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Solving the Production and Processing Methods (PPMs) Puzzle

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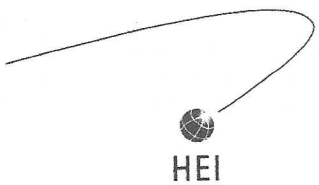

Graduate Institute of International Studies
Institut universitaire de hautes études internationales
The Program for the Study of International Organization(s) (PSIO)

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Preface

The Graduate Institute of International Studies created the PSIO in 1994 to facilitate collaboration between the international and academic communities in Geneva and worldwide. It is both a research program aiming to further the study of international organizations and a forum designed to stimulate discussions between academics and policy makers within the environment of the Graduate Institute and Geneva. The Program harkens back to the original mandate of the Graduate Institute with the establishment of the League of Nations in Geneva and recognizes the continuing importance of Geneva as one of the world's leading centres for international organizations.

With the support from the State Secretariat for Economic Affairs of the Swiss Federal Department of Economy, the Graduate Institute and the PSIO will hold a series of 12 meetings during 2000 and 2001 entitled "Academics and Negotiators Evening Seminars".

The overall justification for this series is the increasing importance of the WTO's activities to economic growth and commercial relations around the world, the growing complexities of issues on the WTO's agenda, and the commitment to begin a new round of multilateral trade negotiations on at least agriculture and services, and perhaps on a broad range of issues that could approach the breadth and complexity of the Uruguay Round agenda.

During the Tokyo Round negotiations, and again during the main part of the Uruguay Round negotiations, the Graduate Institute obtained financial support from the Ford Foundation to organize a series of meetings at the Institute involving "academics and negotiators". The regular participation of a substantial number of GATT delegates, and the popularity of the printed versions of the papers presented at the seminars, was strong evidence that these meetings were an important input into the deliberations and negotiations in both the Tokyo Round and the Uruguay Round.

With support from the Ford Foundation during the years 1997 and 1998, the Graduate Institute and its PSIO organized a series of 12 meetings, this time taking place prior to a new round of trade negotiations. The reason for this change was three-fold: the importance of the initial three-to five years of work in the new WTO - in terms of substance and procedures - for its evolution as both an institution/forum and a set of multilateral rules and disciplines; the fact that the Uruguay Round agreements signed at Marrakesh mandated a series of new negotiations on agriculture and services; and the growing complexity of new topics on the agenda of the WTO.

As more policies become "trade-related", the agenda of trade negotiations becomes more complex. Delays can result, as was evident from the efforts of delegations in the early years of the Uruguay Round to understand liberalization of services and the protection of intellectual property at the global level. This suggests that a new series of "academics and negotiators" meetings can play an important educational role in helping the delegations in Geneva - as well as academics/researchers - prepare in advance for the first round of multilateral trade negotiations under the new World Trade Organization (WTO).

These occasional papers are designed to stimulate reflection on potential issues for that first round.

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Chapter 1

Introduction

One of the most knotty issues of the "trade and environment" debate is the use of trade measures linked to the production process. These are called PPMs. It is often alleged that the rules of the World Trade Organization (WTO) prohibit PPMs. In response, many environmentalists say this shows that the trading system interferes with ecological protection. Conflicting views about PPMs have been one of the biggest barriers to reducing tensions between the WTO and environmentalists.

PPMs can be appropriate instruments of environmental policy. The World Charter for Nature, approved by the United Nations General Assembly in 1982, calls on governments to "Establish standards for products and manufacturing processes that may have adverse effects on nature, as well as agreed methodologies for assessing these effects."[1] Even the WTO Agreement on Agriculture -- in prescribing criteria for domestic support measures that remain exempt from reduction -- states that payments under environmental programs must be dependent on specific conditions such as "conditions related to production methods or inputs."[2] So long as a country applies PPMs only to domestic producers, no other country will complain.

[1] World Charter for Nature, U.N. Doc. A/RES/37/7, Nov. 9, 1982, para. 21(b).

[2] Agreement on Agriculture, Annex 2, para. 12(a), *reprinted in* WORLD TRADE ORGANIZATION, THE LEGAL TEXTS. THE RESULTS OF THE URUGUAY ROUND OF MULTILATERAL TRADE NEGOTIATIONS.

The conflict occurs because governments seek to apply PPMs to imported products. A government that does so is signaling that it cares about conditions outside of its own borders. Of course, this may not be the only motivation behind a PPM. A government that has imposed a regulatory burden on its domestic producers may seek to impose a similar burden on foreign producers so they do not gain a competitive advantage. PPMs may also constitute disguised protectionism.

The use of externally-directed PPMs is an inevitable byproduct of globalization and of the increased recognition that activities in one country can impinge on the environment in another. Thus, PPMs are not likely to be extinguished. If anything, they will probably be used more in the future than in the past.

Nevertheless, the use of PPMs and the debate surrounding them continue to be a puzzle. Both sides of the debate are convinced that they are in the right, and little common ground has been found in the past several years. A central disagreement is whether rules of the General Agreement on Tariffs and Trade (GATT) prohibit PPMs *per se*, or whether they are permitted in certain circumstances.

This paper takes one step toward "Solving the PPM Puzzle." The thesis advanced here is that if governments share the same understanding of the legal status of PPMs in the WTO, then it would be easier to move forward with agreements for supervising the use of externally-directed PPMs. Right now governments do not share the same legal understanding. This has led to an inside-out debate that cannot possibly go forward. Without a common understanding about the legal status of PPMs, it has been impossible even to hold a meaningful dialogue on how to curb PPM excesses.

As will be shown below, a widespread myth exists that the WTO forbids PPMs. If this were true, it would put the WTO at odds with environmental regulation. Happily, it is not true. The WTO does not categorically prohibit the application of a PPM to an imported product. The WTO's Shrimp-Turtle

decision of 1998 clarified trade rules on this point.[3] Ironically, turtles remained a flash point with the public in late 1999 when some of the anti-WTO protestors in Seattle dressed up as turtles [4]

This paper will proceed in the following way. Following this introduction, Chapter 2 explains what PPMs are and explores when they might be justifiable. It also sets out taxonomy of PPMs. Next, Chapter 3 conducts a careful examination of the relevant WTO caselaw on the issue of PPMs. Using the taxonomy from Chapter 2, it concludes with a Restatement of the WTO Law of PPMs. Chapter 4 ties together Chapters 2 and 3 to show how a correct legal reading may enable new integrative positions that can resolve trade and environment tensions and establish a better framework for preventing inappropriate PPMs. The final chapter presents a brief conclusion.

This paper only addresses environmental PPMs. The legal and policy conclusions reached here are not necessarily transferable to other kinds of PPMs, such as labor, human rights, or animal welfare restrictions. This point is noted at the start to deal with the inevitable complaint that countenancing environmental PPMs would lead to a slippery slope of less justifiable PPMs.

One possible weakness of this paper is that it is written by a United States national who might be perceived as taking a Northern, big economy perspective. In Chapter IV, however, the paper suggests ways of disciplining and managing PPMs so that they will not undermine the interests of developing countries. As will be noted, many PPMs have been designed and implemented in ways that are unfair to economic actors in developing countries who are struggling to export.

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[3] Bruce Neuling, *The Shrimp-Turtle Case: Implications for Article XX of GATT and the Trade and Environment Debate,* 22 LOYOLA OF LOS ANGELES INTERNATIONAL AND COMPARATIVE LAW REVIEW 1 (1999). Despite its formal name that gives no mention of the turtles, this matter is widely known as the Shrimp-Turtle case. Even the WTO website notes this shorthand designation. Robert Howse calls it the Turtles panel. For his critique of the panel report, see Robert Howse, *The Turtles Panel. Another Environmental Disaster in Geneva,* 32 JOURNAL OF WORLD TRADE 73 (Oct. 1998).

[4] Joan Lowy, *Protesters Have Long List of Complaints Against World Trade Group,* CHATTANOOGA FREE PRESS, Dec. 2, 1999, at A7.

Chapter 2

What are PPMs and When Are they Justifiable ?

Let's start with the term PPM itself. It means "processes and production methods." The term originated in the Tokyo Round Agreement on Technical Barriers to Trade, and referred to standards aimed at the production method rather than product characteristics.[5] During the 1990s, the connotation of PPM expanded beyond that origin. Now PPM refers to any trade measure or any domestic regulation or tax that distinguishes products by looking beyond perceptible characteristics. For example, a law prohibiting the sale of fish caught using a driftnet is a PPM. By contrast, a law prohibiting the sale of fish below a prescribed size is not a PPM.

A custom has developed of dividing PPMs into two categories -- product-related and non-product-related.[6] Product-related PPMs are used to assure the functionality of the product, or to safeguard the consumer who uses the product. The best example is in the area of food safety where regulators rely on process-based sanitary rules so as to avoid having to test the salubrity of the final product (which could destroy its market value). Such PPMs help assure that consumers receive a product at the anticipated quality level. Thus, they are *related* to the product. By contrast, the non-product-related PPM is designed to achieve a social purpose that may not even matter to the consumer. For example, prohibiting the use of a driftnet to catch fish may achieve a public goal, but has no effect on the fish as such or on the nutritional and gustatory

[5] Agreement on Technical Barriers to Trade (1979), GATT, BISD 26S/8, para. 14.25.

[6] OECD Secretariat, "Processes and Production Methods (PPMs): Conceptual Framework and Considerations on Use of PPM-Based Trade Measures," OCDE/GD(97)137. This study presents an analytical framework for PPMs.

functionality for the consumer. Thus, such PPMs are denoted as non-product-related.[7]

Although this related/unrelated distinction is not stated explicitly in WTO rules, it appears to be followed in two agreements. The Agreement on Technical Barriers to Trade (TBT) defines a covered regulation as a document which "lays down product characteristics or their *related* processes and production methods . . . ."[8] This would seem to suggest that TBT covers the product-related PPMs, and excludes the others.[9] The Agreement on the Application of Sanitary and Phytosanitary Measures (SPS) defines covered measures broadly including those referring to "processes and production methods."[10] But because SPS applies only to measures seeking to protect life or health *within* the territory of the importing country, the typical non-product-related PPM would be excluded by this geographic limitation.[11] For example, regulations referring to the humane treatment of a farm animal used to make meat for export would be a non-product-related PPM, and thus not covered by SPS.

The related/unrelated distinction is popular with commentators, but is flawed. It is used for its simplicity and because that distinction can help to explicate WTO rules. This paper will use it too. Yet before doing so, I want to point out that the distinction is not as clear as it may seem. To start with, the assertion of

[7] Another term used is unincorporated PPMs meaning that the characteristics of the process do not become part of the product.

[8] WTO Agreement on Technical Barriers to Trade, Annex 1, para. 1 (emphasis added).

[9] *See* Negotiating History of the Coverage of the Agreement on Technical Barriers to Trade with regard to Labelling Requirements, Voluntary Standards, and Processes and Production Methods Unrelated to the Product Characteristics, WTO Doc. G/TBT/W/11, Aug. 29, 1995, paras. 131, 146.

[10] Agreement on the Application of Sanitary and Phytosanitary Measures, Annex A, para. 1.

[11] *Id.*, para. 1. It is conceivable for a non-product-related PPM to be covered by SPS. For example, a measure forbidding the use of a pesticide in foreign agriculture, not because it is harmful to the consumer but because wind blows the pesticide across the border into the importing country and hurts its agriculture, would be covered by SPS.

unrelatedness is too strong. Since any PPM is employed with reference to a product, categorizing it as "unrelated" or "non-related" is a misnomer.[12]

A deeper problem is the assumption that consumer preferences can be neatly divided between the functionality of the product itself and broader concerns. To be sure, the blindfolded consumer will not be able to tell whether the fish on the dinner plate was caught using a driftnet. Yet in the real world, consumers do not have blindfolds on. Once a consumer suspects that the fish was caught with a driftnet, it may taste different to her. Indeed, she may not want to eat it at all. It will be simply impossible to convince the sovereign consumer that her concerns about unsustainable fishing practices are not related to the fish itself.

Another problem with the related/unrelated distinction occurs with regulations that have multiple purposes. For example, a ban on genetically-modified food might be used to address the alleged ecological impact on agriculture, or the human health impact of consumption. So the same regulation might be both product-unrelated and product-related.

Still another difficulty is that for some PPMs, the product is the process. The best example is a regulation specifying a minimum amount of recycled content. Such a regulation defines the product and also mandates a production process that uses recycled inputs. Yet recycled newsprint may be indistinguishable from virgin newsprint and will be used in the same way by the consumer.[13] So is this PPM product-related?

Notwithstanding these conceptual dilemmas, this paper will follow the custom of categorizing PPMs as being either product-related or non-product-related. This paper will focus on the non-product-related environmental PPMs. We will explore why they are used and what the trade regime should do about them.

[12] Arthur E. Appleton, *Telecommunications Trade: Reach Out and Touch Someone?*, 19 UNIVERSITY OF PENNSYLVANIA JOURNAL OF INTERNATIONAL ECONOMIC LAW 209, 216 (1998).

[13] J. Christopher Thomas, *The Future: The Impact of Environmental Regulations on Trade*, 18 CANADA-UNITED STATES LAW JOURNAL 383, 389–90 (1992) (discussing newsprint standard).

Why PPMs are Needed

Begin with the popular view that the non-product-related PPMs are ill-conceived and should be forbidden by the WTO. That simplistic view is unjustified. The driftnet fishing example is just one of a wide array of concerns that consumers may have about the externalities of production. Various terms are used to describe this -- like the social profile of a product, or its ecological footprint, or its embedded values. And for a consumer to have these concerns may be rational. Consumers in one country can be affected by the production methods used in another. And they may logically ask their governments to take action and to work together to manage this interdependence.

The need for doing so is not a new idea, and certainly not a new idea to the Graduate Institute. As Professor William Rappard explained in 1925:

Little by little the boundaries of what is held to be solely within the domestic jurisdiction of individual States are receding and the realm of what is governed by international law is expanding.[14]

Rappard's point is that a State's domestic jurisdiction over an issue may not be exclusive and does foreclose a broader community interest and jurisdiction over what transpires within a State. Rappard's insight is especially applicable to environmental policy, where many irritants flow across political borders.

From the beginning of international environmental law, PPMs unrelated to the product have been employed by governments. For example, a 1925 treaty between Mexico and the United States set up an International Fisheries Commission to conserve marine life in the Pacific Ocean and committed the parties to refuse the landing of any fish taken in violation of the Commission's regulations.[15] A 1931 treaty between Denmark and Sweden to protect migratory birds forbade the use of nets for catching seabirds and prohibited the

[14] WILLIAM E. RAPPARD, INTERNATIONAL RELATIONS AS VIEWED FROM GENEVA 127 (1925). Rappard was the co-founder and longtime Director of the Graduate Institute.

[15] Convention to Prevent Smuggling and for Certain Other Objects, Dec. 23, 1925, U.S.-Mex., 48 L.N.T.S. 444, arts. 10-12 (no longer in force).

sale or transport of such birds when caught in nets.[16] Even when they obtain treaties, governments will use trade measures to promote treaty compliance. For instance in 1950, the United States enacted a law prohibiting the import of whale products taken in violation of the Whaling Convention.[17] These examples serve to demonstrate the historical point that governments use PPMs to promote changes in foreign practices inimical to the international interest. Regulatory prescriptions regarding the production process are an inherent part of environmental policy.

Because the environment regime has successfully produced many important treaties during the past three decades, there is sometimes a tendency to believe that any significant transborder environmental problem will engender a treaty that will obviate unilateral PPMs. This was a common theme in the criticism of PPMs throughout the 1990s, which assumed that countries like the United States were choosing national action over equally available multilateral action. But the reality is that effective, broad-membership treaties are difficult to achieve. Furthermore, treatymaking negotiations sometimes succeed because leading countries have manifested a willingness to act alone if necessary, a process called "policy-forging" unilateralism by Laurence Boisson de Chazournes.[18]

In their introductory essay to *The Greening of World Trade Issues* in 1992, Kym Anderson and Richard Blackhurst framed the issue properly. They said that "If all countries participated in all international environmental agreements, there would be nothing more to add."[19] Yet as Anderson and Blackhurst and the

[16] Agreement regarding certain provisions for the Protection of Migratory Game-Birds, Oct. 9, 1931, Den.-Swed., 126 L.N.T.S. 259, art. 1.

[17] 16 U.S.C. § 916c(a).

[18] Laurence Boisson de Chazournes, *Unilateralism and Environmental Protection: Issues of Perception and Reality of Issues,* 11 EUROPEAN JOURNAL OF INTERNATIONAL LAW 315, 317, 325 (2000).

[19] Kym Anderson & Richard Blackhurst, *Trade, the Environment and Public Policy, in* THE GREENING OF WORLD TRADE ISSUES 3, 20 (Anderson & Blackhurst eds., 1992).

other authors recognized in that seminal volume, many environmental problems are not addressed by treaties with universal participation.[20]

The protection of migratory sea turtles is a good example of a long-recognized problem for which international legislation has been slow in developing. As early as 1924, the Pan-Pacific Food Conservation Conference declared that "prompt action is necessary to save the marine turtles of various countries from commercial, if not actual extinction . . . ."[21] In 1979, the World Conference on Sea Turtle Conservation called for international and national fishery commissions to "promulgate regulations requiring the use of gear which precludes the capture of sea turtles . . ." and for the U.N. Environment Programme and the Food and Agriculture Organization to make U.S. technology for turtle-safe shrimping available to world fishing fleets.[22] In 1989, the U.S. Congress directed the Secretary of State to initiate negotiations as soon as possible with all foreign governments who have nationals engaged in commercial fishing that may adversely affect sea turtles.[23] Yet it was not until 1996 that governments succeeded in negotiating a treaty on sea turtle conservation, and this did not occur until the U.S. government had embargoed shrimp imports from countries whose vessels were not using turtle excluder devices (TEDs).[24]

Of course, environmental negotiations will not always need the catalyst of trade measures. Most environmental treaties were achieved without any inducement

[20] The earliest analysis that has come to my attention of the difficulty in attaining an environmental treaty is: Charles Edward Fryer, *International Regulation of the Fisheries of the High Seas*, 28 BULLETIN OF THE BUREAU OF FISHERIES 91, 95 (1908).

[21] 29 MID-PACIFIC MAGAZINE 182–83 (Jan. 1925).

[22] BIOLOGY AND CONSERVATION OF SEA TURTLES. Proceedings of the World Conference on Sea Turtle Conservation, Nov. 1979 (Karen A. Bjorndal ed., 1981), at 582.

[23] P.L. 101-162 § 609(a)(2).

[24] Inter-American Convention for the Protection and Conservation of Sea Turtles, Dec. 1, 1996, Senate Treaty Doc. 105-48. U.S. embargoes on shrimp began in 1991. U.S. Customs Service memorandum regarding Importation of Shrimp from Suriname, May 2, 1991.

by trade measures. But trade measures can sometimes be useful to address the problem of free riders. For example, the Montreal Protocol on Ozone prohibits trade in controlled substances with non-parties (unless they are in full compliance with the Protocol's control measures).[25] This provision is considered to be an important factor in eliciting the wide membership of this treaty.[26]

When the first-best option of multilateral cooperation is unavailable, an affected government may consider using a trade PPM to address transborder problems indirectly. Precisely because it is so indirect, such a PPM will be less than fully efficient. But the most efficient measures are only available to a government with prescriptive jurisdiction over the production process. So if the producing country's government fails to use the regulatory instruments at its disposal, other affected country governments may be left with only inefficient or blunt instruments.[27] In deciding whether to use such a PPM, a government may consider not only the immediate impact but also the demonstration effect of acting to address an environmental problem.

The earliest recognition of this quandary in international environmental affairs involved bird hunting. In the early 20th century, millions of birds were being killed for their plumage. Bird protection groups in Great Britain sought a ban on feather imports, but were opposed on the grounds that this would not necessarily safeguard birds in other countries. One essayist responded to this claim eloquently in 1909 by saying that

> . . . if the importation into our country is stopped, other Governments may follow suit. Representations to foreign countries are much more likely to be effectual if made by a Government, which has had the

[25] Montreal Protocol on Substances that Deplete the Ozone Layer, Sept. 16, 1987 and as adjusted thereafter, art. 4, available at www.unep.org/ozone/mont_t.htm.

[26] DUNCAN BRACK, INTERNATIONAL TRADE AND THE MONTREAL PROTOCOL 54–58 (1996).

[27] Regulatory action may not be efficient for the producing country. For example, a hypothetical electorate might place little value on sea turtles and therefore that government may be justified in taking no action to regulate shrimp harvesting.

courage of its convictions, and has already put its principles into practice.[28]

By 1917, Great Britain took action to ban the importation of bird plumage. Similar action in other countries cut down traffic in birds and led to changes in fashion that reduced demand for feathers.[29]

Some commentators have suggested that it is illegitimate for a government to apply environmental PPMs to imports because that seeks to force changes in practices occurring in other countries. If this were true, then it would also be true for product-related PPMs, such as food safety rules, that work by eliciting changes in production practices in other countries. The same concern would also apply to simple product standards, for example automobile safety requirements that regularly induce foreign manufacturers to adapt their assembly lines.[30] The WTO itself contains 33 pages of textile tariff classifications, some of which create fine categories that may encourage producers to qualify their products for one rather than the other.[31] Since such normal standard-setting cannot possibly be illegitimate, the initial premise must be faulty. The fact that a government regulation in Country A will induce businesses in Country B and C to change their behavior, does not render A's regulation illegitimate.

Because environmental PPMs are employed to correct market failure, they can increase global economic efficiency when well designed. But not every country will necessarily be better off. Trade measures taken for environmental purposes can cause adverse economic effects on exporting countries.

[28] A HOLTE MACPHERSON, LEGISLATION FOR THE PROTECTION OF BIRDS 29 (1909).

[29] *See generally* ROBIN W. DOUGHTY, FEATHER FASHIONS AND BIRD PRESERVATION (1975).

[30] For example in 2001, the United States will require that car trunks have inside releases. This new standard will surely force foreign automakers to redesign their products.

[31] Agreement on Textiles and Clothing, Annex. Some of these categories read like PPMs (e.g., 5702.10).

Policymakers using PPMs need to be sensitive to how much burden is being shifted to target countries. It may be useful to regularize the examination of the costs imposed by PPMs to the least developed countries.

Yet one needs to keep this in perspective. The biggest impediment to market access for developing countries are *undisguised* protectionist measures in industrial and other developing countries. The complaints about PPMs are highly disproportionate to their relative adverse impact on developing countries, in comparison to all of the other practices that constrain their exports. Indeed, it is a sad irony that developing country governments devote so much time to complaining about environmental PPMs (which provide some social benefits through the correction of market failure) while giving less attention to commercial barriers in agriculture and textiles (which do not correct market failure).

Of course, any PPM -- product related or not -- should be subjected to scrutiny by the WTO to see if it is protectionist.[32] This inquiry needs to be carried out in a sophisticated manner. The fact that domestic producers may want foreign producers to be subject to harmonized environmental PPMs may be a warning signal of protectionist intent, but is not itself conclusive. The key question to ask is whether there is an environmental rationale for the importing country government to be concerned about production practices in the exporting country. If not, then the effort to prescribe equivalent PPMs in other countries in order to level the playing field is probably protectionist. In many instances, however, the importing country will have an environmental reason to want other countries to take comparable action to safeguard a shared natural resource.

Let me summarize this paper so far. Governments use environmental PPMs in treaties and national law in order to achieve conservation or anti-pollution

[32] Daniel P. Blank, *Target-Based Environmental Trade Measures: A Proposal for the New WTO Committee on Trade and Environment,* 15 STANFORD ENVIRONMENTAL LAW JOURNAL 61, 119 (1996).

goals.[33] PPMs aimed at foreign governments are indirect and thus will always be inefficient, but resort to such PPMs may be better than doing nothing in the absence of multilateral cooperation. It is wrong to assert that governments should mind their own business environmentally. It is also wrong to assert that PPMs are illegitimate because they may induce changes in foreign production practices. Even the simplest product standard can do that.

Generalizing about non-product-related PPMs is challenging because they come in many different forms. The next section will introduce a taxonomy that is the key to solving the PPM puzzle. The debate on PPMs has made little progress in 10 years because it jumbles up too many different kinds of measures.

A Taxonomy of PPMs

PPMs can be divided into two main types -- (1) the How Produced standard and (2) the (Foreign) Government Policy standard. The How Produced standard looks at the processing method used in making the product. For example, a law banning the importation of driftnet-caught fish is a how-produced PPM. [34] The Government Policy standard looks at the foreign government's laws or regulations regarding the production process, or at its enforcement of them. For example, a law banning the importation of fish from any country that permits driftnet fishing is a government policy PPM. [35] Both types of PPM train on the methods used for mining, harvesting, manufacturing, packaging, and transporting.[36]

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[33] JAMES R. LEE, EXPLORING THE GAPS. VITAL LINKS BETWEEN TRADE, ENVIRONMENT AND CULTURE 174 (2000).

[34] No such law exists in the United States, but federal law bars the import of tuna that is not "dolphin safe" which until recently was defined in relation to the method of harvesting. 16 U.S.C. § 1417(a)(1), (d) (1998).

[35] U.S. law provides for an import ban in certain circumstances of fish and sport fishing equipment from countries whose governments have not agreed to terminate large-scale driftnet fishing by nationals beyond the exclusive economic zone. 16 U.S.C. § 1826a(b).

[36] Thus, banning the importation of fish caught with a driftnet is different than banning the importation of widgets as a sanction to induce the other country to stop driftnet fishing practices.

In using the term "standard," I mean its everyday connotation of an instruction that is binding. Thus, the usage here differs from the definition of "standard" in the TBT Agreement, which refers to product characteristics or product-related PPMs with which compliance is not mandatory.[37] By contrast, in the TBT definitions, a regulation is "mandatory." I am not using the term "regulation" for two reasons. First, while some environmental PPMs are regulations applied equally to foreign and domestic products, many PPMs are import bans that do not come within the scope of TBT. Second, the term "regulation" may connote a jurisdiction to prescribe or mandate, but this does not fit PPMs, which set conditions for entry or sale which the exporter may decide to meet or not to meet. If it does not meet them, no disadvantage is incurred other than an inability to sell to the PPM-applying country.

A standard prescribing *where* a product must be produced is not a PPM. For example, a U.S. law that bans fish (and all other) imports from Cuba is an embargo rather than a PPM. Sometimes import laws blend "where" and "how" standards.

A where-produced standard can be disguised as a how-produced standard by using origin-neutral language that pertains only to a particular country. Consider for example, the most well-known PPM before the tuna-dolphin case. That was the German law of 1904 providing a tariff reduction for "large dappled mountain cattle or brown cattle reared at a spot at least 300 meters above sea level and which have at least one month's grazing each year at a spot at least 800 meters above sea level."[38] That's a how-produced PPM that is non-product related. It is a classic example of how origin-based protectionism can be disguised as a how-produced standard.[39]

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[37] Agreement on Technical Barriers to Trade, *supra* note 8, Annex 1, para. 2.

[38] League of Nations, Memorandum on Discriminatory Tariff Classifications (1927), League Doc. C.E.C.P. 96, at 8.

[39] Robert E. Hudec, *"Like Product": The Differences in Meaning in GATT Articles I and III, in* REGULATORY BARRIERS AND THE PRINCIPLE OF NON-DISCRIMINATION IN WORLD TRADE LAW 103, 109–11 (Thomas Cottier & Petros C. Mavroidis eds., 2000).

A standard prescribing eligible producers or importers can be viewed as a subset of a how-produced standard, but may not always be classified as a PPM. For example, a law that bans fish imports from a producer owned by a pariah government can be considered an import control, rather than a PPM. Nevertheless, in setting out a PPM taxonomy, we will need to take account of the Producer Characteristics standard. This is so for two reasons: First, in prescribing attributes of a producer or its contractual relations, the importing government can seek to accomplish policy purposes similar to what might be sought using a how-produced or a government-policy PPM. Second, much of the trade law jurisprudence that seems applicable to PPMs involved measures based on producer characteristics. So the producer characteristics standard will be treated here as a PPM.

Although this paper looks at environmental PPMs, one should note that the suggested taxonomy applies to other PPMs too. For example, in July 2000, the World Diamond Congress took action to address the problem of "conflict diamonds" which fund terrorism in Africa.[40] The Congress recommended that governments enact laws to prohibit imports of diamonds from countries that have not enacted redline legislation which requires that diamond imports be sealed and registered. This is a standard based on the foreign government's policy, not on how a particular diamond was mined or on whether it is being mined or sold by rebel forces.

In presenting this PPM taxonomy, I am suggesting that form matters. My thesis is that the how-produced standard is preferable to the (foreign) government policy or producer characteristics standards. In Chapter 3, I will show that the how-produced standard may be more WTO-consistent than the other two. At this time, no GATT or WTO dispute panel has ruled against a how-produced standard utilized for an environmental purpose.

[40] Holly Burkhalter, *Deadly Diamonds,* LEGAL TIMES, Sept. 11, 2000, at 74. *See also* Andrew Parker, *Pledge on Action to Curb Sales of "Conflict Diamonds,"* FINANCIAL TIMES, Oct. 27, 2000, at 8.

The government policy standard has numerous faults. First, it is coercive in that it dictates environmental policies to foreign governments. Second, it penalizes private economic actors who may be doing everything right environmentally, but whose exports remain blocked because its environmental behavior is not mandated by law. Third, the government policy standard is unfair because it is more available to large than to small countries. Fourth, the government policy standard can engender irreconcilable conflicts because two importing countries might impose inconsistent policy standards on an exporting country government.

By contrast, the how-produced standard operates similarly to a simple product standard. It does not coerce governments.[41] It does not penalize economic actors who are willing to assure that their exports meet the importing country standard. Small countries can use such standards because they will almost always find willing suppliers. So the how-produced standard will never cause as much trade tension as the government policy standard does. Thus, if environmental PPMs are needed, they should be written in the how-produced form rather than the government policy form.

The how-produced standard can be a proportionate and measured response to a situation where importing from the other country can exacerbate an environmental problem. When a government allows the importation of fish caught with a driftnet, the importing country signals that such odious practices are acceptable for future trade, and so exporting country producers may continue to use them. But when a country bans such fish, it signals its objections to that method of production and makes it less profitable. Private economic actors will then have a new incentive to improve their environmental behavior.

[41] Robert Howse & Donald Regan, *The Product/Process Distinction – An Illusory Basis for Disciplining "Unilateralism" in Trade Policy,* 11 EUROPEAN JOURNAL OF INTERNATIONAL LAW 249, 277 (2000).

To be sure, a how-produced PPM may be less effective than a government policy standard, and that could be unsatisfactory to environmental regulators.[42] But this lower effectiveness needs to be balanced against the disadvantages to environmental policy of being heavy-handed. It is one thing for Country A to specify a PPM for the fish that it imports from Country B. It is quite another for Country A to say that it will not import any fish from B unless *all* of B's fish are caught in the prescribed way. Environmentalists must not forget that any PPM applied to imports is an indirect measure and is thus inferior to attaining appropriate regulations in other countries. Treating Country B unfairly may make it harder to convince B's government and stakeholders to cooperate on the environment.

In summary, Chapter 2 explains why PPMs are needed and presents a taxonomy of them. The government policy standard is contrasted with the how-produced standard and the latter is shown to be a more reasonable approach. In Chapter 3, we will look at how international trade law treats different types of PPM.

[42] *See* Howard F. Chang, *An Economic Analysis of Trade Measures to Protect the Global Environment,* GEORGETOWN LAW JOURNAL 2131, 2177–85 (1995).

Chapter 3

The WTO Law of PPMs

Chapter 3 will analyze how WTO rules supervise PPMs applied to imports. The focus will be on non-product-related environmental PPMs. Thus, it will not be necessary to look at the SPS and TBT agreements. Instead, the main focus will be on the GATT.

Many commentators have contended that the GATT does not permit importing governments to make distinctions based on the production process. For example:

> The most fundamental problem with Article XX is that it makes the legitimacy of environmental regulations turn on what is produced, not how it is produced. Specifically, GATT's existing rules focus on the concept of "like products," barring environmental discrimination against imports that are physically similar to domestic products no matter how damaging the production process used to make or obtain the good.[43] (Daniel Esty, Institute for International Economics, 1994)

> [GATT] Article XX only examines what is produced and not how it is produced, without explicitly mentioning this fact. Trade cannot be restricted on the basis of different environmental PPMs.[44] (Markus Schlagenhof, Swiss Government, 1995)

In other words, PPM requirements are permissible under the GATT law basically to absorb "consumption externalities" rather than "production

[43] DANIEL C. ESTY, GREENING THE GATT 49–51 (1994). In correspondence with the author, Esty states that this passage represented the prevailing reading of the GATT in 1994, but that since then, a more refined reading of Article XX has emerged in WTO caselaw.

[44] Markus Schlagenhof, *Trade Measures Based on Environmental Processes and Production Methods,* 29 JOURNAL OF WORLD TRADE 123, 138 (Dec. 1995) (footnote omitted).

externalities": the latter should be dealt with by the producing, exporting country.[45] (Shinya Murase, Academy of International Law, 1995)

The WTO agreements are interpreted to say two important things. *First,* trade restrictions cannot be imposed on a product purely because of the way it has been produced. *Second,* one country cannot reach out beyond its own territory to impose its standards on another country.[46] (World Trade Organization, 1998)

The trade community has emphasized repeatedly that discrimination between "like" products based solely on method of production should find no place in trade rules.[47] (Sir Leon Brittan, European Commission, 1998)

. . . [T]he WTO rules generally prohibit distinguishing among non-product-related Production and Processing Methods (PPMs).[48] (Lori Wallach & Michelle Sforza, Public Citizen, 1999)

One of the basic principles of the WTO is that member countries may not discriminate between "like products." This has hitherto normally been interpreted as preventing discrimination between goods on the basis of how they are produced. . . . To allow discrimination on the basis of production and processing methods (PPMs), there would have to be a re-interpretation of the crucial term "like product."[49] (House of Lords, Select Committee on European Communities, 2000)

As part of it core non-discrimination principles, the GATT requires that "like products" be treated the same by the importing country and distinctions based

[45] Shinya Murase, *Perspectives from International Economic Law on Transnational Environmental Issues,* 253 RECUEIL DES COURS 287, 339 (1995).
[46] WORLD TRADE ORGANIZATION, TRADING INTO THE FUTURE. INTRODUCTION TO THE WTO 47 (1998). The same text remains on the WTO website as of November 2000.
[47] "Vice President Brittan Calls for More Coherence in Trade and Environmental Policy," European Union News, Mar. 23, 1998.
[48] LORI WALLACH & MICHELLE SFORZA, WHOSE TRADE ORGANIZATION? 174 (1999) (footnote omitted).
[49] House of Lords, Select Committee on European Communities, The World Trade Organisation: The EU Mandate After Seattle, June 13, 2000, paras. 223–24.

on "production processes or methods" (PPMs) are generally prohibited.[50] (Kim Elliott, Institute for International Economics, 2000)

And, we noted, WTO law does not allow countries to discriminate against like products, whatever their different environmental impacts. This prohibition makes little environmental sense. The way a product is produced is one of the three central questions for an environmental manager . . . .[51] (UN Environment Programme & International Institute for Sustainable Development, 2000)

Yet is all that really true? Certainly, the text of the GATT does not forbid national regulations, taxes, tariffs, or import bans based on the production process. On the contrary, the GATT allows governments to discriminate against imports made in prohibited ways. Thus, governments can take customs action against an imported article made using a subsidy, or whose producer prices it too low, or whose producer does not have the requisite intellectual property licenses.[52] The consumer may not agree with his government that these methods of production should be attacked with trade measures. The subsidized, low-cost imported fish will taste as good as the higher-cost domestic fish. But the GATT permits governments to impose PPMs of this sort anyway even though the behavior being complained about has no effect on the product as such.

Even without explicit language, however, GATT rules may still prohibit environmental PPMs. As noted above, many commentators take this position. Over the years, the GATT Secretariat has taken both sides of the debate. When it first addressed the matter in 1971, the Secretariat explained that:

A *shared resource*, such as a lake or the atmosphere, which is being polluted by foreign producers may give rise to restrictions on trade in the *product of that*

[50] Kimberly Ann Elliott, *(Mis)Managing Diversity: Worker Rights and US Trade Policy,* 5 INTERNATIONAL NEGOTIATION 97, 120 (2000).
[51] U.N. ENVIRONMENT PROGRAMME & INTERNATIONAL INSTITUTE FOR SUSTAINABLE DEVELOPMENT, ENVIRONMENT AND TRADE. A HANDBOOK 43 (2000).
[52] GATT arts. VI, XVI, XX(d).

process justifiable on grounds of the public interest in the importing country of control over a *process* carried out in an adjacent or nearby country.[53]

Twenty years later, after environmental concerns grew in importance, the GATT Secretariat shifted its position. Now it asserted that "In principle it is not possible under GATT's rules to make access to one's own market dependent on the domestic environmental policies or practices of the exporting country."[54] This negative view was reaffirmed by WTO Director General Renato Ruggiero in 1997 who stated in a speech that

What a country cannot do under WTO rules, however, is apply trade restrictions to attempt to change the processes and production methods -- or other policies -- of its trading partners. Why? Basically because the issue of production and process methods lies within the sovereign jurisdiction of each country.[55]

Three years later, the WTO Secretariat continues to insist that PPMs violate trade rules.[56]

The WTO Secretariat's characterization of the rule against PPMs is similar to what many trade law commentators contend. The quotations above were selected to show how widespread the view is that PPMs are illegal under trade rules.[57] This list is balanced in containing commentators who favor the WTO's anti-PPM stance and those who oppose it.[58]

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[53] GATT, INDUSTRIAL POLLUTION CONTROL AND INTERNATIONAL TRADE, GATT Studies in International Trade No. 1, July 1971 (emphasis added).

[54] *Trade and the Environment, in* GATT, 1 INTERNATIONAL TRADE 90-91, at 23.

[55] Renato Ruggiero, "A Shared Responsibility: Global Policy Coherence for our Global Age," Dec. 1997, available on WTO website.

[56] *See* WTO, *infra* note 46.

[57] In his treatise of 1989, John Jackson suggests that the Article XX exceptions imply a focus on the product itself, and not on the production process. But he goes on to add that it might be possible to argue the contrary, and that the issue has not been squarely posed in dispute settlement. JOHN JACKSON, THE WORLD TRADING SYSTEM 209 (Paperback Edition, 1992).

[58] Of course, a vocal minority of commentators deny that the WTO prohibits PPMs. For example, *see* Howse & Regan, *supra* note 41.

Fortunately, these legal assessments are wrong. The GATT caselaw on PPMs is nuanced and does not point to a prohibition on the use of such environmental instruments. This will be explicated below.

The structure of GATT obligations is as follows: A PPM could be inconsistent with GATT Article I (most-favored-nation, or MFN) or GATT Article III (national treatment) or GATT Article XI (elimination of quantitative restrictions). If so, it would be reviewed under the General Exceptions in Article XX when there is an applicable exception.

The relationship between the GATT disciplines and Article XX is subject to different interpretations. One school of thought is that GATT Articles I, III, and XI impose *disciplines* on governments and that GATT Article XX provides exceptions to those disciplines. Whether a national measure is in conformity with the GATT can only be determined by looking at *both* the disciplines and the exceptions in tandem. Viewed in this way, when there is a measure that fails to provide national treatment, it should not be called a GATT violation merely because it violates Article I; a determination of GATT status requires a review of Article XX too. As Richard J. McLaughlin has noted with respect to Article XX, governments "have an expectation that they will be able to restrict trade in order to conserve exhaustible natural resources or to protect the health of humans, animals, and plants."[59]

The other school of thought is that GATT Articles I, III, and XI grant (or define) a *right* of a WTO member country to have the exports of its nationals accepted by other WTO member countries. Viewed in this way, the Article I, III or XI "rights" of the exporter will need to be weighed against the Article XX rights of the importer to rely upon one of the listed exceptions. Acting inconsistently with Article I constitutes a GATT violation, but it might be excused by Article XX.

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[59] Richard J. McLaughlin, *Sovereignty, Utility, and Fairness: Using U.S. Takings Law to Guide the Evolving Utilitarian Balancing Approach to Global Environmental Disputes in the WTO,* 78 OREGON LAW REVIEW 855, 938 (1999).

The WTO Appellate Body leans toward the latter school. In the U.S. Gasoline case, the Appellate Body held that "If those [Article XX] exceptions are not to be abused or misused, in other words, the measures falling within the particular exceptions must be applied reasonably, with due regard both to the legal duties of the parties claiming the exception and the legal rights of the other parties concerned."[60] In the U.S. Shrimp-Turtle case, the Appellate Body stated that

> . . . WTO Members need to maintain a balance of rights and obligations between the right of a Member to invoke one or another of the exceptions in Article XX, specified in paragraphs (a) to (j), on the one hand, and the *substantive* rights of the other Members under the GATT 1994, on the other hand. Exercise by one Member of this right to invoke an exception, such as Article XX(g), if abused or misused, will, to that extent, erode or render naught the substantive treaty rights, in, for example, Article XI:1, of other Members.[61]

The Appellate Body did not explain why Article XI:1 provides a "substantive" right, while Article XX does not. More fundamentally, the Appellate Body does not explain how Article XI:1 confers a "right" on any government. In the Japan Alcoholic Beverages case, the Appellate Body alludes to the "sheltering scope" of Article III, which suggests that Article III shelters measures from

[60] United States - Standards for Reformulated and Conventional Gasoline, Report of the Appellate Body [hereinafter Appellate Body Gasoline Report], Apr. 29, 1996, WT/DS2/AB/R, at 22. In its interpretation of GATT Article XX(g), the Appellate Body declared that this exception ("relating to the conservation of exhaustible natural resources") "may not be read so expansively as seriously to subvert the purpose and object of Article III:4." Appellate Body Gasoline Report, *Id.* at 18. This conclusion seems questionable. The purposes of objects of Article III are already reflected, to the appropriate extent, in the Article XX chapeau which excludes a measure that would constitute a "disguised restriction" in international trade.

[61] United States - Import Prohibitions of Certain Shrimp and Shrimp Products, Report of the Appellate Body [hereinafter Appellate Body Shrimp-Turtle Report], Oct. 12, 1998, WT/DS58/AB/R, para. 156 (emphasis added). *See also* para. 159 (discussing the "competing rights" under Articles XI and XX).

GATT review by conferring a right to undertake them.[62] But Article III is not a shield; it is a sword against discrimination.

By using the language of rights, the Appellate Body muddles GATT law and weakens the General Exceptions in Article XX. If the exporting country has a WTO "right" to have its exports accepted, then there will be tendency to interpret Article XX narrowly and begrudgingly so as not to interfere with that putative right. In characterizing Article XI as substantive, while implying that Article XX is not, the Appellate Body positions them at different levels and makes it easier for panels to forget the overriding injunction of Article XX, which provides that subject to certain requirements, "nothing" in the GATT shall be construed to prevent the adoption or enforcement of listed measures. An exporting country that faces an environmental trade measure may feel more justified in challenging the measure if it believes that GATT Articles I, III, and XI are detachable from Article XX.

A recent decision by a WTO arbitral panel, in the Brazil Aircraft case, continues down the path of minimizing Article XX. In that case, the panel had to interpret Item (k) of Annex I to the Agreement on Subsidies and Countervailing Measures (SCM). To simplify Item (k), it contains a rule and an exception. Looking at Item (k), the panel said that "A possible *justification* under item (k), like a justification under Article XX of the GATT 1994, does not change the legal nature of the measure."[63] While this may be a good analysis for the SCM Agreement, it is a troublesome analysis for the GATT because a justification of a measure under Article XX does change its legal nature. Thus, an environmental measure that violates GATT Article III, and might therefore violate the GATT, will have its legal nature transformed if it can be justified under Article XX. Unfortunately, under current WTO jurisprudence, the implications of Article XX can be characterized differently.

[62] Japan -Taxes on Alcoholic Beverages, Report of the Appellate Body, Oct. 4, 1996, WT/DS8/AB/R, at 20.

[63] Brazil - Export Financing Programme for Aircraft - Recourse to Arbitration by Brazil under Article 22.6 of the DSU and Article 4.11 of the SCM Agreement, Decision by the Arbitrators, Aug. 28, 2000, para. 3.39. Article XX was not an issue in this case, so this analogy is dicta.

It is said that if an environmental trade measure violates Article III, it violates the rights of the exporting country, and perhaps even violates the GATT, but is nevertheless tolerated because of Article XX.

This issue of orientation is noted at the start because it may facilitate understanding of the PPM jurisprudence as presented below. The first section will consider GATT Article I; the next section Article III, and the last section Article XX. A PPM-based import ban will violate Article XI -- just as a non-PPM import ban would -- and so the Article XI caselaw has not directly addressed PPMs.

Article I

GATT Article I:1 (General Most-Favoured-Nation Treatment) provides that with respect to customs duties, taxes, regulations, and import rules, any advantage or favor granted by a Party to any product shall be accorded immediately and unconditionally to the "like" product of all other Parties. What this means is that a WTO member government cannot discriminate by treating the product of one WTO member country better than the like product of another member country. The decision as to whether two products are "like" will often be pivotal since Article I does not prohibit differential treatment of unlike products.

One of the earliest GATT decisions considered whether a PPM violated Article I. The case was "Belgian Family Allowances" in 1952.[64] At issue was a Belgian tax on imports purchased by local government bodies. The 7.5 percent tax was used for the family allowance program in Belgium which was otherwise funded by employer taxes. Not every country was subject to the import tax however. An exemption was available for countries that imposed an employer tax for family allowances similar to Belgium's tax. The two plaintiff governments, Denmark and Norway, complained that the tax violated Article I because an exemption had been given to Sweden but not to them. The panel sided with the plaintiffs but on broader grounds. Since Belgium had granted

64 Belgian Family Allowances, GATT, BISD 1S/59.

the exemption to some GATT parties, the panel reasoned, Article I required that it grant the exemption to every other GATT party *regardless* of whether a government had a family allowance system similar to that of Belgium.[65]

To reframe this case, Belgium was levying a PPM tax on other countries based on a (foreign) government policy standard. In the panel's view, the nature of an exporting country's family allowance program was "irrelevant" to GATT Article I, which did not permit discrimination based on that factor.[66] Because Belgium did not claim an Article XX exception, the case ended with the finding of the MFN violation.

No other Article I cases involving non-product-related PPMs ensued before the advent of the WTO. In a 1981 decision, a panel considered a product-related PPM and found that the distinction was not enough to prevent two similar products from being deemed "like."[67] At issue was whether different methods of cultivation and processing of coffee beans justified different tariff classifications for various types of unroasted coffee. The panel said no.

The WTO has considered two GATT Article I disputes involving PPMs, both about automobiles. In the Indonesia Automobile case, Japan, the European Communities, and the United States complained that Indonesia applied higher customs duties and sales taxes to imported products when the exporting manufacturer did not utilize a sufficient amount of Indonesian parts and personnel.[68] In the Canada case, Japan and the European Communities complained that Canada provided an import duty exemption for an eligible corporation conditioned on its having a manufacturing presence and sufficient

65 *Id.*, paras. 3, 6.

66 *Id.*, para. 3.

67 Spain - Tariff Treatment of Unroasted Coffee, GATT, BISD 28S/102, para. 4.11.

68 Indonesia - Certain Measures Affecting the Automobile Industry, Report of the Panel [hereinafter Indonesia Automobile Panel Report], July 2, 1998, WT/DS54/R. This case was not appealed.

value-added in Canada.[69] In both cases, the panels found a violation of GATT Article I. No Article XX exception was invoked.

In the Indonesia Automobile decision, the panel held that under Article I, an advantage "cannot be made conditional on any criteria that is not related to the imported product itself."[70] Elaborating on this point, the panel stated that "In the GATT/WTO, the right of Members cannot be made dependent upon, conditional on or even affected by, any private contractual obligations in place."[71] To reframe this case, Indonesia was levying a PPM tax and tariff based on producer characteristics and domestic content, and that was deemed an MFN violation.

In the Canada automotive decision, the panel held that Article I was being violated, but adopted a more nuanced interpretation of the Article I discipline. Specifically, the panel said: "We therefore do not believe that . . . Article I:1 must be interpreted to mean that making an advantage conditional on criteria not related to the imported product itself is *per se* inconsistent with Article I:1, irrespective of whether and how such criteria relate to the origin of the imported products."[72] In other words, the panel suggested that truly origin-neutral conditions might be permissible under Article I. The panel took care to distinguish the holdings in the Belgian Family Allowances and Indonesia Automobile cases, both of which it viewed as relating to origin-based discrimination. In the instant case, the panel concluded that the conditions were not origin-neutral, and so Article I was being violated. On appeal, the Appellate Body upheld the panel's finding of the Article I:1 violation, and did not address the panel's interpretive point.

Here is a summary of the caselaw showing how GATT Article I addresses PPMs. A government policy standard violates MFN because it is origin-

[69] Canada, Certain Measures Affecting the Automotive Industry, Report of the Panel [hereinafter Canada Automotive Report], Feb. 11, 2000, WT/DS/139/R.

[70] Indonesia Automobile Panel Report, *supra* note 68, para. 14.143.

[71] Indonesia Automobile Panel Report, *supra* note 68, para. 14.145.

[72] Canada Automotive Report, *supra* note 69, para. 10.24. *See also* paras. 10.29, 10.30.

contingent.[73] A producer characteristics standard was held a violation in the Indonesia and Canada automobile cases, but the latter panel suggested that PPMs are not *per se* violations of MFN. No how-produced standard has yet been reviewed under Article I.

Article III

GATT Article III (National Treatment) contains disciplines for domestic taxation and regulation. Under Article III:2, imported products shall not be subject to taxes of any kind in excess of those applied to like domestic products. Under Article III:4, imported products shall be accorded treatment no less favorable than that accorded to like products of national origin. In addition, Article III:1 provides that internal taxes and regulations affecting the internal sale, 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."

It is sometimes alleged that the drafters of Article III did not contemplate PPMs or, if they did, intended to disallow them. Yet the text of Article III suggests otherwise. As noted above, Article III:1 addresses regulations requiring the mixture or processing of products, but states only that it should not afford protection to domestic production. The implication is that mixture or processing regulations that do not afford protection to domestic production are not prohibited. This interpretation is confirmed by looking at other provisions in Article III that address mixture and processing. For example, Article III:5 prohibits mixture/processing regulations linked to domestic content. Article III:7 prohibits mixture/processing regulations that seek to allocate proportions among external sources of supply. If all mixture/processing

[73] It is interesting to note that in 1927, the Swedish delegation to the World Economic Conference pointed out that the MFN principle might be evaded by an unfounded distinction (between similar kinds of goods) such as the "measures taken by the authorities of the exporting State." LEAGUE OF NATIONS, 1 REPORT AND PROCEEDINGS OF THE WORLD ECONOMIC CONFERENCE 235–36 (1927), League Doc. C.356.M.129.1927.II.

regulations were prohibited, then why would Article III have three prohibitions aimed at particular kinds of mixture/processing regulations?

Suppose that a government had a regulation prohibiting the sale of lumber unless at least 95 percent of its weight came from sustainably harvested timber. This how-produced PPM would specify a minimum proportion for processing. Written in this way, such a measure would not seem a *per se* violation of Article III.

Nevertheless, as shown below, panels adjudicating Article III have objected to PPMs. in the few cases where PPMs were reviewed. Under the GATT, there were four cases, all against the United States. Under the WTO, only two cases have arisen, but other decisions bear on how Article III will be applied to PPMs.

The earliest GATT decision came in 1991, and is known as the first Tuna-Dolphin decision.[74] At that time, the United States imposed an import ban on tuna from countries that did not have a regulatory regime to protect dolphins comparable to the U.S. regime. Mexico, one of the embargoed countries, complained that this law violated Article III. The U.S. import ban was a government policy standard that looked at Mexico's laws. (Indeed, it went further than that by requiring Mexico to keep its overall dolphin killing rate no more than 25 percent higher than the United States' annual rate.[75]) The panel ruled that Article III "covers only those measures that are applied to the product as such," and so the U.S. measure regarding dolphins did not fit Article III because this PPM "could not possibly affect tuna as a product."[76] The panel

[74] *See* Henry L. Thaggert, *A Closer Look at the Tuna-Dolphin Case: "Like Products" and "Extrajurisdictionality" in the Trade and Environment Context, in* 1 TRADE AND THE ENVIRONMENT: THE SEARCH FOR BALANCE 69 (James Cameron et al. eds., 1994).

[75] This is not a producer characteristics standard because no solitary producer can meet it on its own. It is also not a how-produced standard since the import ban is country-wide.

[76] United States - Restrictions on Imports of Tuna [hereinafter Tuna-Dolphin I Report], GATT, BISD 39S/155, paras. 5.14, 5.15 (not adopted).

went on to say that if the U.S. measure were covered by Article III, it would constitute a violation because the United States treatment to Mexico cannot be predicated on whether or not the incidental taking of dolphins by Mexican vessels corresponds to that of U.S.-flag vessels. This judgment was not adopted by the GATT Council and thus has no legal status. When the matter was debated before the Council in 1992, the European Commission argued that adoption of the Tuna-Dolphin report was "a necessary first step in clarifying the relationship between environmental policies and GATT provisions."[77]

In the next case -- U.S. Alcoholic Beverages -- Canada complained about an excise tax credit in the State of Minnesota for small beer breweries whether domestic or foreign.[78] The panel held that beer from micro-breweries is a like product to beer from large breweries, and so a tax that distinguished the two violated Article III:2.[79] The tax credit was a producer characteristics PPM.

The second Tuna-Dolphin decision came next and it too was not adopted. Its holding was similar to that of the first Tuna-Dolphin panel. The second panel held that Article III did not apply to laws "related to policies or practices that could not affect the product as such . . . ."[80]

The last pre-WTO decision was U.S. Automobile Taxes and it too was not adopted. The European Communities lodged several complaints, one of which was that the U.S. Corporate Average Fuel Economy (CAFE) regulation violated Article III:4 because it was based on a fleet averaging method that treated domestic and foreign-made autos separately. The panel ruled that "Article III:4 does not permit treatment of an imported product less favourable

[77] Minutes of Meeting held on 18 February 1992, GATT Doc. C/M/254, at 23.

[78] United States - Measures Affecting Alcoholic and Malt Beverages [hereinafter U.S. Alcoholic Beverages Report], GATT, BISD 39S/206. This was only one of numerous complaints in the case. For purposes of its decision, the panel assumed that the Minnesota tax credit was available to Canadian producers. *Id.* para. 5.19.

[79] *Id.* From the report of the case, the U.S. Trade Representative made little effort to defend Minnesota's law.

[80] United States - Restrictions on Imports of Tuna [hereinafter Tuna-Dolphin II Report], June 16, 1994, 33 I.L.M. 842, para. 5.8 (not adopted).

than that accorded to a like domestic product, based on factors not directly relating to the product as such."[81] Thus, fleet averaging itself violated Article III because it was "based on the ownership or control relationship of the car manufacturer" and therefore "did not relate to cars as products."[82]

The first WTO case, U.S. Gasoline, considered a PPM regulation for gasoline pollution. Venezuela and Brazil complained that the regulation (which required reduction from a pollution baseline) was discriminatory because it assigned foreign producers a standard baseline while giving domestic refiners an individual baseline. Because foreign gasoline was generally higher-polluting, the assignment of a standard baseline required some of those producers to undertake greater reductions in polluting ingredients than if they had been given an individual baseline. The U.S. regulation was undoubtedly a violation of national treatment but in so finding, the panel issued a broad decision that built on the U.S. Alcoholic Beverages and Automobile Taxes decisions. Noting that the U.S. regulation had been defended on the ground that data from foreign producers was unverifiable, the panel held that Article III:4 "does not allow less favorable treatment dependent on the characteristics of the producer and the nature of the data held by it."[83] This holding was not appealed.

The second WTO case was Indonesia Automobile. The panel found an Article III:2 violation because the tax measures were based on nationality and origin "or other factors not related to the product itself . . . ."[84] This was similar to the panel's ruling on Article I.

The Japan Alcoholic Beverages panel did not consider a PPM, but in rejecting the so-called "aim-and-effect" test, its holding would seem to implicate all PPMs as GATT Article III violations. Aim-and-effect was a treaty

[81] United States - Taxes on Automobiles [hereinafter U.S. Automobile Taxes Report], Sept. 29, 1994, GATT Doc. DS31/R, para. 5.54 (not adopted).

[82] *Id.* para. 5.55.

[83] United States - Standards for Reformulated and Conventional Gasoline, Report of the Panel [hereinafter Gasoline Panel Report], Jan. 29, 1996, WT/DS2R, para. 6.11.

[84] Indonesia Automobile Panel Report, *supra* note 68, para. 14.112.

interpretation developed in GATT caselaw and commentary during the 1990s which sought to define product likeness in a way so as to prevent Article III from unnecessarily infringing on national regulatory autonomy.[85] As the U.S. Alcoholic Beverages panel explained in 1992, "once products are designated like products, a regulatory product distinction, e.g., for standardization or environmental purposes, becomes inconsistent with Article III even if the regulation is not *applied so as to afford protection to domestic production.*"[86] Nevertheless, the first time this test was invoked in the WTO, in Japan Alcoholic Beverages, the panel rejected such a test in Article III:2 in favor of an analysis of the physical and functional likeness of two products.[87] The Appellate Body upheld the panel on this point and in a later decision (Bananas) stated its rejection of "aim-and-effect" explicitly.[88] Although it was not propounded as a way to defend PPMs, the aim-and-effect test could have provided a doctrinal basis for distinguishing two otherwise like products that differ only in their conformity to the PPM. Without the aim-and-effect test, a PPM-complaint domestic product may be easily deemed a "like" product to a PPM-non-compliant imported product. If so, an Article III violation will ensue when government action denies the imported product an equal opportunity to be sold in the domestic market.

[85] Robert E. Hudec, *GATT/WTO Constraints on National Regulation: Requiem for an "Aims and Effects" Test,* 32 INTERNATIONAL LAWYER 619 (1998). One intellectual foundation of this test can be found in a paper by two GATT Secretariat officials in 1989. *See* Frieder Roessler, *The Constitutional Function of the Multilateral Trade Order, in* THE LEGAL STRUCTURE, FUNCTIONS, & LIMITS OF THE WORLD TRADE ORDER. A COLLECTION OF ESSAYS BY FRIEDER ROESSLER 109, 127-30 (2000).

[86] U.S. Alcoholic Beverages Report, *supra* note 78, para. 5.72.

[87] Japan - Taxes on Alcoholic Beverages, Report of the Panel, July 11, 1996, WT/DS8/R, para. 6.17. One stated reason for doing so was that if protection of health could be accomplished without violating Article III, that could "circumvent" Article XX which requires governments to show that a health measure is necessary. The panel did not explain why non-violation of Article III circumvents Article XX.

[88] *See* European Communities - Regime for the Importation, Sale and Distribution of Bananas, Report of the Appellate Body, Sept. 9, 1997, WT/DS27/AB/R, para. 241 (making clear that the Appellate Body had rejected this test).

The most recent Article III decision came in the European Communities Asbestos case. In response to a complaint by Canada, the panel found that a French ban on asbestos violated Article III:4 because a Canadian asbestos fiber was a like product to non-imported substitute fiber that was permitted. In a surprising decision, the panel held that the risk to human health or life could not be a factor in determining whether two products were "like" under Article III because that would allow a government "to avoid the obligations in Article XX . . . ."[89] This was not a PPM decision; the French ban was based on the dangers of the product to the user. But if this new interpretation is upheld, it would make it even harder to defend a PPM against an Article III challenge.

In summary, the textual ambiguities in Article III are being resolved in a way unfavorable to PPMs. A producer characteristics standard was held a violation in U.S. Alcoholic Beverages, U.S. Automobile Taxes, U.S. Gasoline, and Indonesia Automobile. The first Tuna-Dolphin decision suggested that a government policy standard would violate Article III if Article III were applicable. No how-produced standard has been tested, but WTO jurisprudence points to the likelihood that such a standard would be deemed a national treatment violation.

It is interesting to note that in a recent article, Robert Howse and Donald Regan contend that the text of Article III provides no support for the product/process distinction or the proposition that Article III prohibits all process measures. The authors contrast origin-neutral process measures (which would include how-produced standards as defined here) with country-based measures (which would include government policy standards as defined here) and say that while Article III prohibits the country-based measure, it does not prohibit origin-neutral measures that distinguish products according to their production process. In their view, WTO panels remain free in applying Article III to consider the aim and effect of a regulatory PPM in order to determine the

[89] European Communities - Measures Affecting Asbestos and Asbestos Containing Products, Report of the Panel, Sept. 18, 2000, WT/DS135/R, para. 8.130. This decision is now under appeal.

legality of differential treatment of PPM-compliant and non-compliant products.[90]

Article XX

GATT Article XX lists ten exceptions to GATT disciplines. These exceptions are "[s]ubject to the requirement that such measures are not applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade. . . ." This requirement is now known as the "chapeau." Two of the exceptions would be available for environmental measures -- paragraph (b) for measures "necessary to protect human, animal or plant life or health," and paragraph (g) for 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 will be central to an analysis of PPMs because, as discussed above, many PPMs will violate Articles I, III, or XI.

The first Article XX PPM case was United States Automotive Spring Assemblies in 1983. In this case, Canada complained about an import exclusion order against certain automotive spring assemblies produced in violation of a valid U.S. patent and without a license from the patent holder. The panel ruled that the exclusion order was necessary under the Article XX(d) exception and met the terms of the chapeau.[91]

[90] Howse & Regan, *supra* note 41, at 264–68. In a paper that predates some of the recent WTO jurisprudence, two commentators suggested that when based on broadly shared consumer preferences, PPM distinctions might not violate Article III. Marco Bronckers & Natalie McNelis, *Rethinking the "Like Product" Definition in GATT 1994: Anti-Dumping and Environmental Protection, in* REGULATORY BARRIERS AND THE PRINCIPLE OF NON-DISCRIMINATION IN WORLD TRADE LAW, *supra* note 39, at 345, 376–77.

[91] United States - Imports of Certain Automotive Spring Assemblies, GATT, BISD 30S/107, paras. 55–56, 59–61. GATT Article XX(d) provides an exception for measures necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of the GATT, including those relating to customs enforcement, the enforcement of certain monopolies, the protection of patents, trademarks, and copyrights, and the prevention of deceptive practices.

In the Tuna-Dolphin cases, two panels held that the PPM-based import bans did not qualify for an Article XX exception. The first decision addressed the import ban of tuna from Mexico. The panel asserted that Article XX(b) did not cover such an "extra-jurisdictional" measure to safeguard dolphins outside the United States. According to the panel, if Article XX(b) were applied in this way, the importing government "could unilaterally determine the life or health protection policies from which other contracting parties could not deviate without jeopardizing their *rights* under the General Agreement."[92] The second decision focused on the intermediary import ban of tuna from certain European countries. This tuna was being barred because the implicated governments had not prohibited the importation of tuna from Mexico (or other countries targeted by the U.S. embargo). As the U.S. import ban was predicated on the policy of the European tuna-consuming countries, it was a government policy standard. Reviewing the import ban under Article XX(g), the panel pointed out that tuna imports were prohibited "whether or not the particular tuna was harvested in a manner that harmed or could harm dolphins . . . ."[93] The primary embargo had the same fault, said the panel, and both types of embargo "were taken so as to force other countries to change their policies with respect to persons or things within their own jurisdiction," and therefore did not meet the terms of XX(g).[94] The panel declined to interpret Article XX(g) in a way so as to permit such a measure because "the balance of rights and obligations among contracting parties, in particular the right of access to market, would be seriously impaired."[95] Note that the panel assumes that the Netherlands Antilles has a "right of access" to the U.S. market that has independent valence in interpreting Article XX.

[92] Tuna-Dolphin I Report, *supra* note 76, para. 5.27 (emphasis added). As many commentators noted, this point was circular since Mexico's rights to have its tuna accepted by the United States could not be determined independently of application of Article XX. The panel made a similar ruling regarding Article XX(g).

[93] Tuna-Dolphin II Report, *supra* note 80, para. 5.23.

[94] Tuna-Dolphin II Report, *supra* note 80, para. 5.24. The panel uses the term "countries" as a synonym for governments.

[95] *Id.* para. 5.26.

The second panel seemed to be trying to correct the overreaching by the first panel, but the second decision was too ambiguous to be a guidepost. One leading GATT commentator, Robert Hudec, read the decision as saying that the U.S. law was a GATT violation because of its coercive design, but that a rewritten law barring imports of fish caught by dolphin-unsafe methods could be justified under Article XX.[96] Yet other commentators read the decision as prohibiting all PPMs directed at foreign countries.

In U.S. Automobile Taxes, the panel held that the fleet averaging method could meet the requirements in paragraph (g) of Article XX.[97] As noted above, fleet averaging violated GATT's national treatment discipline because the U.S. regulation was dependent on factors not directly relating to the product as a product. But Article XX(g) does not preclude such factors, according to the panel. Despite this favorable holding, the panel ruled that another feature of the U.S. measure -- separate foreign fleet accounting -- prevented the U.S. measure from qualifying under Article XX(g). To reframe this holding, the panel ruled that Article XX could potentially permit a producer characteristics PPM. The GATT Council did not adopt this decision however.

In the U.S. Gasoline case, the Appellate Body concluded that the U.S. baseline rule fit within the terms of paragraph (g), but found that its application violated the Article XX chapeau.[98] This was the first adopted decision that an environmental PPM could fit within one of the Article XX exceptions. The measure at issue was a producer characteristics PPM. The marketability of the gasoline depended on the foreign or domestic status of the producer and on achieving reductions from an assigned baseline. (It should be noted that none of the parties of the dispute characterized this measure as a PPM.)

[96] Robert E. Hudec, *GATT Legal Restraints on the Use of Trade Measures Against Foreign Environmental Practices, in* 2 FAIR TRADE AND HARMONIZATION 95, 119, 151 (Jagdish N. Bhagwati & Robert E. Hudec eds., 1996).

[97] U.S. Automobile Taxes Report, *supra* note 81, paras. 5.65–5.66.

[98] Appellate Body Gasoline Report, *supra* note 60, at 13–29.

In complying with the WTO decision, the U.S. government changed its regulation to allow foreign refiners the option of applying for and using an individual baseline.[99] The ability to sell gasoline would still be based on producer characteristics, but the discrimination against foreign producers was removed. To assure compliance, foreign refiners had to agree to a set of enforcement measures including unannounced inspections by U.S. regulators. Under the new regulation, the ability to sell a particular gallon of gasoline depends on whether the producer has met its baseline requirements. Thus, gasoline from one producer could be barred while identical gasoline from another producer is permitted.

The U.S. Shrimp-Turtle case involved an import ban on shrimp from countries that did not have a turtle conservation regime comparable to that of the United States.[100] The U.S. law is complex: it blends a how-produced standard, a government policy standard, and a review of the actual performance of the foreign shrimping fleet in safeguarding turtles. At the time of the case, most of the complaining countries -- India, Malaysia, Pakistan, and Thailand -- were under a shrimp embargo linked to a requirement that they enforce comprehensive requirements regarding the use of turtle excluder devices by their fishing vessels. Thus, in this adjudication, the U.S. measure was framed as a government policy standard.

[99] Regulation of Fuels and Fuel Additives: Baseline Requirements for Gasoline Produced by Foreign Refiners, 62 FEDERAL REGISTER 45,533 (1997). This rule was challenged in U.S. court in part on the argument that the U.S. Environmental Protection Agency should not have considered U.S. obligations under the WTO in administering the statute. The court upheld the Agency's statutory interpretation. Warren Corporation v. EPA, 159 F.3d 616, 624.

[100] All four of the plaintiff countries had a turtle conservation regime in place. Indeed, two of them (India and Pakistan) had imposed unilateral trade bans on endangered sea turtles before the adoption in 1973 of the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES). United States - Import Prohibitions of Certain Shrimp and Shrimp Products, Report of the Panel [hereinafter Shrimp-Turtle Panel Report], May 15, 1998, paras. 3.4, 3.11.

The WTO panel held that the import ban could not be justified by Article XX. In particular, the panel declared that the scope of Article XX did not extend to measures that condition market access on the adoption of particular conservation policies by the government seeking access for its nationals.[101] The panel was troubled by the fact that the U.S. government was requiring the plaintiff countries to adopt prescribed policies for *all* production, not just for exports to the United States. The panel found this situation unacceptable because if the United States did this, so could other countries, and if the unilateral requirements were inconsistent, "it would be impossible for exporting Members to comply at the same time with multiple conflicting policy requirements."[102] The panel contrasted such a regulation with a ban on the import of products made by prison labor. That ban applies only to the products of such labor, not to the exporting country's *policy* on prison labor. In summarizing its holding, the panel explained that its decision did "not imply that recourse to unilateral measures is always excluded, particularly after serious attempts have been made to negotiate. . . ."[103]

The Appellate Body upheld the panel's conclusion that the U.S. import ban violated the GATT, but modified the reasoning substantially. Unlike the panel,

[101] *Id.*, paras. 7.26, 7.45, 7.50, 7.51.

[102] Shrimp-Turtle Panel Report, *supra* note 100, para. 7.45. The panel's important point deserves more attention. Suppose that Country A forbids the importation of shrimp from countries that do not require the use of a Turtle Excluder Device (TED) while Country B forbids the importation of shrimp from countries that do not require the use of a Turtle Untrapping Device (TUD). In that hypothetical, economic actors in Country C would not be able to sell simultaneously to A and B. One can make the hypothetical more troublesome by assuming that A is the leading producer of TEDs and B is the leading producer of TUDs.

[103] *Id.* para. 7.61. David D. Caron & Hans Rudolf Trüeb, *Protecting Trade and Turtles: The WTO and the Coherency of International Law*, TRANSLEX 3,5 (Dec. 1998).

the Appellate Body found that the import ban did fit within the scope of Article XX and was provisionally justified by XX(g).[104] Specifically, the Appellate Body stated that the "means and ends relationship" of banning shrimp imports and protecting turtles was "close and real," and the trade measure used was "not disproportionately wide in its scope and reach . . . ."[105] Nevertheless, the U.S. measure was flawed, the Appellate Body said, because the measure failed to meet the requirements of the Article XX chapeau. One major flaw was that the U.S. certification process "does not allow for any inquiry into the appropriateness of the regulatory program for the conditions prevailing in those exporting countries."[106] Other flaws included inflexibility in administrative determinations and no opportunity for the embargoed country government to appeal.[107] To reframe the point, the Appellate Body seems to be saying that it is not necessarily a GATT violation to impose a government policy PPM on exporting countries, but in doing so the regulator must be sensitive to the conditions in each country, and the administrative process must meet minimum standards of transparency and procedural fairness. This result does not conflict with Belgian Family Allowances, which was not an Article XX case. But the new ruling shows a more sophisticated consideration of discrimination not present in the Belgian Family Allowances judgment.

The Appellate Body also noted critically that the United States was not a party to the Law of the Sea treaty or to the Convention on Biological Diversity, and thus was not making use of the international cooperative mechanisms that did exist.[108] Furthermore, according to the Appellate Body, the U.S. government had not sought to negotiate a treaty with affected countries before imposing the import embargo.[109] The U.S. government admitted this to some extent, but

[104] Appellate Body Shrimp-Turtle Report, *supra* note 61, paras. 121, 141, 145, 149. The Appellate Body found that the U.S. measure was made effective in conjunction with a restriction on domestic production (harvesting) of shrimp -- that is, the domestic PPM and imported-product PPM were applied evenhandedly. *Id.* para. 144.

[105] *Id.* para. 141.

[106] *Id.* para. 165.

[107] *Id.* paras. 177–82.

[108] *Id.* para. 171.

[109] *Id.* paras. 166, 171.

pointed out that its subsequent efforts to negotiate a treaty were spurned by the Asian country plaintiffs.

Although the Appellate Body did not say that the shrimp-turtle PPM was GATT-legal, the inferences in the decision are affirmative for PPMs. The lower panel had asserted that this kind of PPM fell outside the scope of Article XX, and the Appellate Body reversed that conclusion. Then the Appellate Body found that the import ban fit paragraph (g), but failed to comply with the chapeau. Had the Appellate Body believed that the GATT prohibits non-product-related PPMs, then it could have said that in one sentence. The fact that the Appellate Body reviewed the PPM carefully and gave specific criticisms of how the U.S. government was applying the law demonstrates that PPMs are potentially justifiable under Article XX. Although not all PPMs will be covered by a GATT General Exception, environmental PPMs will be.

In complying with the WTO decision, the U.S. Department of State revised its regulation to provide more due process to foreign governments and to permit shrimp imports so long as the shrimp were harvested by vessels using turtle excluder devices.[110] In other words, the U.S. government shifted the implementation of the statute from a government policy standard to a how-produced standard. Although this shift may not have been proper under U.S. law,[111] the new policy remains in force. In fall 2000, Malaysia asked the WTO Dispute Settlement Body to consider whether the U.S. compliance meets WTO requirements.[112]

The Asbestos case does not involve a PPM, but it was the first ruling by a WTO panel that an import measure could be justified by Article XX(b). In applying this exception, the panel held that a health measure could be deemed

[110] Notice of Proposed Revisions to Guidelines for the Implementation of Section 609 of Public Law 101-162 Relating to the Protection of Sea Turtles in Shrimp Trawl Fishing Operations, 64 FEDERAL REGISTER 14,481 (1999).

[111] Rossella Brevetti, *State Department Considers Options After Court Ruling on Shrimp Import Ban,* BNA DAILY REPORT FOR EXECUTIVES, Aug. 18, 2000, at A-8.

[112] *Malaysia Poised to Fight U.S. Turtle Protection After Talks with U.S.,* INSIDE U.S. TRADE, Oct. 6, 2000, at 12.

"necessary" under this provision if there were not other measures consistent (or less inconsistent) with the GATT that could achieve the defendant government's health policy objectives.[113] This clarified that the application of Article XX(b) does not utilize a least-trade-restrictive test.[114] This arduous test had been one of the recommendations of Agenda 21 which states that "Should trade policy measures be found necessary for the enforcement of environmental policies, certain principles and rules should apply . . . [including] the principle that the trade measure chosen should be the least trade-restrictive necessary to achieve the objectives."[115] So in this respect, the WTO is greener than Agenda 21.

In summary, the Article XX exceptions apply to PPMs. Indeed, no adopted GATT or WTO decision has suggested that PPMs are outside the scope of Article XX. The decisions in the WTO Gasoline and Shrimp-Turtle cases against the environmental measure did not turn on its PPM status. Although the Shrimp-Turtle panel criticized the coerciveness of a government policy standard, the Appellate Body in Shrimp-Turtle did not perceive this regulatory approach as legally fatal. None of the environmental cases has involved a how-produced standard. The first review of such a standard may occur in the impending examination of U.S. compliance in the Shrimp-Turtle dispute.

Restatement of the Law

For environmental PPMs, the most important WTO law is found in GATT Article XX and can be restated as follows: The WTO/GATT does not prohibit environmental PPMs *as such*. PPM-based import bans may be inconsistent with GATT Articles I, III, or XI, but if undertaken for an environmental purpose, such measures may qualify for an Article XX exception. Both the

[113] European Communities - Measures Affecting Asbestos and Asbestos Containing Products, *supra* note 89, paras. 8.173, 8.179, 8.183, 8.199, 8.204, 8.206. Furthermore, the panel suggests that each government can determine what level of risk it wants to assure. *Id.* para. 8.175 n. 119.

[114] The judgment of the U.S. Gasoline Panel also suggests a least-GATT-inconsistent rather than a least-trade-restrictive test. Gasoline Panel Report, *supra* note 83, para. 6.24.

[115] EARTH SUMMIT AGENDA 21, para. 2.22(i).

government policy standard and the producer characteristics standard are potentially justifiable under Article XX, and will receive scrutiny as to procedural fairness and environmental justification. A how-produced standard has not been tested and should present a diminished problem under GATT law.

In its two Article XX environmental decisions, the Appellate Body breathed life into the Article XX chapeau which can serve as a bulwark against unfair and protectionist measures.[116] The rigorous chapeau review in Shrimp-Turtle may develop as a key foundation of the new law of PPMs.

This paper is focused on environmental PPMs, but the question arises whether the same conclusion -- that the WTO does not prohibit environmental PPMs -- applies to other kinds of PPMs. For example, what would be the legal status of an import ban on a rug made by indentured children, or on fur from a country that permits leg hold traps, or on pharmaceuticals tested on animals?[117] The answer is not clear. In Shrimp-Turtle, the Appellate Body saw a "nexus" between the locus of the environmentally-harmful shrimping and the U.S. interest in conserving migratory sea turtles.[118] Such a nexus should be easy to find for environmental issues when the two litigant countries share an ecosystem. But for other issues, the required nexus may not exist.

It should also be noted that PPMs address only one part of the product cycle, and the legal conclusions presented here might not be applicable to regulations that extend beyond production. For example, importation can be made contingent on a variety of post-production practices. Goods that are stolen, expropriated, mislabeled, or packaged in certain ways might be stopped at the border. Similarly, importation can be contingent on how a product is to be

[116] *See* Chang, *supra* note 42, at 2172, 2208 (noting that the Article XX chapeau contains clauses designed to prevent abuse of the Exceptions).

[117] *See, e.g.*, Adelle Blackett, *Whither Social Clause? Human Rights, Trade Theory and Treaty Interpretation*, 31 COLUMBIA HUMAN RIGHTS LAW REVIEW 1 (1999); ROYAL SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS, WTO–FOOD FOR THOUGHT–FARM ANIMAL WELFARE AND THE WTO (1999).

[118] Appellate Body Shrimp-Turtle Report, *supra* note 61, para. 133.

used or how it is to be disposed.[119] Importation can also be contingent on whether exportation is legal in the country of export. Note that the common feature in all of these requirements is that two otherwise like products are treated differently.

Although this paper addresses only regulations on import, many of the same legal issues arise in export regulations. For example, an export ban on hazardous waste to countries that are not parties to a treaty would be a violation of GATT Article XI that would be tested under Article XX.

In conclusion, Chapter 3 explicated the WTO law of PPMs and demonstrated the falsity of the myth that PPMs are illegal under the WTO. Chapter 4 will discuss the implications of that insight for making progress in resolving trade and environment tensions.

[119] For example, in the United States, there is a high tariff on hand-woven wool fabrics, but no tariff when such fabrics are to be used or sold by a religious institution. Harmonized Tariff Schedule of the United States, subheading 9810.00.20.

Chapter 4

Debunking the Myth and Moving Forward

The argument that environmental PPMs violate the WTO has not had the intended effect. Rather than stamping out PPMs, it has prevented a reasoned discourse about how to distinguish appropriate from inappropriate PPMs. Little is being done to deal with the root causes of such trade restrictions.

Without any agreement on PPMs, governments have found it harder to move ahead on any of the other elements of the trade and environment work program at the WTO. For example, many commentators and governments have suggested that the first priority should be to address the use of trade measures in multilateral environmental agreements (MEAs). Yet since some of these measures are PPMs, the confusion about their legal status spills over into the debate about MEAs.

When negotiators do not share a common legal understanding about the subject of a negotiation that will tend to impede a successful resolution. It is hard to bargain in the shadow of the law when stakeholders have widely divergent views on what the law is. Because the governments most opposed to PPMs believe (incorrectly) that they are illegal, they have adopted an implacable and adversarial stance toward PPMs that may undermine settlement of conflicts.

But it is not just governments opposed to PPMs who are victims of the myth that PPMs are illegal. Some of the governments that recognize the need for PPMs are also confused about WTO law. Therefore, these governments tend to frame their proposals as amending or interpreting GATT to permit multilateral PPMs. Yet because WTO decisionmaking is consensual, such an amendment will be impossible, and the lack of receptivity reinforces the perception that "trade and environment" issues are irresolvable.

The divergent views about the status of PPMs has undermined support for the WTO. Developing country officials -- who may believe the myth that the WTO prohibits PPMs -- perceive the continued use of PPMs by the United States as proof that the WTO remains power-based rather than rule-based. Proponents of using environmental PPMs may view the WTO negatively because it may rule against such laws in favor of commercial interests.[120] This is bad for the trade regime, since alienated environmentalists will undermine public support for the WTO. But the schism between environmentalists and the trading system is also bad for environmental policy. Until the status of PPMs is properly understood, many environmentalists are not going to pay much attention to the ways that WTO rules and trade itself can promote opportunities for better environmental policy. Therefore, win-win opportunities may be missed.

If stakeholders shared a common understanding of the WTO law of PPMs, it might be possible to begin to bridge the gap between expectations and reality, between commerce and conservation, and between the sovereignty of the producer and the sovereignty of the consumer. When a foreign environmental practice has an adverse environmental impact at home, the WTO cannot blindly demand that consumers accept foreign products of that process in the interest of promoting greater trade. What the WTO can do, however, is to erect effective disciplines for assuring that PPMs have an environmental justification and are applied in a reasonable manner. The current implementation of Article XX is not ideal. Yet replacing it with something better will not be easy because the topic of PPMs is emotionally charged. The proponents of PPMs should admit that they sometimes impose global costs and the opponents should admit that PPMs sometimes generate global benefits.

The next two sections make suggestions for disciplining and managing PPMs. Disciplines are needed to screen out improper PPMs. Better global

[120] Peter Fugazzotto & Todd Steiner, SLAIN BY TRADE. THE ATTACK OF THE WORLD TRADE ORGANIZATION ON SEA TURTLES AND THE US ENDANGERED SPECIES ACT (1998).

management is needed to resolve the transborder problems that give rise to PPMs.

Disciplining PPMs

We need effective disciplines against ill-conceived environmental PPMs applied to imports. The worst abuse is a protectionist PPM, and that should be prohibited. So should PPMs that discriminate in an arbitrary or unjustifiable way. International rules should strongly discourage PPMs that prescribe inappropriate policies and PPMs that impede intergovernmental cooperation. Some of these factors are within the competence of the trade regime, while others will require inter-regime cooperation.

It is often said that a key distinction is multilateral versus unilateral PPMs. Yet this distinction can be misleading because in reality there are many different shades of multilateralism. A treaty can require a PPM -- for example, the Montreal Protocol on Ozone forbids the importation of controlled substances from States that are not a party to the Protocol (or have not agreed to be bound by it).[121] A treaty can authorize a PPM -- for example, the Wellington Convention on Driftnets states that each Party may take measures consistent with international law to prohibit the importation of fish caught using a driftnet.[122] A treaty can authorize trade measures in response to actions that undermine the treaty -- for example, the Anadromous Stocks Convention directs the Parties to take appropriate measures to prevent trafficking in anadromous fish taken in violation of the Convention.[123] Furthermore, the Commission administering an environmental treaty can authorize non-product-related PPMs. For example, on several occasions the International Commission for the Conservation of Atlantic Tunas has recommended that

[121] Montreal Protocol on Substances that Deplete the Ozone Layer, *supra* note 25, arts. 4.1, 4.9. This is a government policy standard.

[122] Convention for the Prohibition of Fishing with Long Driftnets in the South Pacific Ocean, Nov. 24, 1989, 29 I.L.M 1454, art. 3(2).

[123] Convention for the Conservation of Anadromous Stocks in the North Pacific Ocean, Feb. 11, 1992, U.S. Senate Treaty Doc. 102–30, art. III:3.

Parties take "non-discriminatory trade restrictive measures" on specified fishery products from listed countries that are adjudged to be violating the Convention.[124] All of these examples might be called multilateral, but they are also unilateral (except for the first) because the PPM-using country is encouraged but not required to use the trade measure. Moreover, under some of the treaties, the trade action is or can be directed at non-parties, so it is not consensually based.

Despite these complexities, the degree of multilateral approval for the PPM ought to be a factor in evaluating its appropriateness. If several countries are applying the PPM, it is much less likely to be protectionist or arbitrary. On the other hand, an environmental treaty can also signal disapproval of a PPM or even preempt unilateral action against Parties in compliance with the treaty.[125] For example, the Inter-American Convention for the Protection and Conservation of Sea Turtles directs Parties to act in accordance with GATT Article XI with respect to the subject matter of the Convention.[126] This seems to imply no import bans since Article XX is not mentioned.

When unilateral PPMs are under review, GATT Article XX will often be the decisive law. If product Y is banned to safeguard a resource Z, the WTO will need to analyze the facts related to both Y and Z. For example, in the Shrimp-Turtle case, the Appellate Body considered shrimping regulation, turtle conservation, and how shrimping affected turtles. Had the U.S. government

[124] For example, see the ICCAT Resolution for an Action Plan to Ensure the Effectiveness of the Conservation Program for the Atlantic Bluefin Tuna, transmitted Jan. 23, 1995.

[125] *See* Robert Howse, *Managing the Interface between International Trade Law and the Regulatory State: What Lessons Should (and Should Not) Be Drawn from the Jurisprudence of the United States Dormant Commerce Clause, in* REGULATORY BARRIERS AND THE PRINCIPLE OF NON-DISCRIMINATION IN WORLD TRADE LAW, *supra* note 39, at 139, 151.

[126] Inter-American Convention for the Protection and Conservation of Sea Turtles, *supra* note 24, art. XV:2.

banned widgets from countries that did not require turtle-safe shrimping, then the Appellate Body's analysis would have been different.[127]

In scrutinizing PPMs, the WTO needs to assess the validity of the environmental purpose underlying the trade measure. As the Appellate Body pointed out in U.S. Gasoline, WTO member governments retain "a large measure of autonomy to determine their own policies on the environment . . ."[128] But the WTO does not have to tolerate an economic motivation for imposing a PPM on imports.[129] For example, it is one thing for the United States to demand that the shrimp it imports be caught in a turtle-safe way so as to safeguard turtles. Yet it is an entirely different matter to seek to "level the playing field" by insisting the foreign producers use the same production practice so as to offset any difference in environmental costs. This latter motivation should not be shielded by GATT's Article XX.

The WTO will never be able to prevent all PPMs, but can discourage the most troublesome ones. The government policy standard should be disfavored because it is coercive and because it abides origin-based discrimination. The producer characteristics standard should be disfavored because such a standard is too easy to tilt against foreign producers. Thus, if a unilateral PPM is to be used, it should be crafted as a how-produced standard that can be aimed directly at the odious production practice.

In calling for the government policy standard to be disfavored, I am not calling for it to be outlawed. There may be circumstances when a how-produced standard is impractical. For example, when raw materials are co-mingled in production, there may be no way to enforce a how-produced PPM. A how-

[127] Under Article XX(g), there would be a highly tenuous "means and ends" relationship between shrimp and widgets. See *supra* note 105. Under the Article XX chapeau, a widget ban might constitute arbitrary discrimination. Why widgets rather than trifles?

[128] Appellate Body Gasoline Report, *supra* note 60, at 30.

[129] Frederic L. Kirgis, Jr., *Effective Pollution Control in Industrialized Countries: International Economic Disincentives, Policy Responses, and the GATT*, MICHIGAN LAW REVIEW 859, 901–02 (1972).

produced standard may also prove to be unsuccessful.[130] One can easily imagine a scenario whereby the how-produced standard does not prevent the environmental damage, but instead only reallocates the product.[131] For example, in a dispute like shrimp-turtle, the turtle-safe shrimp could be shipped to countries that insist on it while the more haphazardly-caught shrimp is shipped elsewhere (at a lower price).

In that scenario, should the WTO permit a more coercive trade measure that might cure the problem? The Shrimp-Turtle panel answered with a categorical "no," and in my view went too far.[132] Yet the legal hurdle for a unilaterally-determined government policy standard ought to be set high. It will rarely be reasonable for one government to require that another government adopt a particular law as a condition for trade.

In addition to examining the PPM itself, the WTO should also examine why it was invoked and how it is applied. The Appellate Body decisions in U.S. Gasoline and Shrimp-Turtle lay down helpful markers for steps that should be taken to attain multilateral cooperation and to accord due process to the exporting country. Some commentators have been critical of these requirements, particularly as they relate to treatymaking. For example, Lakshman Guruswamy contends that the Shrimp-Turtle decision "constitutes a violation of the principle of state sovereignty by attempting to second-guess the manner in which the United States should have conducted treaty negotiations."[133] Virginia Dailey argues that the language of Article XX should not be interpreted to require governments to attempt to negotiate a treaty as a precondition for using a trade measure.[134] In my view, prior efforts to negotiate

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[130] The issues presented in this paragraph arise out of a discussion with Robert Hudec, but the conclusion is mine.

[131] Chang, *supra* note 42, at 2179.

[132] *See* Shrimp-Turtle Panel Report, *supra* note 100, paras. 7.44–7.45.

[133] Lakshman Guruswamy, *The Annihilation of Sea Turtles: World Trade Organization Intransigence and U.S. Equivocation,* 30 ENVIRONMENTAL LAW REPORTER 10261, 10267 (2000).

[134] Virginia Dailey, *Sustainable Development: Reevaluating the Trade Vs. Turtles Conflict at the WTO,* 9 JOURNAL OF TRANSNATIONAL LAW AND POLICY 331, 377 (2000).

a treaty can be relevant to an Article XX review, but the adjudicator should look at the actions of the exporting country too.

Although better disciplines for PPMs can emerge through WTO adjudication, some of the criteria suggested above are not in GATT Article XX and should not be read in. Thus, rather than relying on interpretation, it would be better for the WTO to negotiate new rules so that all governments could participate in this exercise. (Moreover, the opportunities for lawmaking through interpretation are limited by the content and flow of the cases.) Such negotiations could bring to bear other solutions -- for example, capacity building for environmental management -- that would require action outside the WTO.

Managing PPMs

PPMs are not a syndrome, they are a symptom. While it is easy to criticize PPMs as a manifestation of eco-imperialism, that is too simplistic an explanation. PPMs are a symptom of dysfunctions in international environmental governance. Among the biggest problems are poor stewardship of the global commons, lack of accountability for transborder environmental harms, and free riding in efforts to achieve treaties. PPMs are an inevitable response to independent countries at different stages of development and enlightenment who share the same planet. Addressing these root causes would not only obviate many PPMs, but could also improve prospects for economic growth and environmental protection.

The world needs better environmental governance. To boost membership in treaties, rich countries should make more funding and technical assistance available. To improve compliance, treaties need better developed non-compliance mechanisms that use civil society participation as one means to putting pressure on governments to comply. For many issues, however, a treaty might not be achievable. In those circumstances, concerned governments and private actors should put more emphasis on market-based mechanisms such as product labels and certifications, corporate codes and seals, and monitoring processes.

Although the WTO is not responsible for environmental protection, it should become an ally to the various international organizations that do have an environmental mandate. Just before he retired in 1999, WTO Director-General Ruggiero gave a thoughtful speech here at the Graduate Institute in which he said:

> [W]e need to look at the policy challenges we face as pieces of an interconnected puzzle. We can no longer treat human rights, the environment, development, trade, health, or finance as separate sectoral issues, to be addressed through separate policies and institutions.[135]

I could not agree more with this reflection. The WTO needs to work more closely with the U.N. Environment Programme, the governing conferences of multilateral environmental treaties, the World Health Organization, and other U.N. agencies. Authority exists for this in Article V:1 of the WTO Agreement which provides that the "General Council shall make appropriate arrangements for effective cooperation with other intergovernmental organizations that have responsibilities related to those of the WTO."

To improve management of PPMs, the following steps should be taken:

First, the WTO should promote greater transparency of PPMs. This might be done through the Trade Policy Review Mechanism (or through another subsidiary body) with input from relevant international organizations. A WTO review of a particular PPM -- written outside the context of dispute settlement -- might give some impetus to reform within the authoring government. We should not assume that the only way to get a government's attention is to convict it of a WTO violation.

Second, a new trade and environment conflict is often a signal of inadequate environmental cooperation. The WTO could seek to relay that signal to the appropriate multilateral environmental institutions. Analogously, if the environment regime sees a way in which trade negotiations might exacerbate or control an environmental problem, it should communicate that to the WTO.

[135] Renato Ruggiero, "Beyond the Multilateral Trading System," Apr. 1999, available on WTO website.

Third, the WTO should look for opportunities to coordinate its technical assistance on trade with the technical assistance on the environment being sponsored by other international agencies. By doing so, the WTO might encourage better coordination between the trade and environmental officials in participating countries.

Fourth, the WTO needs to clarify its disciplines regarding labeling. PPM labeling offers a potential avenue to avoid trade restrictions by leaving the choice up to retailers and consumers.[136] This is a market friendly response, and should not be discouraged by the WTO.

Finally, although steps like these will help, new trade and environment disputes are almost inevitable. When they occur, the WTO Director-General should be more active in offering mediation and conciliation services.[137] In some cases, like Shrimp-Turtle, both sides were partly right and partly wrong. That dispute should have been settled (or prevented) with the United States giving help to the complaining countries to improve shrimping practices.[138] Another idea -- authored by Gabrielle Marceau -- is for the WTO to establish an Environmental Monitoring Body. This Body would seek a solution to trade and environment conflicts short of formal dispute settlement.[139] The composition of such a Body could include experts from industry and non-governmental organizations.

[136] Of course, a consumer may want to free ride by buying the less expensive product without the label. So a label alone may not be an optimal response to economic externalities. Chang, *supra* note 42, at 2177.

[137] *See* Understanding on Rules and Procedures Governing the Settlement of Disputes, art. 5.6.

[138] *See* Matthew Stilwell, "Applying the EPTSD Framework to Reconcile Trade, Development & Environmental Policy Conflicts," Expert Panel on Trade and Sustainable Development Working Paper, Sept. 1999, at 11–13.

[139] Gabrielle Marceau, *A Call for Coherence in International Law, Praises for the Prohibition Against "Clinical Isolation" in WTO Dispute Settlement*, 33 JOURNAL OF WORLD TRADE 87, 148–49 (Oct. 1999).

Chapter 5

Conclusion

An environmental PPM is not illegal under WTO rules. Whenever it violates GATT Articles I, III, or XI, the PPM will be reviewed under GATT Article XX(b) or (g) and the chapeau to the Article. With respect to the chapeau, the Appellate Body has explained that the line of legality "moves as the kind and the shape of the measures at stake vary and as the facts making up specific cases differ."[140] Thus, the WTO legality of a PPM will depend both on its implementation and its environmental rationale.

The myth that PPMs are illegal under the WTO has had three unfortunate effects. First, it has undermined the WTO in the public's perception. In his careful study of trade-related environmental measures in 1995, Howard Chang warned of these dangers:

> The creation of barriers to environmental protection in the name of free trade has eroded respect for GATT institutions in particular and political support for free trade in general. . . . The GATT panels were understandably concerned about the potential for protectionist abuse of Article XX. Their crude but sweeping rules against trade restrictions, however, make no attempt to distinguish between legitimate environmental concerns and protectionism, and in the process do the cause of free trade a great disservice: the political backlash against free trade may also fail to make the same distinction.[141]

Ironically, the GATT jurisprudence on Article XX has improved substantially since 1995.[142] But the public may not be aware of that. The second negative effect is that the divergence of views on the legality of PPMs has undermined any potential progress in the ongoing work of the WTO Committee on Trade

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[140] Appellate Body Shrimp-Turtle Report, *supra* note 61, para. 159.

[141] Chang, *supra* note 42, at 2209.

[142] Carrie Wofford, *A Greener Future at the WTO: The Refinement of WTO Jurisprudence on Environmental Exceptions to GATT*, 24 HARVARD ENVIRONMENTAL LAW REVIEW 563 (2000).

and Environment. Even without being on the formal agenda, the issue of PPMs colors many of the other issues, such as the use of trade measures in environmental treaties. The third repercussion is that without a shared understanding of the legal baseline, it is impossible to develop new disciplines to prevent inappropriate PPMs.

By debunking the PPM myth and by exploring why PPMs are used, this paper points the way to the next stage in analysis which is to recognize PPMs as a symptom of governance dysfunction and to act accordingly to address the root causes of conflict. Not all recourse to PPMs will be justifiable. But sometimes governments may use PPMs because that is the only way to respond to a global or transborder environmental harm occurring in another country. In those situations, the right role for the WTO may be to stand aside and permit the PPM. Outside the WTO, there will be a need for international environmental institutions to step in with technical assistance and other efforts to spur environmental cooperation. In the end, PPMs may be less important for what they accomplish through trade than for what they reveal about the interface between trade, the environment, and international law.

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Notes on the Author

Mr. Steve Charnovitz practices law at Wilmer, Cutler & Pickering in Washington, D.C. From 1994 to 1999, he was Director of the Global Environment & Trade Study (GETS) at Yale University, which conducts and sponsors research on trade and environment. Mr. Charnovitz was also on the Steering Committee for the Talloires Group on Trade and Environment and Policy Director of the US Competitiveness Policy Council, an advisory committee to the US Congress and President. From 1987 to 1991, he was a legislative assistant to the Speaker of the US House of Representatives.

Mr. Charnovitz has written extensively on international trade law, environmental law and labor law. He is a frequent lecturer on those topics.

Until the publication of the Appellate Body's decision in the Shrimp-Turtle case (1998), it was widely assumed that GATT/WTO rules did not allow member countries to discriminate against imports of a product from a particular country or firm on the basis of the "processes and production methods" (PPM) used to make that product. This conclusion that *how* a product was made could not be used to justify a more restrictive duty or import ban was vigorously criticized by, among others, groups concerned with environmental pollution and the humane treatment of animals.

There are many experts who believe the Appellate Body opened the door to PPM-based discrimination in its Shrimp-Turtle decision. Steve Charnovitz's view, in contrast, is that WTO rules do not categorically prohibit PPM-based discrimination, and that the Shrimp-Turtle decision simply "clarified trade rules on this point."

In this paper, he begins with an explanation of what PPMs are and when they might be justifiable. Next, he divides PPMs into those involving a "How Produced standard" and those involving a "Foreign Government Policy standard", and concludes that the former are more likely to be WTO-consistent. He then examines how WTO rules govern PPM-based discrimination against imports, in order to demonstrate "the falsity of the myth that PPMs are illegal under the WTO." After outlining steps he believes should be taken to improve the management of PPMs, he concludes by observing that the myth that PPM-based discrimination is WTO-inconsistent has harmed the WTO's public image, undermined work in the WTO's Committee on Trade and Environment, and made it impossible to develop new rules to prevent the misuse of PPMs.

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