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Legal Memo: Questions of Compatibility with WTO Law of Trade Measures Taken under a New Climate Change Protocol[1]

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1. Questions:

1.1. Based on the provisions of the agreement reached at the Copenhagen summit, what would be the legal implications under WTO law, if a signatory state imposes trade measures (e.g. extra tariffs) to persuade a non-signatory state to adhere to the agreement?

1.2. What are the legal consequences under WTO law if a climate change protocol requires signatory states to impose trade measures against other signatory states in cases of non-compliance (e.g. with financial commitments)?

2. Brief answer:

- While the case law has not yet taken a definite and convincing position on the issue, trade measures based on a MEA which both countries are parties to should be justifiable in WTO law. Although the option appears appealing at first view, a MEA cannot be used at the interpretive level to influence the interpretation of WTO law. In practice this would amount to interpretation *contra legem*. As a self-standing defense, a MEA would have to be admitted as applicable law by a panel. Even if such a change in the case law would occur, a conflict of norms is the consequence. The conflict rules of public international law prove highly inadequate for a panel trying to adjudicate such a case, which renders the final outcome more than uncertain (for a more detailed discussion, see Section 4.1.).
- The case law has not clearly answered the question of trade measures under a MEA against non-parties either. While the lack of consent of the third party prevents the use of the MEA as applicable law or self-standing defense, the MEA is still an important factor to assess the justification of unilateral trade measures under Article XX's[2] derogation for environmental protection. It is suggested that trade measures based on a MEA could be justifiable with higher probability under this provision, as there is less likelihood of hidden protectionism. Care must be taken to use the least trade restrictive alternative, in particular if the MEA at issue gives discretion. In some instances, financial assistance could arguably qualify as such an alternative. The application of trade measures must at all times be free of arbitrary or unjustifiable discrimination between countries which requires great care in the design of extra-tariffs (for more details, refer to Section 4.2.).
- Next to the question of trade measures under a MEA, the present study also sheds light on an alternative model, carbon border adjustments, and their WTO compatibility. A short overview of such adjustments as an alternative approach to persuasion by means of extra-tariffs shows several potential problems under WTO law. It is in particular unclear whether WTO law permits border tax adjustments on inputs of products which are not

[2] All article numbers which are not differently designated refer to the GATT.

incorporated in the final product such as “dirty” energy or fuels. Furthermore, adjustments imposed on imports most likely breach several GATT provisions such as most favoured nation treatment and national treatment, while the conditions for justification under Article XX may not necessarily be easy to meet. Border adjustments (i.e. rebates) on exports fall under the rules on subsidies of the SCM Agreement. While these disciplines are quite straightforward to meet in order to exempt consumption taxes, production taxes are an unsettled question mainly because again the relevant rules do not clarify whether taxes on inputs may be rebated if the inputs in question are not physically incorporated in the final product (for more details, see Section 4.3).

Policy proposals for treaty drafters and countries willing to use extra-tariffs as a dissuasive tool against MEA free-riders:

- As for a post-Kyoto deal, the analysis shows that extra-tariffs as a means of persuasion for non-participants would probably face a challenge under WTO law. In this light, it appears questionable whether the risk of such highly trade disruptive measures should be taken in view of the evidence that their dissuading effect on free-riders might be limited.
- As regards a process of negotiation of a post-Kyoto MEA, as an ideal solution either a waiver should be aimed for within the WTO or a carefully drafted conflict clause ought to be included in the relevant MEA, if parties want to provide for extra-tariffs. Such non-WTO law provisions could serve as a self-standing defense for extra-tariffs under WTO law if the trade measures are taken amongst parties to the MEA. A provision which *requires* the imposition of tariffs against other countries would be more apt to justify a *prima facie* violation of WTO law than one which merely *allows* the use of such trade measures. Still, even in this first scenario the use of discretion given to a WTO member would come under close scrutiny by a panel. Therefore, respect of the following considerations appears highly advisable for individual states which want to impose extra-tariffs on other countries.
- Generally, as the analysis in the memo has shown, the stronger the link of extra-tariffs to a MEA is, the easier it may find justification under WTO law. A state should, thus, cooperate in good faith if multilateral efforts are undertaken in order to achieve a MEA as a basis for trade measures.
- Depending on how the MEA is drafted, a state may enjoy more or less discretion in implementing trade measures. The more discretion is given, the more a state must take into account WTO law: For example, if the determination of a breach of obligations of another party is undertaken by the conference of the parties of a MEA, a member may simply take over this determination. If the determination has to be done unilaterally, the state must carefully avoid arbitrary distinctions in the methodology and criteria used for the determination.
- In implementing a regime of extra-tariffs, a state must carefully draft these tariffs to avoid the suspicion of protectionism. The regime should, thus, aim to create an incentive to adhere if non-participation is to be dissuaded. It must not, on the other hand, overprotect certain domestic industries, for instance to help them adapt to burdensome requirements under a domestic emissions trading scheme or carbon taxation in view of foreign competition. The latter would be a task which border tax adjustments would pursue.

- Extra-tariffs to dissuade free-riders must be linked to domestic efforts under a MEA which fights climate change. Domestic efforts could be a carbon tax or an emissions trading scheme. It appears virtually impossible to prove that tariffs are not imposed for protectionist reasons if domestic efforts are insufficient, while "outsiders" should be persuaded to adhere to a MEA which is not even respected by the party imposing the tariffs.
- Any regime of extra-tariffs most crucially must provide space for a targeted country to bring forward its own arguments why it should not be target of tariffs. The country should receive the opportunity to show that it pursues its own equivalent strategy to fight climate change apart from the measures suggested under the MEA. The procedure for this purpose must give the country right to a fair hearing, grant due process and a satisfactory procedure for review of any decision taken. Should equivalent efforts be found to be implemented, no tariffs may be imposed on the country.

3. Fact statement and setting of the inquiry:

The present inquiry departs from several assumptions that have to be clearly set out in advance. The general benchmark of compliance is WTO law as it stands today. While amendments to the WTO covered agreements or waivers to prevent some of the legal problems found in the inquiry below are frequently discussed in the doctrine, we depart from a situation in which trade measures taken under a multilateral environmental agreement (MEA) are taken in the background of the WTO at its current stage of development.

Secondly, the inquiry should depart from the agreement reached at the Copenhagen Summit in December 2009 in the framework of the 15th Conference of the Parties (COP 15) to the United Nations Framework Convention on Climate Change.[3] However, the agreement is a mere political accord, which the parties have "taken note of". It contains, therefore, neither strong legal force under the circumstances of its conclusion nor does its content. In addition, all major players are already parties to the agreement,[4] which renders the scenario of trade measures against non-parties with the objective of persuading them to adhere to the agreement virtually inapplicable. The question itself, however, does not lose its relevance despite the weak force of the Copenhagen accord. Leaving aside the accord, we assume, thus, for the scenario of the first question the existence of a MEA on climate change which foresees the imposition of trade measures (here in the form of extra-tariffs) against non-parties in a way similar to the Montreal Protocol.[5]

[3] Available at unfccc.int/meetings/cop_15/items/5257.php (last visited 10 June 2010).
[4] The full list of parties can be found at unfccc.int/home/items/5262.php (last visited 10 June 2010).
[5] For a brief overview of the provisions of the Montreal Protocol on ozone-depleting substances concerning trade measures see D Brack, 'Environmental Treaties and Trade: Multilateral Environmental Agreements and the Multilateral Trading System' in G Sampson and B Chambers (eds), *Trade, Environment, and the Millenium* (2 edn, United Nations University Press, Tokyo 2001), 275-277.

Thirdly, we assume again the existence of a follow-up agreement on the Kyoto Protocol[6] which shall be referred to as the International climate change Protocol (hereinafter ICCP). This document sets out emission reduction requirements in a similar manner to its predecessor and also contains financial commitments from developed countries (annex I countries) towards developing countries (non-annex I countries). We further presume that in case of breach of commitments by one signatory state, the other signatory states of the ICCP are entitled or required to impose increased duties on imports originating from this state.[7] The second scenario, thus, inquires into the WTO legality of trade restrictive measures among parties to a MEA.

There are several reasons why the inquiry as set out now appears relevant and of importance. Institutional elements indicate that the topic is perceived as relevant within the WTO., WTO Director-General Pascal Lamy for example has consistently emphasized before the Copenhagen Summit that WTO members should aim for consensus in the form of a renewed multilateral environmental agreement on Climate Change before taking action within the WTO, f.ex. in the form of "proper pricing of energy" or similar measures.[8] This emphasis on multilateral action, upon which individual measures by WTO members should be based, strengthens the argument that a new baseline for MEA-based action with trade impacts has to be found.

Furthermore, the mandate for the Doha Development Round of trade negotiations of the WTO takes up the issue.[9] However, the emphasis is on the relationship between WTO obligations and trade obligations set out in MEAs between parties to both treaties. The issue of trade measures against non-parties to a MEA and of such trade measures which are merely allowed and not required is deliberately left aside[10] and requires, despite or even because of this omission, further attention.

As a practical consideration, the outcome of the Copenhagen conference has shown, that the conclusion of a MEA or protocol to the UNFCCC to follow up on the Kyoto Protocol is unlikely for the near future. While the first two parts of this memo focus on the question of trade measures under MEAs in WTO law, the third section goes to the centre of the current debate. As some legislative action which has already taken place[11] or is currently in the pipeline[12] suggests, border adjustments are perceived by

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[6] For more information on the Kyoto Protocol see http://unfccc.int/kyoto_protocol/items/2830.php (last visited 10 June 2010).

[7] The draft text of the relevant Article 3 ICCP reads: "As a way to ensure compliance with this Agreement, parties will report back annually to the UNFCCC on their emission reductions and financial commitments. If a party is not respecting its commitments, other parties will impose increased duties on imports originating therefrom."

[8] See e.g. Lamy's speech to the European Parliament in Brussels, 29 May 2008, available at www.wto.org/english/news_e/sppl_e/sppl91_e.htm (last visited 10 June 2010).

[9] In paragraph 31 (i) of the Ministerial Declaration (WT/MIN(01)/DEC/1, 20 November 2001), the negotiators are given the task to focus on "the relationship between existing WTO rules and specific trade obligations set out in multilateral environmental agreements (MEAs). The negotiations shall be limited in scope to the applicability of such existing WTO rules as among parties to the MEA in question. The negotiations shall not prejudice the WTO rights of any Member that is not a party to the MEA in question[.]"

[10] M Elizalde Carranza, 'MEAs with Trade Measures and the WTO: Aiming towards Sustainable Development?' (2007-2008) 15 Buffalo Environmental Law Journal 43, 65.

[11] See in this respect newer EU legislation which provides for a possible future inclusion of importers in the EU emissions trading scheme in case of carbon leakage problems, see Directive 2009/29/EC

many developed countries as a viable alternative to a multilateral deal on climate change which failed to emerge in Copenhagen. At the same time, the admissibility of such carbon border adjustment is fiercely contested by other WTO members.[13] It should be noted that the most recent European initiative points in the direction of more broadly applied carbon and energy taxation, whereby the problem of carbon leakage should be addressed by supporting European industries through free allowances, "adding to the cost of imports" from countries that do not sufficiently engage in mitigation measures and bringing "the rest of the world closer to EU levels of effort".[14]

The third and last section addresses, thus, the state of the debate on border adjustments in WTO law as alternative action which is not based on a MEA or taken as required by such an agreement.

4. Discussion:

The discussion focuses on three different issues as set out in the fact statement. First, we shall examine the WTO legality of trade measures adopted by one WTO member against another one based on a MEA which they are both parties to (4.1.). Second, the situation of trade measures of a party to a MEA against a non-party is assessed under WTO law (4.2.). Lastly, we exhibit the state of the debate on border adjustments as a unilateral mechanism by parties to a MEA such as the Kyoto Protocol to level the playing field between their industries and foreign industries which do not suffer the impact of carbon reduction commitments (4.3.).

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amending Directive 2003/87/EC so as to improve and extend the greenhouse gas emission allowance trading scheme of the Community, Official Journal [5.6.2009] L 140, 63-87, Article 10b alinea 1(b). Simultaneously, France has advanced quite far towards a regime of carbon taxation. However, problems of equal treatment among different industrial sectors arise, as a recent ruling of the French Constitutional Court on the planned carbon consumption tax shows. See Décision n° 2009-599 du 29 décembre 2009, paras 77-83, available at www.conseil-constitutionnel.fr (last visited 10 June 2010). The Constitutional Court ruled that the relevant tax was in breach of the principle of tax equity, as it exempted a number of industries with the argument that the latter were within the scope of the Cap and Trade System established by the European Union (Emissions Trading Scheme). The Court found this foundation of the law unconvincing, since the Emissions Trading Scheme would give out allowances for free for the moment and would only start charging the concerned industries in the wider future.

[12] United States' legislative proposals foresee that together with the introduction of a planned cap and trade system importers of fuels and industrial gases are required to buy allowance requirements in the cap and trade scheme like domestic producers. They can only be exempted if they participate in a similar cap and trade scheme in their state of origin. See for one example Bill Number H.R. 2454 for the 111th Congress (often referred to as the Waxman-Markey Bill) which encompasses the American Clean Energy and Security Act of 2009 in the version "Engrossed as Agreed to or Passed by House", available at http://thomas.loc.gov/cgi-bin/query/z?c111:H.R.2454: (last visited 10 June 2010), Section 722 "Prohibition of excess emissions", pp. 735 ff. In addition, there are also two other competing proposals, the so-called Kerry-Boxer Bill and the Kerry-Graham-Lieberman Bill, but these also contain similar provisions on the subject of carbon leakage.

[13] See e.g. "India Threatens WTO Case Against Proposed 'Carbon Border Taxes'", Bridges Weekly Trade News Digest, Vol. 14, N°12, 31 March 2010, available at ictsd.org (last visited 10 June 2010).

[14] See "EU Commissioners to Consider Energy Tax Overhaul", Bridges Weekly Trade News Digest, Vol. 14, N°21, 9 June 2010, available at ictsd.org (last visited 10 June 2010), citing a draft European Commission document.

4.1. Trade measures among parties to a MEA

This section will analyse the question of potential violations of the General Agreement on Trade and Tariffs in cases where one party to a MEA imposes trade measures against another party based on the provisions of the MEA. We will consider the hypothetical case of the implementation of a clause allowing or proscribing the increase of duties on imports from a member state violating its obligations under the ICCP, for example because commitments to provide financial assistance are not respected.

4.1.1 The potential of trade measures under a MEA to violate WTO disciplines

The main provisions we are interested in are Art. I, II, III and XI GATT. According to Art. I, known as the most favoured nation clause, like products must receive the same treatment independently of their origin. This article would be violated in a case of trade restrictions against some but not other WTO members by means of extra-tariffs. As a central provision, Article II binds WTO members to the tariff concessions they have given in negotiations. Raising tariffs breaches this commitment, unless certain circumstances such as under Article II:2(a) are given. Under this provision, there is leeway for border tax adjustment. However, extra-tariffs would hardly be able to qualify under such an exception (see section 4.3. for a detailed assessment of border adjustment). Even under Article II:2(a), a border adjustment would have to fulfill the disciplines of Article III:2. Art. III provides that products imported from another WTO member shall not receive less favourable treatment than like domestic products. This provision could be breached in case one WTO member imposes a tax on imports of carbon intensive products (See section 4.3 on border adjustments for a detailed examination of such adjustments). Art. XI forbids quantitative import restrictions; in such a scenario a WTO member would for example impose an import ban as a response to non-fulfilment of obligations under a MEA. As this short overview shows, trade measures will easily fall within the scope of and breach obligations of WTO members under WTO law.

4.1.2 The applicability of multilateral environmental agreements in WTO dispute settlement

As the previous section has shown, there is a high likelihood that WTO panels and the Appellate Body would find an increase in tariffs or similar alternatives to constitute a violation of WTO legal obligations. Before we examine whether such violations can be justified under the derogations foreseen in Article XX GATT, the question of the potential role of multilateral environmental agreements in WTO dispute settlement arises. In the present scenario, the ICCP could develop legal effects in different forms. First, it could be used as an interpretative tool to read WTO law in its light (4.1.2.1.). Second, non-WTO rules of international law such as environmental rules could be directly invoked before and applied by WTO adjudicative bodies (4.2.2.2.). Last, if there is as a consequence a conflict of norms between these norms and WTO rules, we have to assess in detail the nature of the conflict and the potential of conflict rules to provide us with a satisfactory solution (4.2.2.3.).

4.1.2.1 Non-WTO rules and the rules of interpretation in WTO law

The Appellate Body has constantly emphasized in its case law that the general rules of interpretation of public international law are applicable in WTO dispute settlement.[15] The following section shows how "extraneous" rules can be integrated into this interpretative approach.

According to Art. 31.3 (c) of the Vienna Convention on the Law of the Treaties (VCLT) when a treaty is being interpreted "any relevant rules of international law applicable in the relations between the parties" should be taken into account. (Art. 31.3 (c) requires three conditions to be met.[16] First, the treaty which shall be used as an interpretive tool ought to constitute a "rule of international law". The ICCP incorporates rules of international law without any doubt. Second, the treaty has to be relevant for the norm that is actually interpreted and therefore for the purpose at hand. Obviously, extra-tariffs have an impact on WTO law. Third, the treaty has to "be applicable in the relations between the parties". According to the Panel in the *EC-Biotech products* case the phrase "the parties" refers to the all of the parties to a treaty and not merely to the parties to a dispute. The Panel stated that: "This understanding of the term 'the parties' leads logically to the view that the rules of international law to be taken into account in interpreting the WTO agreements at issue in this dispute are those which are applicable in the relations between the WTO Members."[17] According to this argument all WTO members have to become members of the MEA before it can be taken into account for interpretation. This argument is supported by the context of Art. 31.3 (c). Under Art. 31.3 (a) and (b) only subsequent agreements and subsequent practice reflecting the common intentions of all parties to a treaty may be taken into account in interpretation.[18]

On the other hand, this restrictive approach postulates the need for a crossover in membership and thereby protects non-parties to an extraneous treaty from legal consequences flowing from that treaty comparable to the principle *pacta tertiis nec prosunt nec nocent*.[19] However, there are conflicting views: The *EC- Biotech products* case was strongly criticized by the study group of the International Law Commission

[15] See for an early example *United States - Standards for Reformulated and Conventional Gasoline* AB-1996-1, WT/DS2/AB/R, 29 April 1996

[16]B McGrady, 'Fragmentation of International Law or "Systemic Integration" of Treaty Regimes: EC-Biotech Products and the Proper Interpretation of Article 31(3)(c) of the Vienna Convention on the Law of Treaties' (2008) 42 Journal of World Trade 589, 591..

[17] *EC - Measures Affecting the Aproval and Marketing of Biotech Products* DS291/R, WT/DS292/R, WT/DS293/R, 21 November 2006 , para. 7.68. There is no confirmed practice concerning the acceptance of this approach. McGrady, 610.

[18]J Pauwelyn, *Conflict of Norms in Public International Law - How WTO Law Relates to Other Rules of International Law* (Cambridge University Press, Cambridge 2003), 258.

[19]McGrady, 591. This restrictive approach to Article 31(3)c appears, however, questionable, since it entails a higher potential to leave aside norms relevant to interpretation and thereby increases the potential for conflict between different regimes of international law. See in this respect Art. 31.3 (c) of the VCLT as the context of the conflict rules contained in Art. 30 VCLT. A reading of this provision has been suggested as promoting an interpretation of treaty obligations which is aimed at avoiding conflicts. Good faith presumed, States are expected to implement all their international obligations accordingly. Therefore, States' obligations are considered cumulative and must be complied with simultaneously. Only in case of an irreconcilable conflict between a WTO provision and another treaty provision, Art. 30 can be invoked, see G Marceau, 'Conflicts of Norms and Conflicts of Jurisdictions, The relationship between the WTO Agreement and MEAs and other treaties' (2001) 35 Journal of World Trade 1081, 1089.

on Fragmentation of International Law, because in practice such an approach would result in the "isolation of multilateral agreements as "islands" permitting no references *inter se* in their application." Furthermore "[it] would also prohibit any use of regional or other particular implementation agreements - including *inter se* agreements - that may have been concluded under a framework treaty, as interpretative aids to the latter."[20] The argument that treaty provision may reflect customary international law although they are not binding on a state has also been advanced. This argument is not convincing for two reasons, despite the fact that the generality of the treaties would be maintained. First, it would not allow reference to treaties which have a wide acceptance, but have not yet acquired the status of international customary law. Second, it would preclude reference to treaties which elaborate on a specialist subject matter merely because not all WTO members are party to such a treaty.[21] It would therefore seem more convincing to use as a precondition that the parties to the dispute are members of the MEA in question instead of inquiring into overall parallel membership to both the MEA and the WTO covered agreements.[22]

If we follow the logic of the *Biotech product* case, the ICCP could constitute guidance for interpreting the notions of WTO law only if all WTO members are parties to the ICCP. This seems highly unlikely and can be underlined by the limited membership to the Kyoto Protocol. However, if the Appellate Body which has not yet been asked to adjudicate this question should adopt the integrationist position outlined here, the ICCP would be available as an interpretative tool in case both countries are ICCP members and have ratified the provisions. The conflict between the obligation to impose extra duties under the ICCP (assuming that there is such an obligation and that we are not in presence of a mere right) and their character as violations of WTO law, however, does not leave much space for conflict-avoidance through interpretation. The wording of Art. I, III and XI of GATT clearly indicates that extra-tariffs would violate these provisions and does not seem to give any leeway to an interpretation that would allow deviations. Where the WTO provisions are unambiguously clear, treaty interpretation cannot constitute a remedy, as this would here require an interpretation *contra legem* of the GATT's provisions which is generally regarded as inadmissible. We turn, thus, to the following question of whether a MEA such as the ICCP can constitute a self-standing defense as part of the applicable law before a panel in a dispute settlement proceeding.

4.1.2.2. Applicable law in the DSU

The following section discusses whether non-WTO law can be applied as an independent defense before a panel in WTO dispute settlement.[23]

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[20] Report of the Study Group of the International Law Commission, "Fragmentation Of International Law: Difficulties Arising From The Diversification And Expansion Of International Law", UN Doc. A/CN.4/L.682, 13 April 2006, 237 (hereinafter Fragmentation Report).

[21] Ibid., 238.

[22] It is important to bear in mind the risk of divergences in the interpretation of the will of the parties, such as *inter se* modifications. This risk is lessened through a distinction between bilateral and synallagmatic treaties. Pauwelyn (See J Pauwelyn, 'A Typology of Multilateral Treaty Obligations: Are WTO Obligations Bilateral or Collective in Nature?', 14 European Journal of International Law 907) argues that the obligations under the WTO Agreement are bilateral.

[23] It should be stated at the outset, that no question on jurisdiction arises in the present case, which would constitute a different problem if a claim should be brought which was not clearly based on the

Art. XXIII of GATT 1994 and Articles 1.1, 7 and 11 of the DSU stipulate that WTO adjudicating bodies have only limited jurisdiction. Under Art. 1.1 of the DSU WTO panels only possess competence to adjudicate claims based on the WTO covered agreements. Additionally, Art. 7 of the DSU provides that the panel should examine the claims in "the light of the relevant provisions" of the covered agreements cited by the parties to the dispute and that the panel "shall address the relevant provisions in any covered agreement or agreements cited by the parties to the dispute." Art. 11 requires panels to "make an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements, and make such other findings as will assist the DSB in making the recommendation or in giving the rulings provided for in the covered agreements." Furthermore, Art. 3.2 of the DSU states that "Recommendations and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements"[24]. Art. 19.2 reconfirms this rule with reference to the Appellate Body and the Panels.

All these provisions do not indicate that WTO law exists separated from general public international law. The Appellate Body made this also clear in the *US- Gasoline* case by stating that "the *General Agreement* is not to be read in clinical isolation from public international law."[25]

Furthermore, Art. 3.2 stipulates that the WTO dispute settlement system serves "to clarify the existing provisions of [the covered agreements] in accordance with customary rules of interpretation of public international law. " These rules are provided in Article 31 and 32 VCLT. Art. 31 (3) (a) and (c) of the VCLT read that "any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions" and "any relevant rules of international law applicable in the relations between the parties" should be taken into account.

The previous section has already outlined that a legitimate argument can be made out of these findings which promotes the application of non-WTO law as an interpretative tool. In addition, however, such a non-isolationist reading of WTO law and the DSU also supports the thesis that non-WTO can be invoked as an independent defense in the form of a self-standing rule to be applied by a panel next to the rules of the WTO covered agreements.

WTO covered agreements. As shown previously, the claims brought on extra-tariffs obviously touch upon WTO law and therefore only the question of the applicable law is pertinent to the present inquiry.

[24] In *US — Certain EC Products*, the Appellate Body ruled that the purpose of dispute settlement is only to preserve the rights and obligations of Members:"[W]e observe that it is certainly not the task of either panels or the Appellate Body to amend the DSU or to adopt interpretations within the meaning of Article IX:2 of the *WTO Agreement*. Only WTO Members have the authority to amend the DSU or to adopt such interpretations. Pursuant to Article 3.2 of the DSU, the task of panels and the Appellate Body in the dispute settlement system of the WTO is 'to preserve the rights and obligations of Members under the covered agreements, and to *clarify the existing provisions* of those agreements in accordance with customary rules of interpretation of public international law.' (emphasis added) Determining what the rules and procedures of the DSU ought to be is not our responsibility nor the responsibility of panels; it is clearly the responsibility solely of the Members of the WTO." (para. 92)

[25] *US - Gasoline, p. 17.*

Art. 3.2 DSU is understood by some as explicitly setting out an exhaustive list of the rules to be applied, which means that no extraneous norms can be invoked before a WTO adjudicating body.[26] On the other hand, it could be argued that these rights and obligations would not be modified through the adjudicating bodies, since the States did give their consent by concluding other treaties.[27] As a pre-condition under this position, both rules- WTO and non-WTO- must be binding on both disputing parties and must not affect the rights or obligations of third parties.

The applicability of international public law in WTO proceedings has not been fully clarified by the WTO adjudicative bodies so far. The panel in the *Korea Government Procurement* case[28] stated that customary international law applies between WTO members. "However, the relationship of the WTO Agreements to customary international law is broader than this. Customary international law applies generally to the economic relations between the WTO Members. Such international law applies to the extent that the WTO treaty agreements do not 'contract out' from it", that is "to the extent there is no conflict or inconsistency, or an expression in a covered WTO agreement that implies differently." [29] It continued by stating that"(…) we can see no basis here for an *a contrario* implication that rules of international law other than rules of interpretation do not apply."[30]

The Appellate Body itself has shown more reluctance to consider the application of non-WTO rules. In the *EC-Hormones* case,[31] the Appellate Body stated that the "precautionary principle does not by itself and without clear textual directive to that effect, relieve a penal from the duty of applying the normal…principles of treaty interpretation."[32]

However, the *Mexico – Soft Drinks*[33] case might point into another direction. In this case, Mexico tried to bring claims before a panel for which the United States had blocked the formation of a dispute settlement panel in the NAFTA context. Despite the Unites States' claims to reject jurisdiction, the Appellate Body ruled that it had no discretion under the DSU to decline its jurisdiction in a case that had been properly brought before it. It stated, however, apart from this finding that it was "express[ing] no view as to whether there may be other circumstances in which legal impediments could exist that would preclude a panel from ruling on the merits of the claims before it."[34] As a consequence, in case where a non WTO body found a violation of a non-WTO treaty such as the ICCP, it could be possible that the Appellate Body would refer to such a decision and recognize non- WTO law as an independent defense.

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[26] For a discussion of this position see Joel Trachtman, *The Domain of WTO Dispute Resolution*, 40 Harvard International Law Journal 333, 342 – 342 (1999), John McGinnis, The Appropriate Hierarchy of Global Multilateralism and Customary International Law: The Example of the WTO, *Virginia Journal of International Law* (2003), volume 44, issue 1 , pp. 229-284.
[27] J Pauwelyn, ' How to Win a WTO Dispute Based on non- WTO Law ' (2003) 37 Journal of World Trade 997.
[28] *Korea- Measures Affecting Governement Procurement*, WT/DS163/R, 1 May 2000.
[29] Para. 7.96.
[30] Footnote 753.
[31] *EC - Measures concerning Meat and Meat Products (Hormones)*, AB-1997-4, WT/DS26/AB/R, WT/DS48/AB/R, 16 January 1998.
[32] Para. 124.
[33] *Mexico - Tax Measures on Soft Drinks and Other Beverages* AB-2005-10, WT/DS308/AB/R, 6 March 2006.
[34] Para 54.

As a brief conclusion, WTO adjudicative bodies have not clearly rejected the applicability of non WTO law such as the ICCP as a self-standing defense before WTO judicial organs and systematically avoided to take a stance on the question. In the long run the Appellate Body will have to take a clear position and it may accept the applicability of certain rules of non WTO law. If thus two norms confront each other beyond the question of applicability, a conflict of norms is likely to arise between the two. We therefore will now discuss the conflict of norms which would arise in such a case.

4.1.2.3. Excursus: A conflict of jurisdictions?[35]

Apart from a potential conflict of substantive norms, one could ask at this junction whether a conflict of jurisdictions could also arise. This would be the case where two judicial bodies would be asked to adjudicate – at least partly – upon the same claim. If we take the Kyoto Protocol as our example, there is a sophisticated non-compliance mechanism[36] While one part of it, the facilitative branch, focuses on technical assistance and similar positive approaches for parties in difficulties, the enforcement branch is structured closely to a judicial mechanism and is competent to determine non-compliance of parties to the protocol and pronounce its legal consequences.[37]

A conflict of jurisdictions in a temporal sense would, however, hardly ever arise. Normally, trade measures for non-compliance would in most cases ensue as a consequence of a determination of non-compliance and a WTO panel would only be called do adjudicate upon the case once trade measures are in place. However, in substantial terms the overlap could become an issue when a panel has to react on a determination already made by a non-compliance mechanism under an MEA. As the previous discussion of the *Mexico – Soft Drinks* case has shown, the Appellate Body has left the door open to recognize in the future a finding of non-compliance established by a non-WTO adjudicative body in WTO law. As the later discussion on the justification of trade measures against non-parties to a MEA shows,[38] a panel could also use such a determination as evidence that a trade measure imposed possesses a certain legitimacy and does not merely pursue protectionist objectives.

4.1.2.4 .The conflict of norms

[35] This excursus goes back to comments and the discussion at the presentation of this memo on 10 May 2010, for which the authors are thankful to Joost Pauwelyn, the participants in Professor Pauwelyn's trade law clinic and Romain Benicchio.

[36] Generally on the rise of non-contentious mechanisms of conflict resolution in particular in environmental law see the fundamental study of A Chayes and A Handler Chayes, *The New Sovereignty: Compliance with International Regulatory Agreements* (Harvard University Press, Cambridge 1995), passim.

[37] For more details on the Kyoto Protocol's non-compliance mechanism see R Wolfrum and J Friedrich, "The Framework Convention on Climate Change and the Kyoto Protocol", in U Beyerlin, P-T Stoll and R Wolfrum (eds.), *Ensuring Compliance with Multilateral Environmental Agreements – A Dialogue between Practitioners and Academia* (Martinus Nijhoff Publishers, Leiden, 2006), 53; S Urbinati, "Procedures and Mechanisms Relating to Compliance under the 1997 Kyoto Protocol to the 1992 United Nations Framework Convention on Climate Change", in T Treves e.a. (eds.), *Non-Compliance Procedures and Mechanisms and the Effectiveness of International Environmental Agreements* (T.M.C. Asser, The Hague, 2009), 63.

[38] See in particular section 4.2.4.5.

Returning to the main inquiry, the question of a conflict of norms arises, if we admit that non-WTO rules can be part of the applicable law in WTO dispute settlement. International law knows of no hierarchy. In an ideal case, a non-WTO norm would merely be applicable and help to solve the case as an addition. In practice, however, such a rule can also enter into conflict with the applicable WTO rules. At this point, conflict rules of general public international law intervene to determine which of two conflicting rules governing a situation will prevail. In the present case a provision allowing or requiring the imposition of increased duties and a provision which prohibits the imposition of increased duties evidently enter into contradiction. Therefore only one of them can be applied. In order to understand which of these provisions prevails, a norm of conflict has to be chosen. We will first turn to a more in-depth analysis of the definition of conflict, which is necessary in order to establish the existence of a conflict and understand which maxims of conflict might apply. In the following discussion we will review two scenarios: The hypothesis of an ICCP clause which *allows* state parties to impose increased duties on other state parties formulated as a permission and the scenario of an ICCP clause which *requires* state parties to impose increased duties on other parties.

A. The definition of conflict

It is necessary to identify the existence of a conflict before we can look at the way of resolving it. According to the traditional argument, a conflict of norms arises where a party to two treaties "cannot simultaneously comply with its *obligations* under both treaties".[39] This however, raises the question of whether the notion of conflict only comprises prescriptive and prohibitive norms[40] or if it also includes permissions[41]. The definition of conflict of norms therefore determines the possible scope of application of conflicts maxims e.g. *lex posterior*. The WTO case law has not yet taken a clear stance on the subject. It seems, however, that there exists a tendency towards a definition which does not consider the clash between a permission and an obligation as a conflict. As we will see subsequently this entails certain problems. The second scenario includes two obligations, which cannot be complied with simultaneously and does therefore correspond to the strict definition of conflict. In the first scenario one of the rules is formulated as a permission. Hence, only a definition of conflict which includes situations in which the use of a permission by a state causes a conflict with obligations under another treaty can lead to the next step of applying a rule of conflict.

Since no definition of conflict is given by WTO law as it is written, it is useful to look at the practice of WTO panels and Appellate Bodies. The WTO case law has not yet developed a coherent view on the subject. In the panel report in *Indonesia-Automobiles*,[42] Indonesia was accused of violating *inter alia* Art. III GATT. As a defense, Indonesia invoked a *permission* under the WTO Agreement on Subsidies and Countervailing Measures. The panel stated in response that:

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[39] C Jenks, 'The Conflict of Law - Making Treaties' (1953) 30 British Yearbook of International Law, 426.

[40] A legal provision which *requires* a state to adopt or refrain from adopting a certain conduct.

[41] A norm which *allows* a state to adopt or refrain from adopting a certain conduct.

[42] *Indonesia - Certain Measures Affecting the Automobile Industry* WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R, 23 July 1998.

> "In international law for a conflict to exist between two treaties, three conditions have to be satisfied. First, the treaties concerned must have the same parties. Second, the treaties must cover the same substantive subject matter. Were it otherwise, there would be no possibility for conflict. Third, the provisions must conflict, in the sense that the provisions must impose *mutually exclusive obligations.* [...] [T]echnically speaking, there is a conflict when two (or more) treaty instruments contain obligations which cannot be complied with simultaneously."[43]

As a consequence, the panel did not look at the developing country clause containing a specific permission invoked by Indonesia. Therefore, the very definition of conflict precluded the applicability of the permission which was *lex specialis* and would have prevailed according to the conflict clause in Annex 1A[44] of the WTO Agreement.[45]

In the *Turkey- Textiles*[46] case, a claim was brought against Turkey by India under Art. XI. Turkey argued that the quantitative restrictions did not violate relevant provisions of the GATT and the WTO Agreement on Textiles and Clothing since they were justified by GATT rules on regional trade agreements. According to Turkey these rules should be considered *lex specialis* for the rights and obligations of WTO Members at the time of formation of a custom union. The Panel held that "[t]here is no conflict if the obligations of one instrument are stricter than, but not incompatible with, those of another, or it is possible to comply with the obligations of one instrument by refraining from exercising a privilege or discretion accorded by another."[47]

The panel thereby gave a definition of conflict which excludes the existence of a conflict in this case. It nevertheless continued by examining whether the GATT authorized measures which the Agreement on Textiles and Clothing prohibits.[48]

Although there seem to be inconsistencies in the application of the definition of conflict, panels have, thus, shown a clear tendency towards the application of a definition of conflict of norms which favours the stricter of two obligations to the detriment of clauses containing mere permissions.

The Appellate Body's statements in the *Guatemala – Cement* case have generally been interpreted as containing a strict definition of conflict.[49] According to the Appellate Body, a conflict is *"a situation where adherence to the one provision will lead to a violation of the other provision"*.[50] However, it has been submitted by Vranes that the provisions at hand in this case do not constitute norms of conduct, but

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[43] Ibid., footnote 649.
[44] General Interpretative Note to Annex 1 A of the WTO Agreement.
[45] E Vranes, *Trade and the Environment - Fundamental Issues in International Law, WTO Law, and Legal Theory* (Oxford University Press, Oxford 2009), 15; Pauwelyn, *Conflict of Norms in Public International Law - How WTO Law Relates to Other Rules of International Law* , 193-194.
[46] *Turkey - Restrictions on Imports of Textile and Clothing Products* WT/DS34/R, 19 November 1999, para 9.88.
[47] Ibid., para 9.92.
[48] Ibid., para 9.95.
[49] Pauwelyn, *Conflict of Norms in Public International Law - How WTO Law Relates to Other Rules of International Law*, 194; Marceau, 1089.
[50] *Guatemala - Anti-Dumping Investigation Regarding Portland Cement from Mexico* WT/DS60/AB/R, 25 November 1998, para 65.

norms of competence, which have to be distinguished from mere permissions.[51] Similarly, "adherence to the one provision" could also be read in a broad manner as referring to the conditions under a right such as the various conditions of Article XX. Therefore, no such general conclusion can be drawn from the case.

The only instance where a broader definition of conflict has been adopted is the panel's report in the *EC-Bananas* case concerning the GATT's *General Interpretative Note* on the relationship between the GATT and specific WTO Agreements. The panel argued that a narrow definition of conflict "would render whole Articles or sections of Agreements covered by the WTO meaningless and run counter to the object and purpose of many agreements listed in Annex 1 A which were negotiated with the intent to create rights and obligations which in parts differ substantially from those of the GATT 1994."[52] The panel included two possible situations in its definition of conflict: a conflict between two mutually exclusive obligations and a conflict between a permission and a prohibition. It thereby extended the definition of conflict from obligations to situations where obligations and rights confront each other.[53]

In public international law doctrine, the classic narrow definition of conflict seems to prevail. This strict definition has been advocated by Marceau and Trachtman[54], Puth[55] and Wolfrum and Matz[56]. Marceau argues that "if one believes that international commitments should be understood in the light of some coherent international order, one favours narrow definitions of conflict."[57]

However, this strict definition does not seem entirely satisfying. For instance, Pauwelyn objects that states might have the intention to detract from earlier prohibitions by adopting a treaty including a permission.[58] The main negative result of the exclusion of permissions from the definition of conflict is the inapplicability of conflict rules such as *lex specialis* and *lex posterior* for the case of divergences between obligations and permissions.[59] Jenks himself is aware of the fact that such a divergence may "from a practical point of view be as serious as a conflict; it may render inapplicable provisions designed to give one of the divergent instruments a measure of flexibility of operation which was thought necessary to its

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[51] Vranes, 36. For Vranes, norms of conduct encompass permissions, prohibitions and obligations, while norms of competence enable a state or individual to transform by its action a legal situation and to create thereby new norms of conduct (e.g. the power to conclude treaties resp. contracts).

[52] *EC - Regime for the Importation, Sale and Distribution of Bananas* WT/DS27/R, 25 September 1997, para 7.159 and footnote 728.

[53] The panel defined conflict more broadly as "(i) clashes between obligations contained in GATT 1994 and obligations contained in agreements listed in Annex 1A, where those obligations are mutually exclusive in the sense that a Member cannot comply with both obligations at the same time, and (ii) the situation where a rule in one agreement prohibits what a rule in another agreement explicitly permits." (Ibid., para 5.154).

[54] G Marceau and Joel Trachtman, "TBT, SPS, and GATT: A Map of WTO Law of Domestic Regulation" *in* Federico Ortino, Ernst Ulrich Petersmann (eds.), The *WTO Dispute Settlement System 1995-2003*, 2003, pp. 330-331.

[55] Sebastian Puth, *WTO und Umwelt. Die Produkt-Prozess-Doktrin*, 2003, p. 160.

[56] Rüdiger Wolfrum and Nele Matz, *Conflicts in International Environmental Law*, 2003, p. 4

[57] Marceau, 1081-1082.

[58] Pauwelyn, *Conflict of Norms in Public International Law - How WTO Law Relates to Other Rules of International Law* , 174.

[59] Vranes, 19-20.

practicability."[60]

The Appellate Body in *US - Cotton*[61] took a broad view of conflict, accepting that the right to give domestic input subsidy under the Agreement on Agriculture could conflict with and overrule prohibition on domestic input subsidy under SCM agreement, if only this right was specific enough. The International Law Commission has also adopted this definition in its report on fragmentation.[62]

To conclude, while a large amount of debate has taken place in the doctrine, there still is no clear guidance in the case law. A position which constantly adheres to the narrow definition of conflict appears , however, overly restrictive. Similar to the issue of applicable law discussed in the previous section, there seems some need of reform in the case law to allow to give full effect and consider conflicts between MEAs and WTO rules in fact, as the situation of permissions under MEAs conflicting with obligations under WTO rules are highly likely to arise. In the following section, we thus examine how a panel could tackle such a conflict, assuming that it would accept this conflict as one.

B. Norms of conflict

Art. 30 of the VCLT provides for two main rules governing conflicts between treaties relating to the same subject matter and the same parties: 1) specific treaty provisions which regulate conflicts with other treaties must be respected; 2) a treaty over the same subject matter later in time should prevail over a previous one. A third principle, which is not mentioned in the VCLT, but recognized in the case law[63], is the principle of *lex specialis*, according to which the rule which is more specific to a situation should prevail over the more general rule. Since we presume that the ICCP does not include cross-references on its relationship with WTO provisions, only the two other principles are to be examined.[64] It should also be noted at the outset that the relationship between these two rules of conflict is not clearly established.[65] In the future, the inclusion of carefully drafted conflict clauses could avoid the need to resort to these crude rules. As a remedy within WTO law, waivers may be considered by parties.

In order to apply Art. 30 the two conflicting provisions need to be dealing with the same "same subject matter". The term "same subject matter" is not defined in the

[60] Jenks also admits that "such a divergence may, for instance prevent a party to both of the divergent instruments from taking advantage of certain provisions of one of them".
[61] *United States - Subsidies on Upland Cotton* WT/DS267/AB/RW, 2 June 2008.
[62] ILC Fragmentation report, para. 25.
[63] ICJ Advisory Opinion, *Legal consequences of the Construction of a Wall in the Occupied Palestinian Territory*, 9 July 2004, ICJ reports (2004), 136, para 105-106.
[64] It should be underlined that these maxims of conflict follow from the underlying authorization of the legislator to create and modify law, which is an important characteristic of the modern international legal order and is inherent to the principle of state sovereignty (Vranes, 45-50).
[65] Certain authors argue that one principle should prevail over the other (see Pauwelyn: "In sum, the lex posterior rule in Art. 30 is and should remain the rule of first resort", Pauwelyn, *Conflict of Norms in Public International Law - How WTO Law Relates to Other Rules of International Law* , 408). Others defend the position that *lex specialis* and *lex posterior* are at the same level of hierarchy (See W Karl 'Conflict between Treaties', in R Bernhardt, Encyclopeia of Public International Law, vol. 7, 1984, 469)

VCLT. However, it has been advanced that if a conflict exists between two treaty norms, they necessarily deal with the same subject matter.[66]

According to the *lex posterior* rule "later legislation supersedes earlier legislation."[67] International jurisprudence has referred to this maxim at several occasions.[68] Two problems are however related to the application of this principle: First, it is not clear if the assumption that the later treaty expresses the "correct common intent" is always fulfilled. Second, the correct successive order of treaties cannot always be established.[69] Concerning the first problem, assuming that WTO obligations are bilateral in nature,[70] a WTO member should be able to suspend its WTO obligations since it is bound by a MEA in which both countries have agreed to lawfully suspend these obligations. However this holds only true as long as this suspension does not affect the rights of third parties.[71] In the area of Human Rights some examples have shown that WTO members did not contest the suspension of WTO obligations.[72] The second problem is relevant in the presence of two multilateral treaties, where it is difficult to pinpoint the convergence of consent of all states. The point of time of convergence could vary due to different moments of accessions of states to the treaty or due to amendments or revisions of a treaty.[73] Thereby, for certain states the WTO rules might be later in time and for other states the MEA might be later in time.[74] It can also be argued that WTO rules and environmental rules are "continuing treaties", which are continuously confirmed and implemented by judicial organs and that the *lex specialis* principle should consequently be applied.[75]

The *lex specialis* principle stipulates that a law governing a subject matter in a more specific way overrides a law which only governs the matter generally. *Lex specialis* can only exist in reference to a more general law, which requires an often problematic determination on a case by case basis.[76] The relationship between the

[66] Pauwelyn, 365; E Vierdag, 'The Time of the "Conclusion" of a Multilateral Treaty' (1989) 60 British Yearbook of International Law 75, 100. See also ILC Fragmentation Report, 18 para 23. Some scholars suggest that Art. 30 is not applicable in a case where an environmental treaty is in conflict with a trade treaty, because they deal with different subjects, see e.g. C Borgen 'Resolving Treaty Conflicts', 37 George Washington International Law Review 57, 603-604. The ILC, however, argues that classification of treaties has no normative value per se (ILC Fragmentation Report, para. 21).

[67] Jenks, 445.

[68] PCIJ, *Mavrommatis Concessions*, Series A, No 2 (1924), 31; PCIJ advisory opinion, *European Commission of the Danube*, Series B, No 14 (1927), 23.

[69] Vranes, 57.

[70] See J Pauwelyn, 'A Typology of Multilateral Treaty Obligations: Are WTO Obligations Bilateral or Collective in Nature?', 14 European Journal of International Law 907.

[71] Pauwelyn, 945.

[72] For instance, the fact that the WTO did not adopt a waiver concerning members in the Kimberley Process may indicate that the WTO recognizes that such agreement reached outside the WTO does not pose a problem of inconsistency with WTO rules (See J Pauwelyn, 'WTO Compassion or Superiority Complex?: What to Make of the WTO Waiver for "Conflict Diamonds"' (2002-2003) 24 Michigan Journal of International Law 1177). Furthermore, no WTO member challenged the trade embargo imposed by the ILO against Myanmar. In reaction to the failure in responding to the ILO's recommendations, the ILO invoked Art. 33 of its Constitution recommending that ILO members take appropriate measures to ensure that Myanmar did not breach its obligations against forced labour.

[73] Pauwelyn, 378.

[74] Pauwelyn, 375.

[75] Pauwelyn, 378. Vranes argues that the reduction of Art. 30 is not needed.

[76] Martti Koskenniemi wrote in his report : "If a legal subject invokes a right based on "special law", then the validity of that claim can only be decided by reference to the whole background of a legal system that tells how "special laws" are enacted, what is "special" about them, how they are

different branches of international law is not clear and most authors support the view that WTO law cannot exist isolated from international general law. It can represent *lex specialis* or *lex generalis* depending on the context. WTO law trade liberalization rules are considered by some as more general with regard to certain environmental rules.[77] It has also been argued that "a WTO obligation not to restrict trade, irrespective of the product involved, must be seen as less specific than an obligation (or permission) to restrict trade in the specific products A and B".[78]

As a conclusion, both approaches based on *lex posterior* and on *lex specialis* show severe shortcomings when it comes to their concrete application to a case. Panels will have to provide a careful reasoning and might even refrain from entering such discussions by trying to find a way around the very conflict of rules presented to them.

4.1.3. Conclusion

The role of international law in WTO dispute settlement raises difficult questions which the case law has in many instances not satisfactorily answered. While an application at the interpretative level would probably not prove very contentious, it may not offer a convincing solution with legal relevance for the outcome of the present case. The Appellate Body has taken a rather restrictive approach on the question of applicability of non-WTO rules of international law, although it seems to keep the door slightly open in the *Mexico Soft Drinks* case. Once application of non-WTO rules is admitted, not all problems are, however, solved. The definition of a conflict can prove difficult at this point. The WTO case law has not been coherent on this point, but seems to define conflict as a clash between two obligations leaving permissions aside. Whereas a provision requiring the increase of duties would fall under a narrow definition of conflict, a provision providing for a permission to impose duties can only be considered to be in conflict with an obligation if a broader definition of conflict is adopted. Even if this troublesome current state of the case law should be overcome, the norms of conflict which would have to be applied do not necessarily seem to provide a satisfactory solution. Neither the rule *lex posterior derogat priori* nor the *lex specialis* principle are easily applicable in practice. Finally, much depends on who is called to determine the violation of the ICCP in the first place. If a multilateral determination by all parties to the ICCP is foreseen (e.g. a decision of the conference of the parties), WTO adjudicative bodies are more likely to accept and follow this assessment. A unilateral determination by one ICCP member to impose sanctions would first have to be verified by a panel and may therefore encounter more reluctance (see also section 4.2.4.5.).

4.2. Trade measures based on a MEA against a non-party

4.2.1. History of the debate and classification of trade measures against third parties

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implemented, modified and terminated." *Report of the International Law Commission on the Fragmentation of International Law*, para. 122.

[77] J Pauwelyn, 'The Role of Public International Law in the WTO: How Far Can We Go?' (2001) 95 American Journal of International Law 535, 540.

[78] Pauwelyn, 389.

A substantial amount of debate on this issue has taken place at an earlier stage. In the early 1990s the Montreal Protocol began to unravel its effects after its entry into force and several amendments. Part of the parcel were trade restrictions in the form of both import and export bans from and to non-parties of products containing ozone-depleting substances or made with but not containing such substances.[79] At the same time, the first *Tuna/Dolphin* report[80] by a dispute settlement panel seemed to restrict severely the possibilities for states to pursue environmental policies with measures reaching beyond their jurisdiction and aiming at a policy change in other countries. In addition, distinctions between products based on their production process in their state of origin as a crucial tool for environmental policies were also held to be inadmissible.[81] Several scholars have discussed the problem and mostly focused on the potential for such trade measures to find justification in Article XX.

4.2.2. The character of extra-tariffs as a violation of WTO law

As discussed in the previous section, extra-tariffs most likely constitute a violation of WTO law. They certainly breach Article II:1 of the GATT according to which WTO members have to respect the level of tariff concessions which they have engaged in. In addition, as the extra-tariffs apply selectively, most favoured nation treatment is certainly violated as well. Should the tariffs target specific groups of products and aim more at offsetting competitive disadvantages for domestic industries, they could transform into something similar to border tax adjustments (see section 4.3 for a closer discussion). However, at this stage the analysis under Article XX focuses closer on the distinction between extra-tariffs capable to justify as an off-setting measure and tariffs as a means to punish free-riders which are more difficult to justify.

4.2.3. Consent in international law and trade measures against non-parties to a MEA

As a crucial preliminary step, the situation has to be clearly distinguished from the one discussed in the previous section: The party targeted by trade measures in the present scenario has in no way consented to the MEA upon which the measures are based. There is, thus, no issue of a potential conflict of norms as in the previous scenario. The principle of state consent underlying public international law prevents the use of the MEA be it as a means of interpretation in relations between the parties or be it at the level of applicable law. Two consequences arise out of the lack of consent in the present setting.

First, as suggested already in early literature, the idea has been expressed to apply the classic conflict rules of international law in cases of overlap between GATT 1947 obligations and MEA obligations.[82] However, *lex posterior* and other conflict rules

[79] Brack, 276.
[80] *United States – Restrictions on Imports of Tuna* DS21/R, BISD 39S/155 (report from 3 September 1991, not adopted).
[81] J Jackson, 'World Trade Rules and Environmental Policies: Congruence or Conflict?' (1992) 49 Washington & Lee Law Review 1227, 1243.
[82] B Baker, 'Protection, not Protectionism: Multilateral Environmental Agreements and the GATT' (1993) 26 Vanderbilt Journal of Transnational Law 437, 446.

are not applicable in a situation where the second party is not bound by the international obligation at stake.

Second, systemic integration in interpretation as suggested by Article 31(3)c Vienna Convention on the Law of Treaties is inapplicable as well. If resort to this provision is possible because of the ambiguity of a treaty term, this norm suggests that "any relevant rules of international law applicable in the relations between the parties" should be taken into account in the interpretation.[83] However, the addressee of the measures is not party to the rule which can thereby not contribute at this level to the interpretation of WTO law.

As an additional argument, the example of the Kimberley Process Waiver demonstrates that in the present scenario WTO law is the only applicable law and a justification under this regime has to be found for the trade measures. WTO members phrased the waiver in this case as exempting only trade restrictions against non parties to the Kimberley Process. Therefore, they seemed to perceive that trade restrictions against parties would not breach WTO law in the first place.. It can, thus, be concluded from the perceived need for a waiver by the WTO members that trade measures based on a MEA against non-parties to the agreement are WTO violations and do require an express derogation from the rules to be acceptable or have to find at least justification for example under the derogations of Article XX GATT.[84]

To conclude, the only potential justification for the violations under GATT caused by extra-tariffs against a non-party to a MEA constitutes Article XX. This is, however, not to say that the MEA's provisions are irrelevant. They can, as has been suggested by several scholars,[85] play an important role in the different determinations which have to be made under the analysis foreseen in Article XX.

4.2.4. Justification under Article XX

WTO panels and the Appellate Body have developed a sophisticated test over the years to verify whether a state's measure truly pursues one of the legitimate public interests laid out in Article XX or whether there are protectionist elements in the measure which have to be struck down. A MEA which underlies the measure taken by the state can play a useful role as evidence in favour of the pursuit of such a legitimate interest at several stages in the analysis, as will be shown. Different steps have to be distinguished: First, the debate on measures which aim at a policy change in other states has to be assessed (4.2.4.1.). Second, it should be discussed whether there is a requirement for multilateral measures in the WTO instead of unilateral action by one state based on its own policy goals (4.2.4.2.). Then, the analysis under Article XX *stricto sensu* begins: The exact aim pursued by the measure has to be assessed to classify it subsequently under one of the derogations foreseen in Article XX (4.2.4.3.). Furthermore, depending on the classification under a heading of Article XX, different tests of reasonable connection between the measure and the aim pursued have to be fulfilled (4.2.4.4.). If the relevant test is fulfilled, the measure is considered to be

[83] Elizalde Carranza, , 91.
[84] Pauwelyn, 'WTO Compassion or Superiority Complex?', 1181.
[85] See for example Baker, 454; J Donoghue, 'The Trade Provisions of International Environment Agreements: Can they be reconciled with GATT?' (1992) 86 American Society of International Law Proceedings 233, 236; Elizalde Carranza, 88.

provisionally justified. As a final threshold the introductory clause of Article XX – the so-called chapeau – prescribes that no unjustifiable or arbitrary discrimination or disguised trade restrictions may be created at the level of application of a measure (4.2.4.5.). Only if all these conditions are met, a measure is considered to be justified by the relevant exception under Article XX.

4.2.4.1. Environmental measures aiming at a policy change in other countries

Many measures of environmental policy aim at persuading another country to change its policy. Measures often distinguish for this purpose based on how a product was produced. While in the early 1990s, GATT 1947 panels have taken a negative stance on such process-based distinctions and restrictions,[86] the later case law has overcome the bias. In *US-Shrimp*, the Appellate Body held that "conditioning access to a Member's domestic market on whether exporting Members comply with, or adopt, a policy or policies unilaterally prescribed by the importing Member may, to some degree, be a common aspect of measures falling within the scope of one or another of the exceptions (a) to (j) of Article XX. […] It is not necessary to assume that requiring countries compliance with, or adoption of, certain policies […] renders a measure *a priori* incapable of justification under Article XX."[87]

The use of persuasive measures is, thus, perceived as an admissible tool under Article XX policies by the Appellate Body.[88] Extra-tariffs imposed under a MEA on a non-party can therefore still find justification under Article XX even if they pursue the aim of inducing a policy change in the targeted country, the latter being persuaded to join the agreement and to abandon a free-rider position. Scholars argue that a MEA as a basis for trade measures should support overcoming the strict focus on territorial jurisdiction and the latter's boundaries which appears unsuitable to deal with most measures of international environmental policy.[89] The usefulness of Article XX would be unduly reduced by such a restrictive approach.

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[86] *US - Tuna I and United States – Restrictions on the Imports of Tuna* DS29/R (panel report from 16 June 1994, not adopted); for a short, but succinct summary of the cases see S Jinnah, 'Emissions Trading under the Kyoto Protocol: NAFTA and WTO Concerns' (2002-2003) 15 Georgetown International Environmental Law Review 709, 724-727. In a similar vein, Jackson depicts the use the United States made of Article XX in their regulation as inadmissible "eco-imperialism", Jackson, 1241.

[87] *United States - Import Prohibition of Certain Shrimp and Shrimp Products* AB-1998-4, WT/DS58/AB/R, 12 October 1998, para 121.

[88] Section 4.3. will address the issue of process-based restrictions in more detail. As concerns Article XX, the Appellate Body has admitted a process-based distinction in the form of an import ban in *US – Shrimp*, which has been welcomed by part of the doctrine, see S Charnovitz, 'The Law of Environmental "PPMs" in the WTO: Debunking the Myth of Illegality' (2002) 27 Yale Journal of International Law 59.

[89] Baker, 459-460. A similar argument is brought forward in a different context: Woody suggests in her discussion of the Kimberley Process scheme which establishes certain trade barriers on "conflict diamonds" that Article XX GATT should be available as a justification for such restrictions. In her view, the multilateral process which lead to the trade barriers takes matters beyond an issue of mere jurisdictional overreach and leads to a result where no domestic standard is imposed upon others, but a multilaterally agreed standard, KE Woody, 'Diamonds on the Souls of her Shoes: The Kimberley Process and the Morality Exception to WTO Restrictions' (2006-2007) 22 Connecticut Journal of International Law 335, 351.

4.2.4.2. A requirement for multilateral instead of unilateral action in WTO law?

Furthermore, it has sometimes been argued that there is a requirement for multilateral action in the WTO. Trade measures which are imposed unilaterally such as the tariffs in our example would, thus, be less likely to be accepted by a panel, even if they were based upon the provisions of a MEA. It is suggested here that, while the case law has recognized that certain challenges of regulatory policy are better to be tackled by negotiations and multilateral agreements, unilateral approaches such as trade measures in the present scenario are still a valid instrument admitted by WTO law under certain conditions. No general exclusion of unilateralism can therefore preclude us from proceeding to the precise analysis under Article XX.

The concerns against unilateral action go back to the mentioned *Tuna/Dolphin I* case under GATT 1947, where the panel held that measures to persuade a policy change in another country would only be admissible if adopted by all parties.[90] In newer case law, the Appellate Body seemed to express for some a requirement of a multilateral approach, although in less explicit terms.[91] However, much of the often cited "duty to negotiate" clarified both in *US – Shrimp*[92] and in *US – Shrimp (Recourse to Article 21.5 DSU)*[93] has to be traced back to the specificities of the case. Furthermore, the Appellate Body beyond any doubt accepted unilateral action by the United States in this case. In addition, in *US – Gambling* the Appellate Body rejected claims that a measure could not be justified as necessary under Article XX because there had not been consultations and negotiations.[94] Such negotiations should be seen as a process and not as a result which could replace other unilateral measures in all situations.

As a conclusion, the case law does not establish a requirement for multilateral action. The Appellate Body seems to be willing to take into account MEAs and we shall similarly use the MEA as a basis in the evaluation under the different steps of the analysis Article XX. Having said that, there is no guarantee that a mere link to a multilateral basis will save unilaterally imposed trade measures such as extra-tariffs, despite the Appellate Body's encouraging statements in *US – Shrimp*[95] or similar views expressed in earlier doctrine.[96]

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[90] *US - Tuna I, para 6.4.*
[91] Elizalde Carranza, 61.
[92] *US - Shrimp* .
[93] *United States - Import Prohibition of Certain Shrimp and Shrimp Products (Recourse to Article 21.5 of the DSU by Malaysia)* AB-2001-4, WT/DS58/AB/RW, 22 October 2001. The United States' legislation at issue provided for a duty to negotiate, which the United States had only followed in relation to some countries, while others had not been given the chance of good faith negotiations. Discrimination in the application of the legislation was thus the main reason for the United States to be condemned. See R Howse, 'The Appellate Body Rulings in the *Shrimp/Turtle* Case: A New Legal Baseline for the Trade and Environment Debate' (2002) 27 Columbia Journal of Environmental Law 491 for a detailed comment of the cases.
[94] *United States - Measures Affecting the Cross-Border Supply of Gambling and Betting Services* AB-2005-1, WT/DS285/AB/R, 7 April 2005, para 317.
[95] *US - Shrimp, para 168,* wherein the Appellate Body emphasized that certain tasks such as the conservation of migratory species "demand" concerted and cooperative efforts of many countries.
[96] Baker, , 454, DJ Caldwell, 'International Environmental Agreements and the GATT: An Analysis of the Potential Conflict and the Role of a GATT "Waiver" Resolution' (1994) 18 Maryland Journal of International Law and Trade 173, 186.

4.2.4.3. The policy objective of the measure and the headings under Article XX

After these preliminary considerations, the conditions of Article XX have to be scrutinized to determine whether extra-tariffs imposed against a non-party to a MEA can be justified under WTO law.

As a first step, the policy objective pursued by the measure has to be identified. Arguably, the MEA upon which the extra-tariffs are based should be taken into account at this moment.[97] While the measure imposed are extra-tariffs with the aim to prevent free riding, the MEA in our scenario aims at preventing climate change by means of imposing emission restrictions and creating mechanisms for the latter purpose. A vast environmental challenge such as climate change can certainly be compared to the protection of migratory species, where the Appellate body has admitted the need for "concerted and cooperative efforts".[98] The phenomenon of climate change is transboundary by definition and cannot be addressed by individual states. For any meaningful action, concerted efforts must play a central role. In this light, the objective pursued by extra-tariffs imposed against non-parties to a MEA on climate change dissuades such non-parties from free-riding on efforts of parties to a MEA and should be seen as linked to the objective of the MEA which can only be reached by means of concerted action.[99]

The determination of the objective is not only important to classify the measure under one of the headings of Article XX, it constitutes at the same time a crucial benchmark for the determination required later whether a measure is "necessary" to reach the objective.[100]

Having established the aim of the extra-tariffs as the dissuasion from free-riding, two headings for such environmental regulatory objectives are available. First, under Article XX(g) conservation of natural exhaustible resources can be pursued. In *US – Gasoline*,[101] the Appellate Body confirmed that clean air could be considered as a resource which was depleted and thereby exhausted by means of air pollution. In a similar vein, climate change could be perceived to fit the same category. Greenhouse gases are polluting Earth's atmosphere and thereby inflict negative influence upon the climate. In addition, the term "natural exhaustible resource" has already been read by the Appellate Body in an evolutionary manner taking into account the development of international environmental law,[102] suggesting a potential of flexibility for this exception to address also "new" concerns such as climate change.

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[97] Baker, 463, shows similarly that in an early dispute case under the US – Canada Free Trade Agreement a conservation measure was struck down by a panel because it omitted to look at a MEA upon which the measure was based and which could have provided a plausible rationale for the measure at issue.

[98] *US - Shrimp, para 168.*

[99] Some scholars have also suggested that the existence of a MEA on an environmental problem can increase the credibility of the same regulatory objective even if pursued by a state unilaterally, Brack, 284-285.

[100] B McGrady, 'Necessity Exceptions in WTO Law: Retreaded Tyres, Regulatory Purpose and Cumulative Regulatory Measures' (2008) 12 Journal of International Economic Law 153, 157, argues that where a panel does not clearly establish the regulatory purpose of a measure, it is given disproportionate discretion to judge the necessity of a measure in the abstract.

[101] *US - Gasoline* .

[102] *US - Shrimp, paras. 129-132.*

Second, Article XX(b) allows measures to protect public health and could, thus, provide a heading for the tariffs. A legitimate argument could be made that the fight against climate change addresses rather the consequences implied by the phenomenon, which affects human, animal and plant life and health negatively. Article XX(b) could be considered as the more suitable heading in this light. As a practical consequence, a stricter test of rational relation between the objective pursued and the measure itself has to be fulfilled. However, contrary to the direct aim of conservation of a balanced atmosphere under Article XX(g) described previously, it appears questionable to classify the fight against climate change under Article XX(b). The measures taken are aimed at the phenomenon itself, not so much its outcome, as they aim at emission reductions rather than merely at passive adaptation to the consequences. In addition, many measures of conservation policy constitute a step to prevent an actual negative effect on public health under Article XX(b), if – for example – certain species are protected to safeguard an ecosystem without whose functioning more severe environmental consequences would have to be expected.[103] To allow a classification of policy so closely related to conservation under Article XX(b) instead of Article XX(g) appears to deprive the latter provision of much of its scope.

To conclude, while a classification of extra-tariffs to dissuade free-riders from a MEA under Article XX(g) appears more intuitive, it is hard to foresee which road a panel would take.[104] We shall, thus, examine the following steps of the analysis under Article XX taking into account both possible solutions.

4.2.4.4. The rational relationship between the policy objective and the measure

While under Article XX(g), trade measures have to be taken "relating to" the conservation of exhaustible natural resources, Article XX(b) requires them to be "necessary" to protect human, plant or animal life or health. Two different tests have, thus, been developed by the WTO judicial bodies.

4.2.4.4.1. "Relating to" in Article XX(g)

The Appellate Body has observed that in order to fulfil the requirements of this provision, a measure must show a "close and genuine relationship of ends and means".[105] The threshold established is lower than the standard under necessity, which means that there is no comparison between an environmental benefit achieved and the trade effects caused by a measure.[106] Rather, a mere rational connection between the different aspects of a measure and its objective is required. Extra-tariffs imposed under a MEA against non-parties should be able to meet this threshold.

[103] To draw the analogy further, even in the *US – Shrimp* case the panel could have stated that next to the conservation efforts there were also potentially hazardous consequences for the ecosystem of the oceans in case of disappearance of sea turtles and could have examined the claims under Article XX(b).
[104] A Green and T Epps, 'Is There a Role for Trade Measures in Addressing Climate Change?' (2008-2009) 15 UCDavis Journal of International Law and Policy 1 15-16, agree that both headings could be used to justify measures in the fight against climate change, but refrain from taking a position in favour of a particular heading.
[105] *US - Shrimp, para 136.*
[106] In departure of how earlier panel reports under GATT 1947 had interpreted Article XX(g), compare Howse, 503-504.

Unless tariffs would be truly designed in a blatantly protectionist manner in favour of the imposing country, a panel would hardly doubt that the tariffs can bring a contribution towards dissuading free-riders and are linked in a rational manner to this objective. It is another question beyond the review of Article XX(g)'s requirements whether extra-tariffs are the most effective means or likely to achieve the objective pursued.

The MEA as underlying such tariffs provides evidence that such measures are seen by a broad community of states as a suitable means for pursuing the target of dissuading free-riders. This is in particular the case where a MEA prescribes the use of such trade measures explicitly. At the same time, even a permission of such action in a MEA shows a similar conviction and should in our view be taken into account by a panel. Even a mere recommendation issued by a conference of the parties to a MEA can be read in this light. A panel should not simply overlook such evidence even if the targeted WTO member is not party to the MEA at issue. The case for using the MEA might be even stronger if the relevant MEA includes some language to link MEA disciplines with the rights and obligations under other instruments of international law, as it is often the case concerning international trade rules.[107]

As another crucial element, Article XX(g) provides that in order to find justification, conservation measures have to be "made effective in conjunction with restrictions on domestic production or consumption". At this point, a WTO member has to show coherence in its climate change policy and its respect of eventual MEA obligations. Sanctions for non-parties would have to be linked clearly to domestic climate change policy. Mere adherence to a MEA would probably not be sufficient.[108] Rather, a sanctioning regime such as the tariffs must be shown to be linked to a functioning domestic regime which is negatively affected in its struggle towards the overall objective by the free-riding of non-parties to a MEA.

In sum, chances that such tariffs can find provisional justification under Article XX(g) are open, but depend on the care with which the extra-tariff regime is designed and its coherence with domestic climate change policy.

4.2.4.4.2. "Necessary to" in Article XX(b)

Departing from GATT 1947 panel practice,[109] "necessary to" has already for a long time been perceived as implying a less trade restrictive/less GATT inconsistent alternative test. In a later series of cases,[110] the Appellate Body has taken matters further by introducing some new elements and creating an overall "weighing and balancing" test which calls for a more holistic exercise, taking into account other factors next to the existence of less trade restrictive alternatives.

[107] See for some examples Elizalde Carranza, 83-84.
[108] Jinnah, 736.
[109] See for but one important example *Thailand – Restrictions on Importation of and Internal Taxes on Cigarettes* DS10/R, BISD 37S/200 (panel report adopted on 7 November 1990).
[110] In particular *Korea - Measures Affecting Imports of Fresh, Chilled and Frozen Beef* AB-2000-8, WT/DS161/AB/R and WT/DS169/AB/R, 11 December 2000 and *European Communities - Measures Affecting Asbestos and Asbestos-Containing Products* AB-2000-11, WT/DS135/AB/R, 12 March 2001.

In *Korea – Beef*, the Appellate Body has spelled out different elements of the test[111] under the necessity criterion as applied today:

> "In sum, determination of whether a measure, which is not 'indispensable', may nevertheless be 'necessary' […] involves in every case a process of weighing and balancing a series of factors which prominently include the contribution made by the compliance measure to the enforcement of the law or regulation at issue, the importance of the common interests or values protected by that law or regulation, and the accompanying impact of the law or regulation on imports or exports."[112]

The Appellate Body examines all the mentioned and puts reasonably available alternative measures which restrict trade less in addition in the scales. The following section examines, thus, step by step the different tiers of this test.

As a preliminary thought, since only measures "which are not 'indispensable'" have to pass the test, it can be concluded that there is a category of "indispensable" measures which in any case is justified as necessary.[113] It is, however, unlikely that extra-tariffs are perceived as perfectly indispensable to achieve the dissuasion of free-riders in the present case, which is why they are subject to the balancing test as developed by the Appellate Body.

In the first tier of the test, the MEA plays an important role in evaluating the importance of the common interest or value protected at issue. A multilateral agreement on the importance to tackle climate change has a good chance of tipping the balance of the weighing and balancing test in favour of the country implementing the extra-tariffs. To date, the case law has hardly really shown any tendency to truly create a hierarchy of common interests, but constantly confirmed that the regulatory objective of WTO members was important in every single case. It is, thus, unlikely that a change to this approach would happen at the occasion of measures aiming to contribute to the fight against climate change.

When at the following stage the Appellate Body adds the contribution of the measure and the trade restrictive impact to the picture, As regards the contribution of a measure towards the regulatory objective, panels have already in earlier days referred to documents of international organizations as evidence.[114] An excessively high short

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[111] The test has proved challenging in its application for panels, as recent case law has shown. The Appellate Body therefore was asked to clarify the sequence of the different steps of the test under the necessity condition. In *China - Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products* AB-2009-3, WT/DS363/AB/R, 21 December 2009, paras 247-249, the Appellate Body made clear that all the elements of the necessity test and the weighing and balancing formula have to be undertaken, while the fact that the panel did not proceed in the same manner and sequence for each of different measures under scrutiny did not cause concern.

[112] *Korea - Beef, para 164.* There have initially been arguments that some elements of this formula are due to the specific facts of the case and based on the fact that the Appellate Body was called to interpret necessity under Article XX(d). However, the Appellate Body has since then repeated this test several times and constantly referred back to *Korea – Beef*, which is why one can depart from the validity of these statements for future cases.

[113] DH Regan, 'The meaning of 'necessary' in GATT Article XX and GATS Article XIV: the myth of cost-benefit balancing' (2007) 6 World Trade Review 347, 357-358.

[114] See in this respect the panel in *Thailand - Cigarettes* , para 78, which refers to a resolution taken in the framework of the World Health Organization.

term trade disruptive effect caused by the extra-tariffs could cause concern if only a merely marginal persuasive effect as a contribution is achieved. To date, the weighing and balancing test has rather functioned as an emergency brake in rare cases and has not generally be used for the purpose of a true deepened scrutiny in the sense of true proportionality. It has shown its bite in *Korea – Beef*,[115] where the Appellate Body held that the measure implemented by Korea was too trade restrictive in relation to the benefit achieved towards the level of protection which Korea had indicated. Similarly, in the recent *Colombia – Ports* case[116] a panel held that the contribution of ports of entry restrictions towards the goal of fighting practices such as smuggling was not sufficiently established to pass the test. In the present scenario, the existence of a MEA which prescribes or at least authorizes such extra-tariffs is, arguably, seen by a panel as an indication that this form of trade measure has at least basic utility and should not be condemned as excessively trade restrictive. Rather, the main obstacle for extra-tariffs in the different phases of the test probably is the qualification as the least trade restrictive alternative to which we now turn.

Under this crucial part of the overall test, a comparison with alternative measures is undertaken. Such an alternative measure must achieve the same contribution towards the level of protection established by a WTO member for the pursuit of the public interest at issue. However, only if such an alternative measure can contribute to the same degree and is at the same time less trade restrictive, the "test of necessity" may not be fulfilled. As a third qualification, the Appellate Body has consistently held that such an alternative measure must be "reasonably available", which calls for an evaluation of the administrative costs and technical difficulties imposed upon a country when implementing the alternative instead of the original measure.[117]

In a departure from the usual rules on burden of proof, the existence of such alternative measures has to be shown by the complaining member in a WTO dispute.[118] The defending member does not have to think of every potential alternative and deny its applicability, but merely has to react on the alternatives suggested by his opponent and show that they should be dismissed.

As a first step, the contribution towards the objective pursued has to be established.[119] Similarly to the analysis under Article XX(g), a rational relationship of ends and means between the features of the measure and the objective have to be shown. The measure should be apt to make a material contribution beyond a mere marginal or insignificant one, in particular if a severe trade restrictive effect is caused.[120] The positive effect of extra-tariffs to persuade free-riders to join a MEA should not be too difficult to show unless they are excessively protectionist in design, as has been discussed under Article XX(g). Again, the MEA can serve as useful evidence of the perception of a broader community of states that such action can usefully tackle the

[115] *Korea - Beef* .
[116] *Colombia - Indicative Prices and Restrictions on Ports of Entry* Report of the Panel, WT/DS366/R, 27 April 2009.
[117] See e.g. *US - Gambling, para 308.*
[118] Ibid., paras 309-311.
[119] Both a quantitative and a qualitative assessment are admissible for this purpose, see *Brazil - Measures Affecting Imports of Retreaded Tyres* AB-2007-4, WT/DS332/AB/R, 3 December 2007, para 146.
[120] Ibid., para 150.

free-rider problem, be it as requiring, authorizing trade measures or merely recommending them in the framework of its institutional activity.

As a next step a comparison with less trade restrictive alternatives takes place. There might be other measures which could achieve a similar dissuasive effect upon a free-riding non-party of a MEA without the potentially highly disruptive effect on trade relations caused by extra-tariffs. However, it should be noted that the Appellate Body has clearly stated that WTO members can freely pursue policy objectives by means of a comprehensive program which encompasses several instruments with different contributions towards the overall goal.[121] A scholar suggests convincingly that accordingly a panel should not perceive a measure as an alternative if it is merely a different part of the parcel with its own, distinctive contribution, even if it is less trade restrictive than the disputed instrument.[122]

Extra-tariffs would almost immediately be challenged as too trade restrictive and as a breach of perhaps the most central pillar of the GATT system of trade liberalization commitments: the tariff concessions and the stand still obligation. At this point, a classification of trade measures in MEAs helps in evaluating which measures can be considered as potentially complementary or rather cumulative.

Green and Epps[123] provide a useful scheme, according to which trade measures under MEAs can fall into three categories. First, they can act as a "carrot" and provide incentives to other states to engage more in a common struggle.[124] A "stick" approach punishes for example by means of extra-tariffs in cases of non-compliance of a party or in cases of non-participation for non-parties.[125] As a middle-way between carrots and sticks, some measures such as border adjustments aim at eliminating distortions of competition for domestic industries.[126]

Arguably, in order to find an alternative, the "category" of trade measures should not be overstepped. Border tax adjustments bring a different contribution than the extra-tariffs at issue and should therefore not be considered as a less trade restrictive alternative. A case could, however, be made for incentive-based systems which offer for example financial assistance to facilitate adhesion to a MEA.[127] However, their positive contribution would have to be scrutinized on whether it achieves a similar level as the extra-tariffs. The determination appears highly complicated and certainly changes from country to country. Returning to the tariffs, badly drafted extra-tariffs could be struck down as inadequate in favour of a regime which is more aimed at

[121] Ibid., para 151.
[122] McGrady, 'Necessity Exceptions in WTO Law: Retreaded Tyres, Regulatory Purpose and Cumulative Regulatory Measures' 167, who emphasizes that these admissible complementary measures have to be distinguished from merely cumulative measures which offer and add up the same material contribution. The latter can legitimately be perceived as alternatives to each other in his view.
[123] Green and Epps, , 8.
[124] Such incentives work in a comparable manner to the Generalized System of (tariff) Preferences which the EU or the US use to favour certain policies in development cooperation.
[125] Green and Epps, 9.
[126] Compare to this the distinction as envisaged by Hudec between "altruistic" measures which aim at changing the behaviour of others and "level-the-playing-field" measures which set off advantages free riders would enjoy otherwise, cited in C Fletcher, 'Greening World Trade: Reconciling GATT and Multilateral Environmental Agreements within the Existing World Trade Regime' (1995-1996) 5 Journal of Transnational Law and Policy 341, 361.
[127] Donoghue, 237.

increasing the incentive to adhere and less to target specific sectors or provide a competitive advantage for the industries of the imposing country.

As an additional consideration, it has to be kept in mind that extra-tariffs hurt both the targeted country, but also the imposing country in economic terms. An extra-tariff regime could therefore also fall foul under the necessity test if, as the Appellate Body stated, its trade effect is "severe", while its contribution, i.e. the persuasive effect it produces, remains "marginal or insignificant".[128] A problem might arise in particular because "punitive" extra-tariffs are likely to cause high trade damage in the short term without necessarily achieving the desired reaction in the targeted state.[129] In this light, it is hard to foresee how a WTO panel would finally judge such extra-tariffs. The more intense the scrutiny, however, the more likely these measures are to fail the "necessity" test because of their highly trade restrictive effect.

Lastly, a mere suggestion that negotiations and consultations constitute valid alternatives to the tariffs is likely to be rejected, as previously discussed in the field of a requirement in WTO law for multilateral approaches.[130] There have been ongoing negotiations which were open to all countries and led in good faith. Negotiations do not contain an obligation to reach a result as the case law has shown. Therefore, the treatment of different trading partners in the negotiations would meet some scrutiny by a panel under the chapeau. No exclusion of extra-tariffs is, however, likely merely because the multilateral process at issue has not managed to include all countries in the final agreement.

Next to these substantive issues, the role of the MEA merits attention. In determining whether there are less trade restrictive alternatives, as a first step the MEA could again serve as formal evidence that a multitude of states perceived such action as needed. The point is certainly emphasized in case of a MEA which explicitly requires such sanctions. It is suggested that it would render it difficult for a panel to reject extra-tariffs in such a situation in favour of some less trade restrictive alternative. If a MEA merely allows such extra-tariffs, there is more discretion given to the MEA party. A panel could go into more detail, taking into account the previous considerations, and prescribe a less trade restrictive approach. In case of a mere recommendation f.ex. issued by a conference of the parties of a MEA a similar approach is likely to be taken by a panel. The MEA would be taken into account, but the use made of the existing discretion given to a MEA party in imposing sanctions against a non-party would still come under close scrutiny by a panel.

As a final issue, an alternative measure accepted as such by a panel still has to meet the threshold of being "reasonably available". A country defending the tariffs in front of a panel could argue that the implementation of an alternative measure is

[128] *Brazil - Tyres, para 150.*
[129] Severe doubts on the effectiveness of such tariffs are set out by Green and Epps, 26.
[130] Some scholars still seem to argue in favour of a duty to negotiate in WTO law before using other measures, see Jinnah, 735. Others, however, more convincingly consider that the case law mainly emphasizes the requirement for equal treatment of all partners if a negotiation process is engaged rather than a duty to negotiate in itself, see e.g. in the field of human rights sanctions M Ewing-Chow, 'First Do No Harm: Myanmar Trade Sanctions and Human Rights' (2006-2007) 5 Northwestern University Journal of International Human Rights 153, 167.

excessively costly or faces important technical obstacles.[131] In particular developing countries could, thus, successfully argue that suggested alternatives have to be put aside as not being reasonably available, since extra-tariffs as a tool are rather easy to implement. Regulatory approaches involving complex tasks for the legislator and comprehensive supervision could be rejected as a consequence depending on the circumstances in each country.

As a brief conclusion for the rational relationship test under Article XX, there is some chance for extra-tariffs imposed under a MEA against non-parties to qualify and be justified. However, the scrutiny of a panel is quite intense in particular concerning the required qualification of a measure as the least trade restrictive alternative, as the *Brazil – Tyres* case has shown.[132] The discussed factors add some doubt on whether they are really able to meet the overall standard.

4.2.4.5. The requirements of the introductory clause (chapeau) of Article XX

As a final hurdle, the chapeau of Article XX prevents abusive use of the exceptions. It therefore establishes three standards that apply at the level of application[133] of a measure. A measure must not amount to an "arbitrary" or "unjustifiable" discrimination between countries where the same conditions prevail. These first two conditions have in most cases been tested by the Appellate Body together.[134] Thirdly, a measure may not amount to a "disguised restriction on international trade". This third element has been found to constitute a clause against abuse similar to the overall rationale of the chapeau.[135] Beyond a mere obligation of transparency the requirement could find a wide field of application to set in practice the "fundamental theme" of avoiding abuse or illegitimate use of the exceptions. [136] In practice, however, the relevance of the third element has proved very limited to date.

In the most explicit case on the chapeau to date,[137] the Appellate Body interpreted the provision as a requirement for flexibility in regulatory programmes. Unjustifiable discrimination in this sense requires flexibility concerning the substance of the application of a measure: For example, conditioning market access upon a comparably effective regulatory programme would fall under this notion. Arbitrary discrimination takes a more procedural approach: In the application of a measure, certain minimum procedural guarantees have to be respected. Other countries have to be heard in a transparent manner and in case they do not receive market access, some way of appeal should be opened.[138] Finally, concerning the issue of discrimination "between countries where the same conditions prevail" the Appellate Body clarified

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[131] See in this respect *US - Gambling, para 308,* where the Appellate Body notes that "prohibitive costs or substantial technical difficulties" render a measure unavailable.
[132] *Brazil - Tyres, paras 133-175.*
[133] The very possibility of separating strictly between the application and the legislative basis of a measure is, however questioned by some, see generally A Davies, 'Interpreting the Chapeau of GATT Article XX in Light of the 'New' Approach in Brazil-Tyres' (2009) 43 Journal of World Trade 507 or P Mavroidis, *The General Agreement on Tariffs and Trade - A Commentary* (Oxford University Press, Oxford 2005), 213.
[134] *US - Shrimp, para 118.*
[135] *US - Gasoline, p. 25.*
[136] Ibid., p. 25.
[137] *US - Shrimp, paras 164-165.*
[138] J Pauwelyn and A Guzman, *International Trade Law* (Aspen Publishers, New York 2009), 391.

that both the importing country and exporting countries are to be understood as part of the comparison.[139]

For trade measures under a MEA it resorts that again the use of an eventual margin of manoeuvre given to a party state in imposing such extra-tariffs on a non-member may play a crucial role in the determination of whether the chapeau's requirements have been met. If the relevant MEA provides some similar language to the chapeau, harmonious interpretation could help,[140] but would not avoid the strict scrutiny by the panel of how the relevant country actually implements the tariffs in action. As the issue is rather the practical transposition into national law and administrative practice of the MEA's provisions by a state rather than the text of the agreement, its terms are of less significance as evidence under the chapeau.

In its scrutiny, a panel would first focus on whether the system of extra-tariffs as established by a state permits to take into account the relevant circumstances of the targeted country. Some leeway should exist to accept explanations of why adherence to a MEA is for example delayed or momentarily impossible due to technical considerations. In addition, as discussed before, some procedural alley should be available for the targeted country to justify its non-adherence. This could go as far as a requirement to provide for exceptions from the imposition of extra-tariffs if another country can show that by means of its own policy, it pursues the struggle against climate change with equivalent results, e.g. by its own emission trading scheme which is not based on the same MEA or on no MEA at all. Lastly, the design and concrete practice of the imposition of extra-tariffs must not reveal protectionist motives, whereby certain countries are singled out and disadvantaged to protect the imposing country's industry or create unpredictable or discriminatory obstacles to trade for the targeted country, while there are no distinctive characteristics to the situation of that country which would justify such action.

Whether an exemption from trade measures is based upon a multilateral or a merely individual assessment may also influence a panel's view. Multilateral determination of which countries are to be exempted will probably be seen with more deference by a panel.[141] As the main rationale underlying the chapeau of Article XX is to prevent abuse – mostly for protectionist purposes – a multilateral determination of the need to exempt a specific non-party to a MEA from the imposition of extra-tariffs could eliminate some suspicions; for example that a single state is acting against another merely to favour the other at the expense of third states or is applying the extra-tariffs in a manner causing arbitrary discrimination among trading partners.

As an additional consideration, some suggest that a regime of persuasive measures should treat non-participation in a MEA in the same or at least similar manner as non-compliance to be legitimate.[142] Countries should be treated in the same manner both

[139] *US - Gasoline, pp. 23-24.*
[140] Elizalde Carranza, 83-84.
[141] Donoghue, 237, suggests that for this exact reason non-party provisions as in the Montreal Protocol are less likely to fall foul of WTO law than the non-party provisions contained in the Basle Convention.
[142] Baker, 466, develops this argument based on the distinction between the regime under the Montreal Protocol on Ozone depleting substances and the Basle Convention on the Control of Transboundary Movements of Hazardous Wastes and their Disposal.

in a situation where they are unwilling to adhere to a MEA or where they adhere but do not comply with the MEA's provisions. It is argued that in practical terms the consequences – non-respect of the MEA's disciplines – are the same. However, as discussed before, the main consideration should be that a regulatory programme which pursues the same aim with an effort which can be qualified as equivalent exists in the targeted country. This equivalent efforts should be taken into account in the application of the scheme of persuasive measures. Therefore, non-participation might be treated similarly to non-compliance, but does not necessarily have to. Non-compliance might trigger different other measures before the extra-tariffs are imposed. Non-participation on the other hand might not entail any sanction at all if the condition of an equivalent regulatory programme is fulfilled by the targeted country.

To conclude, the requirements of the chapeau have received heightened attention in the case law of the WTO judicial bodies. Article XX has admitted more policy space for unilateralism of WTO members, but has restricted the use of these exceptions by a close scrutiny of the application of members' policies. Extra-tariffs under a MEA against non-parties have to be carefully designed in order not to cause discrimination where no distinguishing conditions prevail between countries which would justify the different treatment.

4.2.4.6. Conclusions

As a brief conclusion, trade measures taken by a MEA party against a non-party have to be justified under Article XX to be compatible with WTO law. The provision has received several interpretations in recent years, but still many issues remain unresolved. Against this background, a panel still has quite a lot of leeway. It has been suggested here that by basing its determinations as far as possible on the MEA and its provisions a panel could find it easier to accept extra-tariffs to persuade a non-party to a MEA to adhere. However, there can be no guarantee that a panel would proceed in this manner. To meet the requirements of Article XX, a regime of extra-tariffs would face two main challenges: First, it has to be established that there are no less trade restrictive alternatives which could achieve the same contribution towards the objective. Financial assistance could be perceived as such an alternative in particular in the case of developing countries. Second, the regime for imposing such tariffs has to be carefully designed to take into account existing efforts in another country to tackle climate change beyond the MEA at question and to account for differences between trading partners in order to avoid all forms of discrimination in the application of the tariffs.

4.3. The state of the debate on carbon border adjustments

4.3.1. The stand of the debate on carbon border adjustments

As has been shown in the fact statement, the debate on how to tackle climate change in a mixture of multilateral and domestic efforts has moved during the last years from the details of emission trading schemes to the domestic market place. The focus lies in particular on implications the competitiveness of domestic industries which arise if

other major economies do not participate in the efforts to fight climate change. It appears, thus, useful to give an overview of the current debate on carbon border adjustments. Such adjustment measures aim at levelling the playing field by imposing charges or requirements on importers and foreign producers which do not carry a comparable burden to their domestic counterparts. As discussed, different proposals are in the pipeline, such as carbon taxes planned in France or the requirement to buy allowances under the domestic emissions trading scheme built in the United States' legislative proposal known as the Waxman-Markey Bill.

The following section provides an overview of the different positions that scholars have taken on the question of the compatibility of such measures with WTO law. Many different views have been expressed, but some common threads (and threats) can be identified.

As a first step, the United Nations Environmental Program and the WTO have produced a common report on the linkages between climate change and trade.[143] It provides a wide overview of the different initiatives to tackle climate change which have been taken on a national level or based upon the multilateral efforts under the UNFCCC and the Kyoto Protocol. In general, depending on the objective pursued, carbon taxes or an emission trading scheme are seen as the more efficient means. If growing emissions have to be capped, emission trading is more suitable, while taxes increase the incentive to switch to "cleaner", less CO2 emitting production processes, whereas no overall limit on emissions is introduced.[144] As far as border measures linked to domestic carbon tax or emission trading schemes are concerned, the report identifies two main challenges for such measures in view of WTO law: to indicate a "clear rationale" for the implementation of such measures depending on carbon leakage problems and competitiveness losses and to determine a "fair price" to be imposed upon the imported products to bring them to the same level as domestic products which have been produced under the influence of domestic climate change policies.[145] These general challenges have to be assessed under the different concrete disciplines which the WTO covered agreements impose. The following section addresses them separately.

4.3.2. Potential problems under WTO law

As a preliminary point, it should be mentioned that some early ideas described border adjustments in terms of avoiding environmental "dumping" or levelling the playing field distorted by means of subsidies in countries where no burden is imposed on producers because there are no comparable efforts to tackle climate change. While in the first case, the anti-dumping provisions of the WTO would be used, in the second countervailing measures against alleged subsidies would come into play. However,

[143] L. Tamiotti et al., *WTO-UNEP Report on Trade and Climate Change* (WTO Publication, 2009). For a comprehensive overview see L Tamiotti and V Kulacoglu, 'National Climate Change Mitigation Measures and Their Implications for the Multilateral Trading System: Key Findings of the WTO/UNEP Report on Trade and Climate Change' (2009) 43 Journal of World Trade 1115.
[144] For a useful overview of economic effects of taxes in comparison to emission trading schemes, see MK Crimp, 'Environmental Taxes: Can Border Tax Adjustments be Used to Counter any Market Disadvantage?' (2008) 12 New Zealand Journal of Environmental Law 39, 44.
[145] Tamiotti and Kulacoglu, 1129.

both scenarios are quite obviously in violation of WTO law. "Green" anti-dumping duties are impossible because the "normal" market price would have to be calculated in the country of origin of the products and not f. ex. the EU's or the United States' market.[146] Countervailing measures could only be imposed if there is a government's financial contribution. However, the non-imposition of a carbon tax is hardly specific enough as a contribution and does not give the right to impose such measures.[147] Carbon border adjustments are therefore likely to take the form of a charge levied at the import of products which will fall under Article II GATT.

4.3.2.1. Tax adjustments under Article II GATT

Generally, border taxes as such are regulated in Article II:2(a) GATT, which allows WTO members to apply to imports charges equivalent to internal taxes. Energy or carbon taxes imposed therefore would in principle have to be assessed under these provisions. Should a border measure require participation of some sort in a domestic emission trading scheme, in most authors' views this would similarly qualify as a charge under Article III:2 and would have to respect the same disciplines.[148]

Under Article II:2, such adjustments have to respect the requirements of national treatment as enshrined in Article III:2 (see later discussion). Apart from this general point, it remains disputed how far inputs which are not physically incorporated in the final product can be targeted by such taxes or charges. Article II:2(a) allows charges imposed on products and on articles from which the product has been produced in whole or in part. The discussion evolves around whether the latter articles can encompass inputs such as fossil fuels or other energy sources and permit thereby taxation based for example on the energy source with which a product has been produced.[149]

Article II:2(a)[150] is seen by some as restricting the potential reach of measures under Article II:2 to taxes targeting inputs present in the final product, which excludes taxes on fuels used during the production process and would merely permit taxes on fuel itself.[151] Others have however argued that Article II:2(a) requires the respect of

[146] J Pauwelyn, 'U.S. Federal Climate Policy and Competitiveness Concerns: The Limits and Options of International Trade Law' (2007) 07-02 Nicholas Institute for Environmental Policy Solutions, Duke University, Working Paper Series 1, 14.
[147] Ibid., , 13-16.
[148] J De Cendra, 'Can Emission Trading Schemes be Coupled with Border Tax Adjustments? An Analysis vis-à-vis WTO Law' (2006) 15 Review of European Community and International Environmental Law 131, 135-136; Pauwelyn, 'U.S. Federal Climate Policy and Competitiveness Concerns', 21.
[149] For one of the earliest contributions on the issue see C Pitschas, 'GATT/WTO Rules for Border Tax Adjustment and the Proposed European Directive Introducing a Tax on Carbon Dioxide Emissions and Energy' (1994-95) 24 Georgia Journal of International and Comparative Law 479, 493.
[150] Article II:2(a) GATT reads: "Nothing in this article shall prevent any contracting party from imposing at any time on the importation of any product: (a) a charge equivalent to an internal tax imposed consistently with the provisions of paragraph 2 of Article III in respect of the like domestic product or in respect of an article from which the imported product has been manufactured or produced in whole or in part [.]" (footnote omitted).
[151] De Cendra, 141, P Demaret and R Stewardson, 'Border Tax Adjustments under GATT and EC Law and General Implications for Environmental Taxes' (1994) 28 Journal of World Trade 5, 32.

Article III:2, which would permit to enlarge the scope of permissible taxes. [152] Article III:2 allows taxes applied "directly or indirectly" to products as far as there is no discrimination. Such indirect taxation could in their view also encompass taxes or charges imposed indirectly, i.e. on inputs used in the production process of a product without final physical incorporation. The *Superfund* case adjudicated by a panel under GATT 1947 is often cited as a reference in favour of the latter approach, although its language remains unfortunately too vague to allow the question to be considered settled.[153]

4.3.2.2. MFN

According to Article I GATT, every WTO member has to extend any privilege it gives to another WTO member to all members. Carbon border adjustments could cause concern in this respect in particular if they distinguish based on the origin of products rather than their characteristics.[154] This would clearly be the case if other countries were targeted by such measures because they are not parties to a MEA.[155] Other distinctions based on country-specific characteristics may also easily fall foul of the most favoured nation obligation, as for example the exemption foreseen in some United States' legislative proposals for least developed countries or *de minimis* emitting countries.[156] There may also be no unjustified distinction in the calculation methodology for border taxes between different countries. Probably, the most "advantageous" methodology would have to be extended to other countries.[157] The principle of "common, but differentiated responsibility" enshrined in international climate change law would partially or fully exempt developing countries from obligations f.ex. under the Kyoto Protocol. If a country would, however, as a consequence exempt developing countries from its border adjustments regime, it would thereby violate the most favoured nation obligation under WTO law.[158]

4.3.2.3. National Treatment

Based on Article III GATT, WTO members may not accord less favourable treatment to like imported products compared to domestic products. As a first problem, the establishment of "likeness" of products has proved one of the thorniest questions of

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[152] Pauwelyn, 'U.S. Federal Climate Policy and Competitiveness Concerns', 20. A similar result is reached by Ruddigkeit based on a teleological reading, see D Ruddigkeit, 'Border Tax Adjustment an der Schnittstelle von Welthandelsrecht und Klimaschutz vor dem Hintergrund des Europäischen Emissionszertifikatehandels' (2009) Beiträge zum Transnationalen Wirtschaftsrecht 5, 13-14.

[153] S Charnovitz, 'Trade and Climate: Potential Conflicts and Synergies' (2003) July Beyond Kyoto: Advancing the International Effort against Climate Change 1, 7; G Goh, 'The World Trade Organization, Kyoto and Energy Tax Adjustments at the Border' (2004) 38 Journal of World Trade 395, 412-413, who in addition cites a later WTO case (*Argentina - Measures Affecting the Export of Bovine Hides and the Import of Finished Leather* Report of the Panel, WT/DS155/R, 19 December 2000) as providing some further positive indications in this sense, Goh 406.

[154] Or, as Pauwelyn puts it, there is "discrimination between like products from different countries", Pauwelyn, 'U.S. Federal Climate Policy and Competitiveness Concerns', 32.

[155] F Sindico, 'The EU and Carbon Leakage: How to Reconcile Border Adjustments with the WTO?' (2008) European Energy and Environmental Law Review 328, 337.

[156] RV Brink, 'Competitiveness Border Adjustments in U.S. Climate Change Proposals Violate GATT: Suggestions to Utilize GATT's Environmental Exceptions' (2010) 21 Colorado Journal of International Environmental Law and Policy 85, 98.

[157] Ibid., 104-105, based on the findings of the Appellate Body in *US - Gasoline* .

[158] Ruddigkeit, 25.

WTO law. In the case law, four criteria have been constantly used, but do not constitute an absolute benchmark: The physical properties, end uses, consumers' tastes and tariff classification define a product for the WTO judiciary. In a landmark case, the Appellate Body has admitted that a different impact on human health can constitute a distinguishing characteristic of a product and therefore lead to two products being unlike.[159] However, it is unlikely that environmental properties would be perceived by a panel to play a similar role. In addition, distinctions based on PPMs have to date faced a rather negative stance by WTO panels and the Appellate Body.[160]

Moreover, the link between an emissions trading scheme and carbon border adjustments could raise additional problems. It is not fully clarified whether an emissions trading scheme should be perceived as a mainly tax-based regime or rather as regulation. Article III:2 on taxation leaves, however, less leeway to domestic regulators than Article III:4 does in cases of regulatory policy. Some argue that an emissions trading scheme should be seen as a tax in the light of OECD definitions.[161] As a problem, the payment for allowances is, however, unrequited because there is no proportionate benefit which is given in return. Some suggest as a consequence that the allowances could be seen as a kind of licence to engage in polluting activities or as a sanctioning mechanism to enforce environmental standards. However, even in this scenario the charges would probably not be considered as a regulation, but rather as an unrequited charge subject to the discipline of Article III:2.[162] In particular, it should be kept in mind that producers have the choice to change their way of producing to use less certificates or to "pay the higher fine" and buy more certificates, which discards the hypothesis of a sanctioning mechanism for environmental standards.[163]

[159] *EC - Asbestos, paras 113-114.*
[160] Sindico, 337. A different view is suggested by Charnovitz, 'The Law of Environmental "PPMs"' passim.
[161] According to definitions of taxes given by the OECD, see R Ismer and K Neuhoff, 'Border Tax Adjustment: A Feasible Way to Support Stringent Emission Trading' (2007) 24 European Journal of Law and Economics 137, 11.
[162] De Cendra, , 135-136.
[163] Ruddigkeit, 19.

4.3.2.1. *The exceptions under Article XX*

4.3.2.2.

Most scholars agree that carbon border adjustment can in principle be brought under the general exceptions of Article XX foreseen for non-trade measures aiming for example at the protection of the environment. Both Article XX(b) and Article XX(g) for the protection of public health and conservation policies are available. Similar to the discussion in the previous section, it is hard to foresee whether a panel would perceive policy to tackle climate change rather as aimed at the protection of the atmosphere as an exhaustible natural resource under Article XX(g)[164] or rather as aimed at preventing the negative effects a change in the global climate would have on the life and health of humans, animals and plants as provided for in Article XX(b).

Contrary to some views,[165] this may have important consequences as the legal tests of the rational relationship between a measure and its objective differ considerably between the two provisions.[166] Under Article XX(g),[167] a defending country would only have to show that border adjustment measures have a "close relationship of ends and means" with the underlying policy goal to tackle climate change, a test that has hardly shown much bite in the past case law.[168] In addition, however, Article XX(g) requires some even-handedness in the application in the form of similar restrictions on domestic production or consumption of the resource at issue. Some criticisms have been issued in this respect, as border adjustments do not necessarily act at the same level of production of products as for example an emissions trading scheme. However, the requirement of non-discrimination stated at this level should according to other scholars not be taken as strictly as the obligation f.ex. under Article III.[169]

Under Article XX(b), however, a measure must be "necessary" to protect public health, which comes down to a first close scrutiny of whether less trade restrictive alternatives are available. Second, it can also lead to the rejection of a measure by a panel or the Appellate Body if its trade restrictive effects are excessive in comparison to the benefits achieved.[170] However, the latter so-called "weighing and balancing" test could be influenced by the importance of the policy goal which is confirmed by the high amount of international cooperation on the subject.[171]

[164] Compare the Appellate Body's findings on air pollution in *US - Gasoline* .
[165] Sindico, 338.
[166] Some closer discussion on this topic can be found in section 4.2.4.4.
[167] Favoured for example by De Cendra, 144.
[168] See in particular the *US - Shrimp* case and its discussion in section 4.2.4.4. of this paper.
[169] Ruddigkeit, 27.
[170] *Korea - Beef, para 164.*
[171] Sindico, 338.

In the case of carbon border adjustment measures, a WTO member would have to prove therefore that these measures are linked to a domestic regime such as an emissions trading scheme or a carbon tax. As for the less trade restrictive alternative test, such an alternative would have to be brought forward by a complainant in a WTO dispute who would have to establish that such an alternative reaches the same beneficial effect.[172] It would have to offset in a similar manner the competitive disadvantages which the domestic industry suffers as a consequence of the local emissions trading or carbon taxation efforts. Such a competing proposal is hardly imaginable to overthrow a system of carbon adjustment present in a state, but could be successful in its challenge in case that the existing border adjustment regime is drafted in a way which overprotects domestic industries and thereby goes beyond what is necessary to offset the competitive disadvantages. The border adjustment regime would have to follow a rationale based on the environmental objective instead of focusing on alleviating harm done to the domestic economy or certain sectors.[173]

Should a carbon border adjustment withstand the scrutiny under the first tier of the analysis under Article XX, it still has to fulfill the requirements of the chapeau. This introductory clause prohibits all forms of unjustifiable or arbitrary discrimination between countries where the same conditions prevail. If negotiations have taken or are taking place, the process would have to be open to all participants to meet these conditions. No arbitrary exclusion of other countries may occur.[174] In addition, it is crucial that a country implementing border adjustments opens both procedural and substantial alleys for other countries to prove that their goods may be imported free of any border adjustment charges. In administrative terms, countries would, thus, have to be given the opportunity to show that their products do already carry some burden in the form of participation of domestic industries in climate change policies. Recognition of these efforts would have to lead to exemption from charges, in cases of non-recognition due process requires a possibility of appeal and transparent procedures.[175]

4.3.2.3. *Carbon border adjustments on exports under the SCM Agreement*

While border tax adjustments on *imports* can cause the discussed problems under GATT, the Agreement on Subsidies and Countervailing Measures could limit the possibility of adjustments on *exports*. In cases of indirect *taxes on consumption*, tax rebates for exports may only be used to set off the tax burden which like products sold for domestic consumption carry under the relevant indirect tax.[176] Should a rebate go beyond this level, it would constitute a subsidy.

Matters are more complicated concerning *taxes on production* because the rules are silent on the very issue. For the case of inputs physically incorporated in the product,

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[172] Ruddigkeit, 29, argues that there are virtually no alternatives to the suggested market-based approaches to tackle climate change such as border adjustments linked to emissions trading or carbon taxes.

[173] Brink, 110.

[174] See on this in more detail section 4.2.4.2. Some scholars, however, would allow border adjustments only as a last resort if cooperative efforts have failed, see Sindico, 339 or similarly Brink, 114. This appears to far-reaching in the light of the more carefully worded case law such as *US - Shrimp (Recourse to Article 21.5 DSU)* and *US - Gambling* .

[175] See in more detail the discussion in section 4.2.4.5. and the *US - Shrimp* case.

[176] Article 3.1. SCM and Annex 1(g).

non-excessive exemptions from input taxes borne by the domestic product are probably in accordance with WTO rules.[177] The SCM rules only cover inputs used or consumed in the production process of goods in cumulative tax systems, whereas such tax systems hardly exist anymore.[178] Carbon and energy taxes certainly do not fall into this latter category as they are only levied at one precise moment. No other rules on such *taxes occultes* are available.[179] Therefore, the SCM Agreement has to be considered as silent on the issue of climate taxes on inputs such as fossil fuels energy which are not incorporated in the final product. Some read this silence as allowing some scope for tax rebates, "though not excessively".[180] Others go even further and state that several rules of the SCM Agreement provide room for rebates for inputs not physically incorporated. As one textual basis, footnote 61 to Annex II enumerates as "inputs consumed in the production process" not only inputs physically incorporated, but also energy, fuels and oil used in the production process and catalysts. Under this view, tax rebates would be more broadly permissible under WTO rules. Requirements to buy allowances under an emission trading scheme as foreseen in United States' legislative proposals might be a different and more complex problem. Ismer and Neuhoff show that such a requirement cannot easily be equated with a tax or duty if free allowances are given out at the same time to some economic actors. A complicated mechanism in order to share the costs in a just manner would have to be established.[181]

4.3.3. Conclusions

The short overview of the state of the debate on carbon border adjustments has shown several problematic issues and uncertainties surrounding such measures. Carbon border adjustments would impose a charge on imports from countries which neither participate in any emission trading scheme nor have their own policy such as carbon taxation to level the playing field and avoid carbon leakage. As a crucial issue, it is not clear how far border taxes under WTO law may be imposed on inputs such as "dirty" energy or fuels which are not physically incorporated in the final product. In addition, such taxes cause concern under the most favoured nation provision if they treat trading partners in discriminatory fashion. According to the classification of domestic climate policy efforts as taxation or regulation (f.ex. emission trading scheme), regulatory or tax discrimination might arise under Article III. A panel would be asked here to determine the likeness of products produced under different circumstances, but similar in their characteristics. Lastly, the exceptions under Article XX might justify such discrimination, but only if requirements of using the least trade restrictive measure and strict non-discrimination in the application of the adjustment measures are fulfilled.

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[177] M Lodefalk and M Storey, 'Climate Measures and WTO Rules on Subsidies' (2005) 39 Journal of World Trade 23, 37.
[178] Article 3.1 SCM and Annex 1(h).
[179] This notion has been used by a GATT Working Party which examined the matter of border adjustments in earlier days, see GATT Working Party Report on *Border Tax Adjustments*, BISD 18S/97, adopted 2 December 1970, para 15. Unfortunately, the party only noted the disagreement between parties on the issue of adjustments for taxes on inputs not physically present in the final product and left the question open, as it found it irrelevant in practice.
[180] Lodefalk and Storey, , 38.
[181] Ismer and Neuhoff, 144.

If exports are targeted by border adjustments, consumption tax rebates work according to the same disciplines as other indirect taxation. However, for production taxes the relevant SCM Agreement does not contain clear provisions on product inputs which are not incorporated in the final product. Despite some more positive views in the doctrine, a challenge before WTO dispute settlement of such tax rebates could be successful.

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