX of the GATT 1994, entitled 'General Exceptions', reads:[163]

> 'Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on inter-

156 WTO, Panel Report, *Argentina-Measures Relating to Trade in Goods and Services,* 2015, WT/DS453/R, para.7.176-179.

157 WTO, AB Report, *Argentina-Measures Relating to Trade in Goods and Services,* 2016, WT/DS453/AB/R, para. 6.127.

158 Article XXI GATT 1994 and Article XIV *bis* GATS.

159 Article XIX GATT 1994 and the *Agreement on Safeguards.*

160 Article XXIV GATT 1994 and Article V GATS.

161 Articles XII and XVIII:b GATT 1994 and Article XII GATS.

162 Article XVIII:a GATT 1994 and the 'Enabling Clause'.

163 Paragraphs (c), (h), (i) and (j) omitted by author. These paragraphs relate to trade in gold and silver; obligations under international commodities agreements; efforts to ensure essential quantities of materials to a domestic processing industry; and products in general or local short supply. They have been of less importance in international trade law and practice, and are furthermore of little relevance to this study.

> national 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;
> (*c*) …
> (*d*) necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement, including those relating to customs enforcement, the enforcement of monopolies operated under paragraph 4 of Article II and Article XVII, the protection of patents, trade marks and copyrights, and the prevention of deceptive practices;
> (*e*) relating to the products of prison labour;
> (*f*) imposed for the protection of national treasures of artistic, historic or archaeological value;
> (*g*) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption;'

Article XX sets out an exhaustive list of exceptions, which can be invoked by a Member when a measure has been found to be inconsistent with one of the GATT provisions. The GATT panel in *US-Section 337* noted that the central phrase in the introductory clause of Article XX is that 'nothing in this Agreement shall be construed to prevent the adoption or enforcement by any Member of measures…'.[164] The AB has stated in *US-Gasoline* and *US-Shrimp* that in the interpretation of Article XX balance needs to be sought between Members' rights to invoke exceptions as well as their duty to respect other Members' WTO rights and to liberalize trade. Such balance must be *bona fide*, or reasonable.[165] The AB stated that the relationship between the commitments and the exceptions can be given meaning only 'on a case-to-case basis, by careful scrutiny of the factual and legal context in a given dispute'.[166]

In order for Article XX to be successfully invoked, the conditions of said article have to be fulfilled through a two-tier test: first, the conditions of the paragraphs must be complied with; and second, the requirements of the introductory clause, referred to as the chapeau. While the panel in *US-Shrimp* suggested to first check the conditions of the *chapeau* of Article XX, seen its conclusive nature, before going into the paragraphs of the article, the AB firmly rejected this approach. According to the AB, panels should first examine whether a measure is justified under a particular paragraph before moving to an examination of consistency with the chapeau,[167] as the chapeau deals

164 , *US-Section 337* GATT Panel Report, para.5.9.
165 AB Report *US-Shrimp* 1998, para. 128.
166 AB Report *US-Gasoline* 1996, 16.; For an interesting discussion on the difficulties of this balancing act under Article XX *see* Christopher Doyle, 'Gimme Shelter: The "Necessary" Element of GATT Article XX in the Context of the *China-Audiovisual Products* Case' 2011, 29 Boston University International Law Journal 143.
167 AB Report *US-Shrimp* 1998, paras 116ff.

with the *application* of a measure rather than with the design of the measure as such. The panel in *Brazil-Retreated Tyres* described the distinction between the two elements of the test in the following way:

> '[In its analysis under Article XX(b)] [t]he panel will not … examine … the manner in which the measure is implemented in practice […]. These elements will, however, be relevant to later parts of the panel's assessment, especially under the chapeau of Article XX, where the focus will be, by contrast, primarily on the manner in which the measure is applied.'[168]

The focus of this research is on the extraterritorial nature of trade measures and thus also on whether and to what extent Article XX GATT precludes extraterritorial measures. Can Article XX only be invoked to protect concerns located within the territory of the imposing state? What if the measure aims at protecting 'common concerns' which are of importance to the entire international community, or concerns located abroad which create domestic moral concerns? Article XX does not contain an explicit jurisdictional limitation, but whether there is an implied jurisdiction limitation will be discussed in greater detail in chapter 3. In this section an overview will be given of the other relevant elements of Article XX GATT with regard to environmental disputes.

2.4.2.1 *Article XX(b) and (g) GATT*

The paragraphs of Article XX lay down specific grounds of justification for measures that are otherwise inconsistent with provisions of the GATT. The grounds range from human, animal or plant life or health, to public morals, and protection of national treasures of artistic, historic or archaeological value. Of most relevance to this study are the two paragraphs which can be used for environmental protection purposes, namely paragraphs (b) and (g).

Article XX(b) concerns measures which are 'necessary to protect human, animal or plant life or health'. The paragraph sets out a two-tier test to determine whether a measure is provisionally justified under this provision. The panel in *US-Gasoline* held that first, the policy objective pursued by the measure at issue must be the protection of life or health of humans, animals or plants; and that second, the measure must be necessary to fulfill that policy objective.[169] Regarding the first element, the panel in *EC-Tariff Preferences* noted that not only the express provisions of legislation or a measure are at issue, but also the design, architecture and structure of that measure.[170] In *Brazil-Retreaded Tyres*, Article XX(b) was invoked for environmental policy measures.

168 WTO, *Brazil – Measures Affecting Import of Retreaded Tyres* Panel Report 2007, WT/DS332/R, para. 7.107.

169 Panel Report *US-Gasoline* 1996, para. 6.20. For a more recent application of this test, see Panel report *EC-Biotech* 2006, para.7.179.; Panel Report *Brazil-Retreaded Tyres* 2007, para.7.40.

170 , *EC-Tariff Preferences* Panel Report, para. 7.200.

The case dealt with an import ban on retreaded tyres, whereby Brazil argued that waste tyres create perfect breeding grounds for disease carrying mosquitos, but also that the accumulation of waste tyres creates a risk of tyre fires and hence toxic leaching of chemicals and hazardous substances. The panel noted thereby that a party invoking environmental policy measures under Article XX(b) 'has to establish the existence not just of risks to "the environment" generally, but specifically of risks to animal or plant life or health'.[171] Hence not all environmental policy measures would fall within the scope of application of Article XX(b) GATT, even though it is likely that most environmental measures will have an impact on animal or plant life or health.[172]

The second element of Article XX(b), the 'necessity' requirement, is more problematic. The panel noted in *Thailand-Cigarettes* that the measure by Thailand

> 'could be considered 'necessary' in terms of Article XX(b) only if there were no alternative measure consistent with the GATT, or less inconsistent with it, which Thailand could reasonably be expected to employ to achieve its health policy objectives.'[173]

The alternative measure must be *as effective* in achieving the policy objective pursued as the measure at issue. The panel in *US-Gasoline* made an important classification as to the requirement of 'necessity' under Article XX(b), stating that it is not the necessity of the policy objective, but the necessity of the disputed measure to *achieve* that objective.[174] The AB further clarified the 'necessity' test in *EC-Asbestos* by stating first, that the level of protection can only be determined by the Member itself and that this cannot be challenged by other WTO Members.[175] Second, the AB reiterated from earlier jurisprudence that 'necessary' refers to 'no alternative to the measure at issue that the Member could reasonably be expected to employ'.[176] In order to determine reasonableness, factors such as difficulty of implementation have to be taken into account. In later disputes it was added that the less restrictive the impact of the measure at issue is on international trade, the more easily the measure may be considered 'necessary'.[177] Third, the AB specified that the GATT-con-

171 Panel Report *Brazil-Retreaded Tyres* 2007, para. 7.46.
172 Peter Van den Bossche and Zdouc Werner, *The Law and Policy of the World Trade Organization: Text, Cases and Materials.* (3d edn, Cambridge University Press 2008) 555.
173 WTO, *Thailand-Customs and Fiscal Measures on Cigarettes from the Philippines* Panel Report 2010, WT/DS371/R, paras. 73 and 75.
174 Panel Report *US-Gasoline* 1996, para. 6.22.
175 AB Report *EC-Asbestos* 2001, para. 168.
176 Ibid para. 172.
177 Panel Report *Brazil-Retreaded Tyres* 2007, para. 7.104.

sistency of alternative measures leads to the question whether an alternative measure that would achieve the same end would be less trade restrictive.[178]

Article XX(g) concerns measures 'relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption'. Article XX(g) sets outs a three-tier test, requiring that a measure first, relates to the *conservation of exhaustible natural resources*; second, *relates* to such conservation; and third, must be made effective in conjunction with domestic restrictions. The first element of exhaustible natural resources has been interpreted broadly, in the sense that it encompasses both biological resources as well as non-living resources,[179] such as clean air.[180] The term 'relating to' has been held to cover a wider scope than terms used in other paragraphs such as 'necessary to' and 'essential to'. In *Canada-Herring and Salmon,* the GATT panel found that a measure was '*relating to* the conservation of exhaustible resources' if it was '*primarily aimed at*' this policy goal.[181] The consequent test resembled the necessity test from paragraph (b). In *US-Shrimp,* the AB interpreted 'relating to' as designating a 'close and genuine relationship of ends and means',[182] i.e. between the measure and the policy objective. The third element of Article XX(g) is a requirement of 'even-handedness' in the imposition of restrictions on imported and domestic products,[183] which does not require 'identical treatment of domestic and imported products', however.[184]

In *EC-Seal Products,* the EU invoked Article XX(a) on public morals to justify its seals regime. The EU relied on public morals expressed by EU citizens on inhumane killing methods of seals to impose an import ban on seal products. The EU equally invoked Article XX(b) but did not make any substantive arguments.[185] It is clear that there can be substantive overlap between Article XX(a) and other substantive exception grounds, as the scope of moral issues can arguably be very broad.[186] It can be difficult to distinguish moral from environmental concerns: for instance, the protection of an animal species threatened with extinction can have a direct environmental impact on country A, but can be a moral concern to the not directly affected country B. The relationship between the public morals exception and the environmental

178 AB Report *EC-Asbestos* 2001, para.172.
179 AB Report *US-Shrimp* 1998, para. 131.
180 AB Report *US-Gasoline* 1996.
181 GATT, *Canada – Measures Affecting Exports of Unprocessed Herring and Salmon* GATT Panel Report 1988, BISD 35S/98, para. 4.6.
182 AB Report *US-Shrimp* 1998, para 136.
183 Van den Bossche and Werner(2008), 637. See also WTO, *China-Measures Related to the Exportation of Various Raw Materials* AB Report 2012, WT/DS394/AB/R, para.357.
184 AB Report *US-Gasoline* 1996, p.20.
185 WTO, Panel Report, *EC-Seal Products,* 2013, para.7.640.
186 Steve Charnovitz, "The Moral Exception in Trade Policy", *Virginia Journal of International Law* 38(1998): 689.

exceptions will be discussed in greater detail in chapter 7, in the context of the extraterritoriality decision tree.

2.4.2.2 The chapeau

Next to meeting the requirements of one of the paragraphs of Article XX, in order for a measure to be justified, the requirements of the *chapeau* of Article XX have to be met as well. The *chapeau* has been highly relevant in dispute settlement practice as for several controversial decisions the *chapeau* was the stumbling block.[187] The purpose of the *chapeau* is to protect the legal rights of the complaining party, ensuring that no abuse is made of the legal rights of the defendant to justify trade-restrictive measures,[188] and thus to maintain a balance between rights and obligations of WTO Members.[189] In assessing the application of the measure, one must examine the manner in which the measure is implemented in practice, how other elements extraneous to the measure could affect the measure's ability to perform its function.[190] In *EC-Seal Products*, empirical evidence was lacking as to whether the measure met the *chapeau*'s conditions. The AB looked at the 'actual or expected application' of the measure, based on the 'design, architecture, and revealing structure' of the measure,[191] elements which are usually considered in the context of the paragraphs.[192]

The *chapeau* of Article XX prohibits 'arbitrary or unjustifiable discrimination between countries where the same conditions prevail' and 'disguised restrictions on international trade'. These concepts may be read side-by-side and impart meaning to one another.[193] WTO Members must take into account the different conditions that may occur in the territories of other Members.[194] A measure needs to be sufficiently flexible and should consider similar measures enacted by other Members, which can be comparable in effectiveness, to address the same policy objectives.[195] In *US-Shrimp (Article 21.5 Malaysia)*, the AB added that the *chapeau* entails a good faith obligation, whereby WTO Members must make serious efforts to negotiate concerns before resorting to

187 In both *US-Shrimp* and *US-Gasoline* for instance the measures at issue were found by the AB to have been applied in a manner which constituted arbitrary and unjustifiable discrimination.
188 AB Report *US-Gasoline* 1996, p.20.
189 AB Report *US-Shrimp* 1998, para. 156.
190 WTO, *Brazil – Measures Affecting Import of Retreaded Tyres* AB Report 2007, WT/DS332/AB/R, para.7.107.
191 AB Report *EC-Seal Products* 2014, para.5.302.
192 Lorand Bartels, 'The Chapeau of the General Exceptions in the WTO GATT and GATS Agreements: A Reconstruction' 2015, 109 American Journal of International Law 95, 101.
193 AB Report *US-Gasoline* 1996, p.23.
194 AB Report *US-Shrimp* 1998, para. 164.
195 Ibid para. 177.

trade restrictive measures.[196] With regard to 'no disguised restriction on trade', even if a measure does not discriminate, the measure shall not be protectionist in nature. It is not clear whether a measure could be justified if it combined legitimate and illegitimate purposes. Should any illegitimate purpose, even when minor compared to the legitimate purpose, suffice to fail a defense under Article XX? In the example of measures that seek to achieve environmental protection, but that at the same time aim at leveling the playing field and protecting domestic industry, this condition may yet prove to be an important aspect of the *chapeau*.[197]

2.4.3 The TBT Agreement

The TBT Agreement has also been ground of debate with regard to PPMs. In particular, it is still unresolved whether npr-PPMs could fall within the scope of the Agreement, or whether it is limited to pr-PPMs. In GATT law, non-discriminatory policies cannot be challenged: in principle countries can do as they please as long as they do not unduly restrict import or discriminate imports as against domestic products. Under the TBT, technical barriers to trade are disciplined (in particular, they must be necessary or least-trade restrictive) even if they do not discriminate against imports.[198] The TBT and GATT seem be cumulatively applicable rather than mutually exclusive. In *EC-Asbestos* the AB observed that the TBT furthers the objectives of GATT

> 'through a specialized legal regime that applies solely to a limited class of measures. For these measures, the TBT Agreement imposes obligations on Members that seem to be *different from*, and *additional to*, the obligations imposed on Members under the GATT 1994 (emphasis added).'[199]

The TBT covers technical regulations (mandatory compliance), standards (voluntary compliance) and conformity assessment procedures.[200] All technical regulations are covered by the TBT, other than sanitary or phytosanitary measures as defined in the SPS Agreement.[201] In order to determine whether the TBT is at all relevant to the discussion of environmental npr-PPMs, the scope

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196 WTO, *United States – Import Prohibition of Certain Shrimp and Shrimp Products, Recourse to Article 21.5 of the DSU by Malaysia* AB Report 2001, WT/DS58/AB/RW, paras. 115.

197 Bartels (2015), 123.

198 See below for a discussion of Article 2.2 TBT. See also Pauwelyn (2004), 580.

199 AB Report *EC-Asbestos* 2001, para. 80.

200 Article 1.6 TBT. Mandatory technical regulations are developed and implemented by governments, whereas standards as voluntary requirements are most often developed and implemented by private bodies. See Rotherham(2007), 179.

201 See the definition of sanitary and phytosanitary measures in Annex A to the SPS Agreement.

of the agreement must be assessed first. The term 'technical regulations' has been defined in Annex 1.1, referring to

> '[A document] which lays down product characteristics or *their related processes and production methods*… It may also include or deal exclusively with terminology, symbols, packaging, marking or labelling requirements *as they apply to a product, process or production method*.' (emphasis added)

Annex 1.1 refers to production methods, but adds that they must be 'related' to product characteristics, when not concerning 'terminology, symbols, packaging, marking or labelling requirements'. In EC-*Seal Products*, the AB examined the meaning of 'product characteristics' and found that characteristics include objectively definable 'features', 'qualities', 'attributes' or other 'distinguishing marks' of a product.[202] The AB then found 'related' in the first sentence of Annex 1.1 to refer to these characteristics: the process or production method must thus be related to the product characteristics, or must in other words have a sufficient nexus to the characteristics of the product.[203] It is unclear what is meant with a 'sufficient nexus' in this context. If one were to argue that 'related' means that the measure must have an impact on 'objectively definable product characteristics', then npr-PPMs that do not affect the physical characteristics of a product, will not be considered 'related' and thus fall outside the scope of the TBT. If a sufficient nexus could be understood as *any* link to the 'characteristics', then certain npr-PPMs could be considered related: for instance, the fact that shrimp was harvested in a turtle-friendly way, could be 'related' to the end product through its moral or ethical advantage. It remains unclear, though, what the AB could have had in mind. Any production process has an automatic 'nexus' to the product, but when is this sufficient? If assessing that nexus would imply a consideration of the objective of the PPM (e.g. an environmental objective, ethical characteristics), then how to distinguish the test from regulatory purpose or a necessity test?

In EC-*Seal Products* the AB found that the ban on seals products imposed a characteristic on products 'by providing that they may not contain seal',[204] however, the exceptions to the EU seal regime (the indigenous communities exception, the marine resources management exception and the travellers exception) did not. According to the AB, there is no basis in the text of Annex 1.1 to 'suggest that the identity of the hunter, the type of hunt, or the purpose of the hunt could be viewed as product characteristics'.[205] As a measure must be examined as a whole, including prohibitive and permissive elements, and the main features of the EU seal regime were the exceptions rather than the

202 AB Report *EC-Seal Products* 2014, para.5.11.
203 Ibid para.5.12.
204 Ibid para.5.39.
205 Ibid para.5.45.

criteria relating to the manner in which seal is killed, the AB considered the EU seal regime to not lay down product characteristics and thus not to constitute a technical regulation.[206] Whether these exceptions could be considered PPMs *related to* product characteristics was unfortunately left unanswered by the AB. As the panel had not examined the issue in its report and as the parties had not submitted sufficient argumentation, the AB did not rule on this point. The AB did note that 'the line between PPMs that fall, and those that do not fall, within the scope of the TBT Agreement raises important systemic issues'.[207] The contours of npr-PPMs within the TBT have thus not yet been determined. If one were to argue that a npr-PPM were to have a sufficient nexus with the product characteristics, despite the lack of physical impact, that measure would then be considered a technical regulation and fall within the scope of the TBT.

The second sentence of Annex 1.1, referring to among others labelling requirements, only refers to PPMs in general, without distinguishing between related and non-related PPMs. It can thus be accepted that for those requirements (labelling, packaging, symbols), it is irrelevant to what extent the production process impacts on the physical characteristics of final product in order to fall within the scope of the TBT Agreement.[208] Labelling requirements could be seen as a special regime, exceptionally bringing npr-PPMs within the scope of the TBT. As suggested by Marceau, the regime of labelling requirements can be more flexible as such measures do not completely restrict trade but essentially provide information.[209] By informing consumers, labels can be a first tool to distinguish between products based on their production methods.[210] Whether or not the labelling measure in question is inconsistent with the agreement then needs to be determined through an analysis of the substantive TBT obligations.

Article 2 TBT, governing technical regulations, contains the most important substantive requirements in the TBT Agreement with regard to PPMs. It includes the national treatment and MFN obligation in Article 2.1 TBT and the additional obligation to ensure that regulations are not more trade restrictive than necessary to fulfill a legitimate objective (non-exhaustive list) in Article 2.2 TBT. Article 2.1 TBT follows a similar approach to Article III GATT with regard

206 Ibid para.5.58.

207 Ibid para.5.69.

208 See for instance *US-Tuna II* on dolphin-safe labels for tuna products. AB Report *US-Tuna II* 2012; Philip I. Levy and Donald Regan, '*EC-Seal Products*: Seals and Sensibilities (TBT Aspects of the Panel and Appellate Body Reports)' 2015, 14 World Trade Review 337, 350; Norpoth (2013), 580.; Vranes(2009), 339.; Marceau and Trachtman (2002), 861.

209 Gabrielle Marceau, 'A Comment on the Appellate Body Report in *EC-Seal Products* in the Context of the Trade and Environment Debate' 2014, 23 RECIEL 318, 327.

210 See Laurens Ankersmit and Jessica Lawrence, 'The Future of Environmental Labelling: *US-Tuna II* and the Scope of the TBT' 2012, 39 Legal Issues of Economic Integration 127, 136.; Enrico Partiti, 'The Appellate Body Report in *US-Tuna II* and Its Impact on Eco-Labelling and Standardization' 2013, 40 Legal Issues of Economic Integration 73, 79.

to the national treatment obligation. It must be determined firstly, whether the relevant products are like, i.e. in a sufficiently strong competitive relationship.[211] If not, are imported products treated less favourably compared to domestic products, and does that impact stem exclusively from a 'legitimate regulatory distinction'?[212] The context of Article 2.1 TBT, among which Article 2.2 TBT and the preamble of the TBT Agreement, supports a finding that technical regulations may pursue legitimate objectives when they are not applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination.[213] When ascertaining whether a technical regulation modifies the conditions of competition to demonstrate less favourable treatment, a panel must analyze whether the detrimental impact on the imported products stems exclusively from a legitimate regulatory distinction.[214] Article 2.2 TBT establishes an additional obligation that technical regulations shall not be more trade-restrictive than necessary to fulfil a legitimate objective. Article 2.2 TBT resembles the sub-paragraphs of Article XX GATT, with a (non-exhaustive in case of Article 2.2) list of objectives, as well as a necessity test.[215] Technical regulations have to conform to the requirements of Article 2.2 though, irrespective of whether a measure was found to be inconsistent with Article 2.1 TBT: Article 2.2 is thus not a justification provision for inconsistencies found with other substantive obligations. This distinction between Article XX GATT and Article 2.2 TBT may have important consequences for the burden of proof: the respondent bears the burden under Article XX GATT to justify its measures, whereas the complainant likely bears the burden under Article 2.2 TBT.[216] The TBT does not contain a general exceptions clause.

Thus, in summary, a textual analysis of Annex 1.1 TBT does not seem to support the inclusion of npr-PPMs within the scope of the TBT Agreement, unless they concern requirements such as labelling or packaging that serve to inform consumers. However, the AB in *EC-Seal Products* created an opening for npr-PPMs by referring to a 'sufficient nexus' between production and end product, without clarifying whether such nexus could only consist of a physical impact. If npr-PPMs would fall within the scope of the TBT Agreement, the measure needs to be consistent with Article 2.1 and 2.2 TBT.

211 AB Report *US-Clove Cigarettes* 2012, para.120.
212 Ibid para.271.
213 AB Report *US-Tuna II* 2012, para.213; AB Report *US-Clove Cigarettes* 2012, para.182; AB Report *US-COOL* 2012, para.240.
214 AB Report *US-Clove Cigarettes* 2012, para.182.
215 AB Report *US-Tuna II* 2012, para.322. As under Article XX GATT, environmental concerns are explicitly mentioned in Article 2.2 TBT.
216 Andrew Green, 'Climate Change, Regulatory Policy and the WTO: How Constraining are Trade Rules?' 2005, 8 Journal of International Economic Law 143, 174.

2.5 Conclusion

Throughout the years, environmental protection has received more and more attention in the WTO and is now recognized as a real and legitimate objective within international trade. The object of this study is to determine the degree of acceptance of trade measures that aim at environmental concerns located outside the territory of the regulating state through regulating the production process, and in particular npr-PPMs that have no impact on the physical characteristics of the product. Whereas chapter 3 will focus on the extraterritorial nature of PPMs, this chapter has outlined the legal challenges for npr-PPMs under the GATT.

The case law on PPMs is scarce and has focused on Article XX GATT. By finding that npr-PPMs fall outside the scope of Article III GATT because they do not regulate products as such, the GATT panels in the *Tuna-Dolphin* cases have strongly, but arguably falsely, influenced the PPM debate. The measures were found to be import bans inconsistent with Article XI GATT, steering the analysis to Article XX GATT. The AB in the landmark *US-Shrimp* was not in the position to clarify the relation between Articles III and XI GATT as Article III was not invoked by either of the parties. The relationship between Article III and Article XI with respect to npr-PPMs thus remains unclear, but could have important consequences for npr-PPMs. A measure falling within the scope of Article XI GATT is in violation of this Article, and will thus need to be justified under the general exceptions. Under Article III, though, an inconsistency is not automatically established. Firstly, consumer preferences could influence a finding of likeness if they demonstrate a sufficiently strong preference for one product over another based on the production method. Secondly, it could be argued that treatment less favourable can only be established when the detrimental impact is due to the foreign origin of the imported products. Through a TBT-inspired, revised 'aims-and-effects' test, regulatory purposes might be taken into account at the stage of determining treatment less favourable, whereby states can make regulatory distinctions based on legitimate regulatory objectives. Only when the conditions of likeness and treatment less favourable are fulfilled, will the analysis turn to Article XX GATT. A measure could be justified under Article XX if the conditions of the paragraphs and the *chapeau* are met.