To: UNCTAD Biotrade Initiative

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8-14, Avenue de la Paix

1211 Geneva 10

Switzerland

National Incentive Measures to Protect Biodiversity and Compliance with the WTO Agreements[1]

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From: Davide Soto Wei Zhuang Somda Y Dieudonne Babette Ancery

[1] This memorandum is a research paper prepared on a *pro bono* basis by students at the Graduate Institute of International and Development Studies (IHEID) in Geneva. It is a pedagogical exercise to train students in the practice of international trade law, not professional legal advice. As a result, this memorandum cannot in any way bind, or lead to any form of liability or responsibility for, its authors, the supervisors of the IHEID trade law clinic or the Graduate Institute.

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Case Study Concerning the Brazilian and Swiss Positive Incentive Measures

to protect biodiversity and the relationship with WTO law

I. Executive Summary

1. This memorandum offers a case study identifying two concrete cases in which Brazil and Switzerland have designed and implemented positive incentive measures to promote the trade of biodiversity related products and services in line with the objectives of the Convention on Biological Diversity (CBD).
2. This memorandum will analyze the tax incentive measure enacted by the State of the Amazonas in Brazil, and the Swiss taxation Regulation on the sustainability of biofuels. These measures will be analyzed on their WTO compliance to offer a better insight into the obligations under WTO law and the interplay between the two different Agreements.
3. The positive incentive measures whose adoption is stimulated by the CBD could potentially lead to WTO inconsistencies. This memorandum will focus upon the question whether the Swiss and Brazilian measures create inconsistencies with WTO law, and if so to what extent the CBD can be invoked to avoid any violations.
4. The CBD could be taken into consideration by a Panel in the application of the WTO law, as the US-Shrimp case demonstrated, as an element of context for the interpretation of the meaning of the provisions of the WTO, and therefore include the conservation of the biological diversity into the general exception of GATT Article XX. Since the report of the Panel of the EC - Biotech case, has neither been uphold by the AB (yet) nor is incontestably acceptable, it can be argued that a direct inclusion of the biodiversity protection and conservation into the scope of the Article XX GATT exception is still possible.
5. Most positive incentive measures will be based on (non products related) product and process methods. Where in the past, these did not seem to be enough reason to allow for distinctions to be made between products, the recent *EC – Asbestos* case law seemed to indicate that, if

PPMs affect the competitive relationship between two products, a specific PPM will become relevant in the likeness determination. They can be analyzed under consumer preferences or otherwise they could be reflected in market. This would allow for distinctions to be made between for example fuels, based on their production process and the environmental impact thereof. Furthermore, the differential treatment of like products may not necessary result in less favorable treatment.[2] In the recent EC- *Biotech* case for instance, the Panel did not found that there was less favorable treatment, because the difference of treatment was based on another factor, namely human health protection and not the origin of the products.[3] This reasoning might also apply to measures based on environmental protection, pursuant to the CBD Agreement. Thus, the CBD might play a role in the analysis of a WTO dispute under the exceptions of GATT Article XX or might influence the analysis under GATT Article III with regard to market perception (consumer preferences) or less favorable treatment.

6. The Swiss measure most likely complies with the TBT Agreement, the SCM Agreement and the GATT Agreement. It is only in very specific circumstances that a violation might be found, depending on the application of the measure. The Brazilian measure might constitute a violation of the SCM Agreement. However, this, as well as any potential violation of the GATT, might be justifiable under GATT Article XX(b) and (g). It is in any case very important to respect all the provisions regarding cooperation with other WTO Members.
7. This memorandum will first give a brief overview of the CBD and its relationship with the WTO, followed by a number of cross-cutting issues that are of relevance to all positive incentive measures. The second part of the memorandum will offer an outline and overview of the obligations under the TBT Agreement, the SCM Agreement and the GATT Agreement (GATT). After each Agreement, both the Brazilian and the Swiss measure will be analyzed on compliance. Finally, the exceptions contained in Article XX GATT will be examined**.**

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[2] Appellate body Report, *EC – Measures Affecting Asbestos and Asbestos-Containing Product*, WT/DS135/AB/R, 5 April 2001,para. 100.

[3] Panel Report, *EC- Biotech*, para. 7.2509-7.2516.

II. Factual and Legal Background

8. The Convention on Biological Diversity (CBD) is an international Agreement aimed at ensuring the conservation and sustainable use of biological diversity. It was signed at the end of the Earth Summit in Rio de Janeiro and entered into force in 1993. To date it has been ratified by 191 Countries.

9. The main objectives of the Convention are listed in Article 1: 'the conservation of biological diversity; the sustainable use of its components and the fair and equitable sharing of the benefits arising from the utilization of generic resources'. To ensure that these objectives are attained, the Contracting Parties committed to adopt a range of measures listed in Article 6 to Article 23. Due to the multi-faceted nature of the biodiversity problem, States are in a better position than international bodies when it comes to adopting concrete measures to protect the biodiversity. Therefore, implementation under the CBD is often a matter of the domestic legislation and these measures, rather than being binding obligations, are structured as targets that States are supposed to achieve while also taking into consideration their capacities and the international and domestic context.[4]

10. One of the most important instruments that the CBD uses for the attainment of its goals is the use of positive incentives: Article 11 of the CBD States that "each contracting party shall, as far as possible and as appropriate, adopt economically and socially sound measures that act as incentives for the conservation and sustainable use of components of biological diversity".

11. The sixth Conference of the parties (COP) in its decision VI/15[5] not only recognized the importance of the incentives measures in the process of implementation of the Convention, but also provided in its annexes a policy guidance on the design and implementation of the incentive measures and very detailed guidelines for selecting appropriate measures.

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[4] P. G. Le Preste, 'Studying the Effectiveness of the CBD, in Governing Global Biodiversity' (P. G. Le Preste, ed.),in *Global Environmental Governance*, 2002, p. 65.

[5] The Conference of the Parties is the governing body of the Convention (Art. 23): it surveys and advances implementation of the Convention adopting decisions in its periodical meetings.

12. In many instances, the COP required the implementation of the incentive measures to be consistent with parties' international obligations[6]. In fact, economic incentive measures might result in incompatibility with the obligations of Members under the WTO framework. This implies an evaluation of the relationship between the two multilateral Agreements, the CBD and the WTO, and in particular under what conditions non-WTO law can be invocated to derogate from WTO obligations and to justify a potential breach of WTO rules**.**
13. Now that the main factual background has been set out, we will first elaborate shortly on the positive incentive measures adopted by Brazil and Switzerland.

A. The Brazilian incentive measure

14. The State of Amazonas in Brazil has enacted a Tax incentives law[7]. The aim of the measure is "The development of the State of Amazonas through the integration, expansion, modernization and consolidation of the following sectors: industrial, agro-industrial, trading, services, forestry and alike" (Article 1). The incentives to industrial and agro-industrial enterprises are granted "[…] only for those products resulting from activities considered of fundamental interest for the development of the State of Amazonas […]" (Article 4).

    Article 4 States also that "[i]n order to be defined as fundamental for the State, enterprises should be involved in activities that meet at least three of the following conditions:

    i) contributing to the increase of the production chain to integrate and consolidate the industrial sector, the agro-industrial sector and the forestry industry of the State;

    ii) contributing to the increase in the industrial, agro-industrial and forestall production volume of the State;

    iii) contributing to the increase in exportations to the national and international market;

    iv) promoting research investment and the social and technological development of the State;

[6] See COP Decision VI/15 and COP Decision IX/6, par. 15.

[7] Law n. 2826 of 29/09/2003.

v) promoting the substitution of national and international importation of products;

vi) promoting the internal economic and social development of the State;

vii) **contributing to a rational and sustainable use of the raw materials from the forest and biodiversity of the Amazon**;

viii) contributing to the increase in the farming, fishing and forest production of the State;

ix) managing direct and/or indirect employment within the State;

x) promoting activities linked to the tourism industry".

15. The list quoted above is a closed list of conditions for the grant of the incentive: if an enterprise meets at least three of the conditions, it may be considered an enterprise involved in activities deemed relevant for the State and able to receive the benefit. It should be highlighted that the relevant condition concerning the conservation of biological diversity is number vii), contribution to a rational and sustainable use of the raw materials from the forest and biodiversity of the Amazon.

16. The enterprises willing to benefit from the incentives should submit a request to the Government of the State of Amazonas. The request should be supported by a technical and economic project. Some activities are excluded from the incentive, among others the production of alcoholic beverages, except those using inputs from the State and located in areas of the State that are considered as a priority.

17. The tax incentive is a credit of the Value-added Tax on Sales and Services[8]: the amount of the tax credit depends on the kind of product. The agro-industrial, forest, animal products, as well as pharmaceutical, cosmetics and similar products produced with local raw materials will be granted a 100% tax credit. The other products, which give right to a different tax percentage depending on the very product if manufactured within the State, will be granted a 20% extra tax credit.

[8] The tax is called ICMS - Imposto sobre Operações relativas à Circulação de Mercadorias e Prestação de Serviços de Transporte Interestadual e Intermunicipal e de Comunicação.

B. The Swiss measure regarding the ecological assessment of fuels

18. On 23 March 2007 Switzerland modified the Regulation 641.611 concerning the taxation of mineral fuels. Article 1 of this Regulation defines mineral fuels as 'heating fuels, average or heavy, generally commercialized in the world and complying with the definitions of the Swiss norm at the time of the taking effect of the present edict'.[9]

19. Chapter 2, Section 1 specifies the applicable taxes, a tariff tax for mineral fuels as well as a surcharge for mineral fuels (Article 18 and 19). The tax is to be paid by respectively the producer or the importer. Article 19a provides for a tax relief for fuels made from renewable resources. The following fuels are considered renewable fuels, bio ethanol, biodiesel, biogas, bio methanol, bio-ether, synthetic biofuels, bio hydrogen, vegetable or animal fuels or used vegetable or animal fuels.[10]

20. Article 19 b provides that the minimum requirements concerning a positive global ecological effect are fulfilled if (a) 'the fuels made from renewable raw resources emit, from their production until their use, concerning their biogenic part, at least 40% less carbon emissions than fossil fuels', (b) 'if the fuels made from renewable resources, from their production until their use, do not cause prejudice to the environment in a way that is notably higher than with fossil fuels', (c) ' if the production of the renewable resources of which the fuels are made in conformity with the latest technology do not constitute a danger to the conservation of tropical rainforests, nor to the biological diversity'.

21. These conditions are in all cases considered to be fulfilled for 'fuels produced in conformity with the latest techniques and which are made from waste or from biogenic residue stemming from the production or transformation of agricultural or forestry products.'[11] Producers of these fuels are not required to submit any evidence. 'It is considered that the fuels made from palm oil, soja or cereals do not meet the minimum requirements mentioned in Article 19b

[9] Article 1 RS 641.611, l'ordonnance sur l'imposition des huiles minerales.

[10] All the fuels are set out in Article 19a (1) (2) (a – h) and are defined more specifically in this Article. Article 19a (3) defines when biogas is considered to be a fuel.

[11] Article 19b (2) of the RS 641.611.

(1).[12] However, if the producer or importer believes that its fuel made from one of these materials does satisfy the requirements, they will be examined nonetheless. For all other fuels, the proof that the fuels meets the criteria has to be delivered by the imported for imported fuels, and by the producer for domestically produced fuels.

22. Furthermore, Article 19d specifies minimum requirements with regard to socially acceptable production conditions. The Article provides that 'the minimum requirements relative to socially acceptable production conditions are fulfilled if, during the culture of the raw resources and the production of the fuel, the social legislation applicable to the place of production, or at least the fundamental conventions of the ILO have been respected.'
23. To proof that a fuel fulfills the criteria to benefit from the tax reduction, the producer has to 'describe the whole production process of the fuels, from the culture of the raw resources to the receipt of the fuel by consumer', 'proof that the culture of the raw materials does not endanger the tropical rainforest (or other ecosystems functioning as CO2 reservoirs), nor the biological diversity', 'underline eventual ecological advantages'.[13] Thus, the examination of the fuel will be based on a life cycle approach of the fuel.
24. Thus, the new Regulation allows for tax reductions if fuels are made from renewable resources. The fuels made from renewable resources only receive this lower tax if they have a positive effect on the global ecology and if they have been produced in socially acceptable circumstances.
25. Before continuing with the examination of the compliance of these measures with WTO law, the relationship between the WTO and the CBD will be addressed.

[12] Article 19b (3) of the RS 641.611.

[13] Article 2 OEcobiC, Edict on the ecologic footprint of fuels, RS 641.611 Articles 3 to 6 provide specifications on how the nature of the fuel should be described as well as the culture of raw resources, the production of the fuel and whether the fuel endangers the tropical rainforests or the biological diversity.

C. The relationship between the WTO and the CBD

26. The CBD is a multilateral treaty outside the WTO. It is still controversial whether such an international treaty can be a source of WTO law. This question requires an analysis of the provisions that establish the applicable law of the adjudicative bodies of the WTO. In other words, it should be determined whether and to what extent WTO Panels can apply non-WTO law. In this regard Article 3.2 of the DSU clearly States that: 'The dispute settlement system of the WTO is a central element in providing security and predictability to the multilateral trading system. The Members recognize that it is an instrument 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. Recommendations and rulings of the DSB cannot add or diminish the rights and obligations provided in the covered Agreements.'
27. These customary rules are reflected in the Vienna Convention on the Law of Treaties (VCLT) and in particular in Article 31 (3), which States that in order to interpret a treaty not only shall the treaty itself be taken into consideration, but also any subsequent Agreement between the parties regarding the interpretation of the treaty or the application of its provisions, as well as any relevant rules of international law applicable in the relations between the parties.
28. This provision gives the impression that it might be possible to refer to outside treaties in the interpretation of WTO obligations. However, in the most recent case on *EC-Biotech* products,[14] the Panel was confronted with the question of the nature of the relationship between the CBD and WTO law. In particular, it had to interpret the meaning of "parties" in Article 31 (3) (c) of the VCLT.
29. The Panel considered that in order to interpret WTO law in the light of other Agreements, the main condition is that all the parties of the WTO Agreement are also parties of the other Agreement.[15] Thus, according to this Panel, it is only possible to invoke another treaty if all

[14] Panel Report, *EC-Measures Affecting the Approval and Marketing of Biotech Products* ,WT/DS291/292/293/R, 29 September 2006.

[15] Panel Report, *EC-Biotech,* para. 7.70.

WTO Members are also party to that treaty. This makes it very difficult and almost impossible to invoke an outside treaty, since it is rare that all Members are party to the same Agreement, for example Taiwan or the EC, which are WTO Members, will not be able to adhere to all treaties. However, it must be underlined that this is a Panel report and that the Appellate Body has not given a ruling on this case yet. If an Appellate Body were to agree, the CBD could not be invoked to justify non-compliance with WTO law, unless all Members are party to the CBD.

30. The conclusion reached by the Panel in the *EC-Biotech* case concerning the applicability of non-WTO law is quite controversial: in fact, the limits designed by the Panel for the applicability of non-WTO law would transform the multilateral framework of the WTO into a nearly closed circuit, thereby jeopardizing the unity of international law. Yet, the DSU itself frames the WTO into the system of public international law, as can be derived from Article 3.2 of the DSU.[16] However, since the Panel limits the actual possibility of the application of Article 31 (3) (c) of the VCLT, it makes the possibility to interpret WTO law in the light of the non-WTO law dependent upon the fulfillment of a considerably restrained condition.
31. The Panel could have interpreted the meaning of "parties" in Article 31 (3) (c) of the VCLT differently: not all the parties of the WTO, but rather all the parties to the dispute before the Panel should be parties of the other multilateral Agreement. This alternative interpretation has a clear advantage: it would allow an easier application of Article 31 (3) (c) of the VCLT. However, this alternative has a drawback, which is that the WTO would be interpreted differently by each party in a dispute.[17] In fact, the application of Article 31 (3) (c) of the VCLT would not be objective, for each WTO Member, in settling each dispute; it would

[16] The Appellate Body in the case *US-Gasoline* clearly explained that the reference of art. 3.2 to customary rules of interpretation of public international law reflects "a measure of recognition that the General Agreement is not to be read in clinical isolation from public international law".

[17] In one dispute between two parties, the CBD might be invoked, while in a dispute between two other parties of which one is not a CBD Member, the CBD cannot be invoked. This might, in similar cases, lead to different outcomes and thus might lead to different relationships between different countries.

rather follow subjective criteria and eventually the very WTO law would be interpreted differently by the Members.

32. The findings of the Panel in the case *EC-Biotech*, in addition being controversial, will have to pass the analysis of the Appellate Body that could not uphold the core of the reasoning on the interpretation of Article 31 (3) (c) of the VCLT. In the present conditions, if the report of the Panel were approved by the Dispute Settlement Body, the possibility to interpret WTO law in the light of the CBD would be excluded except for what Stated by the Appellate Body in the *US-Shrimp* case. In that case the AB stated that the CBD can be taken into consideration, like other multilateral Agreements outside the WTO, for the interpretation of WTO law in its ordinary meaning (see below).
33. Having checked the State of the art of the interpretation of WTO law in the light of non-WTO law and the recent case law from the Panel in the *Biotech* case, we now turn to the question whether it is possible to directly apply non-WTO law for the solution of the controversies before the adjudicative bodies of the WTO. In this different case the CDB would not be a reference for interpreting WTO-law, but it would be applicable law itself. This raises the question, under what conditions the CBD could be directly applicable before a Panel.
34. The condition to be met would be that all the parties of the dispute are part of both the WTO and the CBD: in fact, assuming that one of the parties would not be a part of the CBD, the Panel, by applying the CBD would impose the application of rules that were not agreed to by the party on that party.[18] In addition, in case of real conflict between the WTO-law and the CBD, conflict rules of international law may apply: the rules of *lex posterior derogat priori* and *lex specialis derogat legi generali*.
35. The *lex posterior* rule, if applied to solve a potential conflict between the CBD and the WTO, would have as a result the prevalence of the WTO over the CBD, given that all the covered Agreements (including the Marrakesh treaty and the 1994 General Agreement on Tariffs and

[18] This solution would violate the principle of *pacta tertiis nec nocent nec prosunt* that is included in the VCLT, art. 34: "A treaty does not create either obligations or rights for a third State without its consent".

Trade) were signed *after* the CBD. In this case, therefore, the conflict would be solved in favor of WTO law, with the exclusion of any application of the CBD. However, instead the CBD could be applied by a Panel as a special discipline in the framework of WTO law. In this case the CBD could be applied directly as a special rule that justifies the breach of WTO law.

D Cross cutting issues

36. Before turning to the specific measures, a few controversial and/or important issues relating to the WTO will be underlined and clarified. First, the issue of product related production and process methods (PPMs), followed by the need for flexibility and transparency.

1. Product and Process Methods

37. One of the great questions of the articulation between trade and environment, and more specifically of the relationship between the CBD and the WTO Agreements, is the Product and Processing Methods (PPM) issue. PPM refers to "The focus of government measures that impose taxes or regulatory burdens on goods based on their production or processing methods"[19]. In the WTO, there is a distinction between product related PPMs which by definition modify the physical characteristics of the final product and non products related PPMs (npr- PPMs) which do not have any incidence on the characteristics of the final product. It seems that many governmental measures aimed at enforcing CBD will be based on npr-PPMs, for example the Swiss measure. The question is whether the WTO Agreements cover or allow the use of a npr-PPM based measure.

38. The traditional GATT case law did not seem to accept a PPM as a basis for regulatory distinctions.[20] In the *Tuna* case, the un-adopted GATT 1947 panel report shared this point of view. The Panel found that GATT Article III does not apply to npr-PPMs, which are *per se* violations of Article XI GATT. The panel found that they are illegal quantitative restrictions

[19] R. E. Hudec, 'The Product-Process Doctrine in GATT/WTO Jurisprudence', in *New Directions in International Economic Law, Essays in Honour of John H. Jackson* (M. Bronkers and R. Quick, éd.), Kluwer Law International, 2000, p. 187.

[20] GATT Panel Report, *US – Measures Affecting Alcoholic and Malt Beverages*, BISD 39/S/206, 19 June 1992.

under Article XI. Moreover, in the *Shrimp* case, the US prohibition was based on a npr-PPM and was found to be a violation of Article XI of GATT. However, it seems that non mandatory measures not affecting directly the importation of products cannot violate Article XI of GATT. However, it should be taken into account that *de facto* restrictions are also covered by Article XI:1 GATT. Thus, if a non mandatory measure of a WTO Member has the effect of restricting the import or export of certain products, for instance when there is a high governmental incitation, it can nevertheless fall under the scope of Article XI:1.[21]

39. However, the recent *EC – Asbestos* case law seemed to indicate that, if PPMs affect the competitive relationship between two products, a specific PPM will become relevant in the likeness determination. They could come in under consumer preferences or otherwise they could be reflected in market studies if consumers really care and make a distinction between the products. Most often market determination will lead to the conclusion that PPMs and non PPMs measures are competitive and thus like products. However, the different treatment of like products may not necessary result in less favorable treatment.[22] In the recent EC- *Biotech* case for instance, the Panel did not found that there was less favorable treatment, because the difference of treatment was based on another factor, namely human health protection and not the origin of the products.[23] The panel concluded that it "is not self evidence that the alleged less favorable treatment of imported biotech products is explained by the foreign origin rather than, for instance, a perceived difference between biotech and non biotech products in term of their safety…" The same conclusion was found by the Appellate Body in *Dominican Republic – Cigarette.*[24]

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[21] Panel report, *Argentina – Measures Affecting the Export of Bovine Hides and Import of finish Leather*, WT/DS155/R and corr.1,16 February 2001, para. 11.17.

[22] Appellate body Report, *EC – Measures Affecting Asbestos and Asbestos-Containing Product*, WT/DS135/AB/R, 5 April 2001,para. 100.

[23] Panel Report, *EC- Biotech*, para. 7.2509-7.2516.

[24] Appellate Body Report, *Dominican Republic – Measures Affecting the Importation and Sale of Cigarettes*, para. 96.

40. It seems that npr – PPMs do not necessarily constitute less favorable treatment. By analogy, we can say that, npr-PPM because there are based on factors not related to the origin of the products, such as measures aimed at the protection of biodiversity or the environment, might be considered as not leading to less favorable treatment, hence discriminatory, in the framework of GATT 1994 Article III. The aim of implementing the CBD by means of a npr-PPM could be a relevant factor to take into account when assessing the compliance with Article III:4 GATT, as indicated by the new *Asbestos* and *Biotech* case law. Whether Articles III and XI GATT can both be applicable to a specific npr-PPM is not clear from the case law. To date it seems to suggest that this possibility is not available. Article III and Article XI GATT are mutually exclusive. The application of one depends on the qualification of the npr-PPM as affecting directly the importation or the treatment within the market. It would be not easy to take the CBD directly into account, as it seems the case with Article III, when assessing the compliance of the npr-PPM with Article XI GATT. Such justification is still available under Article XX GATT. With the recent *Shrimp* case, where a npr-PPM was admitted by the Dispute Settlement Body under GATT Article XX, we know that in any event, even if they violate Article III or XI GATT, we know that they can be justified under XX GATT.
41. In sum, it seems that GATT does not prohibit PPMs as such. But in the classical GATT test, a PPM would generally not suffice to treat PPM and non PPM products as unlike. It is however conceivable that different treatment base on PPM consideration would not constitute less favorable and would thus not lead to a violation of national treatment obligation. In any case, PPM regulatory distinctions can be invoked in the context of the GATT exception provisions.
42. The PPM also plays an important and controversial role in the TBT Agreement. Developing countries are opposed to the view that the TBT Agreement could be interpreted in a manner that npr-PPM fall under its scope of application. However, it is clear today that all technical Regulations have to be notified. At the same time, all Members agree on the necessity of a minimum of transparency concerning npr PPMs. The TBT committee States that: « In

conformity with Article 2.9 of the Agreement, Members are obliged to notify all mandatory labelling requirements that are not substantially based on a relevant international standard and that may have a significant effect on the trade of other Members. That obligation is not dependent upon the kind of information provided on the label, whether it is in nature a technical specification or not ».[25] If Members must respect transparency obligations, why not the other provisions of the TBT. Even if TBT Agreement does not cover npr-PPM and consequently such PPM Regulations would be incompatible with WTO law, they will be examined under GATT Article III or XI and may be justified under Article XX.

2. Flexibility and transparency in application of npr-PPM measures

43. WTO Agreements allow Members to protect legitimate non trade objectives, such as biodiversity. Under Article XX GATT, WTO Members are allowed to take trade restrictive measures to enforce the objective of protecting biodiversity. The CBD is a multilateral Agreement, but its implementation requires unilateral measures from the States. However, such unilateral measures will be often considered arbitrary or unjustifiable discrimination or a disguised restriction to international trade if those measures are not applied in a flexible manner, and if they do not take into account the particular conditions of the other countries.

44. In the case *US- Shrimp II*, the US measure was GATT consistent because, even though it restricted trade, it allowed for such flexibility.[26] Cooperation with others States would be the best solution for Members to avoid inconsistency with Article XX GATT. Equivalence and negotiation of mutual recognition Agreements are good examples of cooperation tools. Both Article XX GATT and the TBT Agreement contain the requirement of flexibility of measures.[27]

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[25] Committee on TBT, 28 November 2000, G/TBT/1/Rev.7, section III:10.

[26] It concerned consistency with GATT Article XX, the exceptions.

[27] The TBT Agreement goes far in this by including some transparency provisions. Notification and publication of national measure are important because that permits the prevention of potential disputes before the measure is adopted.

45. The flexibility and transparency requirements make the WTO Agreement and the CBD complementary, since the CBD is a multilateral environmental Agreement which contains trade measures to further its objectives. In some circumstances, the WTO allows for unilateral actions – but only if several multilateral and good faith attempts have been undertaken, if Members take actions that contribute materially to the protection of biodiversity and if thereby flexibility is maintained. Thus, there is a relationship of "Mutual support" between the WTO Agreements and the CBD. They are not in conflict *per se* nor is there is any hierarchy between them since they are interdependent. States must keep this consideration in mind when adopting environmental protection measures that might violate GATT provisions, but that could be justified under GATT Article XX.
46. Both the Brazilian and the Swiss measure can be examined on WTO compliance under different WTO provisions. The Brazilian measure could fall under the scope of the SCM Agreement and the GATT Agreement.[28] The Swiss tax Regulation could fall under the scope of the TBT Agreement, the SCM Agreement and the GATT Agreement. Any potential violations of one of the measures might be justifiable under Article XX GATT. Since TBT and SCM are specialized and specific Agreements, they will be examined before turning to the GATT.[29]

III. Assessment of the positive incentive measures under the TBT Agreement

47. Technical requirements relating to the characteristics of a product or to their related process and production methods (PPM) can be used to protect the environment, life or health. The

[28] The Brazilian measure does not fall under the TBT Agreement, since it does not lay down any characteristics or guidelines and can thus not be considered a technical Regulation, standard or conformity assessment procedure. Moreover, in general pure taxation Regulations do not fall under the scope of the TBT Agreement.

[29] In EC Asbestos, the Appellate Body Stated that specialized and self standing Agreements always have to be examined before the GATT.
It must be noted that obligations contained in the WTO Agreement are generally cumulative and sometimes the same aspects of a Regulation can be subject to various provisions of the WTO Agreement. This was clarified by the Panel in Indonesia – Autos.

TBT Agreement provides for rules on technical regulation and establishes certain requirements that must be met for a measure to fall under the scope of TBT.

A. The scope of the TBT Agreement

48. To fall under the scope of the TBT Agreement, a Regulation must be considered as a technical regulation, a standard, or a conformity assessment procedure.[30] The case law interpreting the terms of Annex 1.1 of the TBT Agreement[31] specifies that a technical regulation is a document which a) 'lays down product characteristics or their related process and production methods, including the applicable administrative provisions', b) 'with which compliance is mandatory'. Furthermore, c) it must apply to an identifiable group of products.[32]

49. If compliance is not mandatory in the sense that, if the characteristics are not met, the product can still be sold in the market of the Member, the measure will not be considered a technical regulation. However, it could still fall under the scope of TBT if the measure is a standard.[33] Annex 1.2 of the TBT Agreement defines a standard as a "document approved by a recognized body, which provides, for common and repeated use, guidelines or characteristics for products or related processes and production methods, with which compliance is not mandatory. It may also include or deal exclusively with terminology, symbols, packaging,

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[30] Appellate Body Report, *EC – Asbestos*, para. 80.

[31] This provision defines technical Regulation as *"…[a] document which lays down product characteristics or their related processes and production methods, including the applicable administrative provisions, with which compliance is mandatory. It may also include or deal exclusively with terminology, symbols, packaging, marking or labelling requirements as they apply to a product, process or production method"*.

[32] Appellate Body Report, *EC – Trade Description of Sardines*, WT/DS231/AB/R, 23 October 2002, para 176; Appellate Body Report, *EC – Asbestos*, para. 67-75.

[33] Annex 1.2 of the TBT Agreement defines a standard as a "document approved by a recognized body, that provides, for common and repeated use, guidelines or characteristics for products or related processes and production methods, with which compliance is not mandatory. It may also include or deal exclusively with terminology, symbols, packaging, marking or labeling requirements as they apply to a product, process or production method"

marking or labeling requirements as they apply to a product, process or production method".[34] Thus, contrary to a technical Regulation, a standard is of a voluntary nature, meaning that compliance is not compulsory.[35]

50. Finally, the Agreement also applied to conformity assessment procedure, which is *"… any procedure used, directly or indirectly, to determine that relevant requirements in technical Regulations or standards are fulfilled"*.[36]

51. However, there is still uncertainty as to whether technical regulations, standards and conformity assessment procedures relating to npr-PPM or based on a life cycle approach of the product fall within the scope of application of the TBT Agreement. This arises from the definitions of technical regulation and standards. The first sentences refer to "***related*** *processes and production methods*" [emphasis added]. This seems to not include npr-PPM. However, the terms ***"related"*** is not used in the last sentences of the definitions. The terms of the definitions do not precise clearly whether the TBT Agreement is applicable to npr-PPM in general. The DSB has not yet ruled on this issue.

B. Substantives rules of the TBT Agreement

52. Article 2.1 TBT lays down a non discrimination obligation for technical Regulations, 'in respect of technical regulations, products imported from the territory of any Member shall be accorded treatment no less favorable than that accorded to like products of national origin and to like products originating in any other country**'.** This applies in a similar way to standards and conformity assessment procedures. [37] Thus, if the TBT Agreement applies, the measure may not be applied in a discriminatory manner.

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[34] Annex 1.2 to the TBT Agreement.

[35] Note that Standards are subjected to a specific discipline in the TBT Agreement. e.i. Article 4 and the Annex 3 Code of practice that contains provisions very similar to the TBT provisions relating technical Regulations. To date, the concept of standard has not been further clarified by case law.

[36] Annex 1.3 of the TBT Agreement.

[37] Respectively paragraph D of the Code in Annex 3, Article 5.1.1 TBT

53. If there are suspicions of a violation, the following analysis will be executed. First, the imported product will be compared to the domestic product/ other imported product to see if they are like. The determination of likeness of those two products is a prerequisite, since if there is no likeness, there can be no discrimination. The likeness of two products within the meaning of the TBT Agreement has not yet been determined by dispute settlement proceedings, but the case law relating to the Article III: 4 of the GATT is relevant for the interpretation of likeness in the context of TBT. Thus the examination of likeness will involve an analysis of a) the physical characteristics of the products, b) their ends uses, c) the consumer preferences and d) the tariff classification for both products. However, the definition of likeness might differ from the meaning in Article III: 4 of the GATT. If the products are found to be like, it will be necessary to examine whether the imported product receives less favorable treatment.
54. The TBT Agreement lays down a necessity requirement, technical regulations[38], standards[39] and conformity assessment procedures[40] must not be prepared, adopted, or applied with a view to or with the effect of creating unnecessary obstacles to trade. They shall not be more trade-restrictive than necessary to fulfill a legitimate objective, and have to be the least restrictive means to reach this objective. The protection of biodiversity and rainforests will most likely be considered a legitimate objective. The Appellate Body has recently confirmed that environment is an important value. [41] The test of necessity defined in the GATT Article XX b) and d) is likely to be relevant for the assessment of the necessity of a measure in the context of TBT Agreement.
55. In a recent case, *Brazil – Retreaded Tyres* the necessity test has been defined. The Appellate Body stated that it should involve a process of weighing and balancing, which makes the test

[38] Article 2.2 of TBT Agreement

[39] Paragraph E of the Code of practice.

[40] Article 5.1.2 of the TBT Agreement.

[41] Appellate Body Report, *Brazil – Measures Affecting Import of Retreated Tyres*, WT/DS332/AB/R, 3 Dcember 2007.

less strict. This case illustrates that a trade restrictive measure can still be considered necessary if *prima facie* it pursues a value of importance and if the contribution of the measure to the fulfillment of the objective is meaningful. Note that; if value is less important it can still pass the test, but with more difficulty. Concerning the second stage of the necessity test, *i.e*. the determination of whether there are alternatives measures, note also that any alternative must be less trade restrictive, it does not only have to be equally effective in the attainment of the legitimate objective, but it also has to be reasonably available, taking into account the importance of the aim, the effectiveness of the measure and its trade restrictiveness.[42]

56. Finally, the TBT Agreement contains provisions on the use of international standards, paragraph F of the Code[43], as well as Article 2.4 of the TBT Agreement relating to technical regulations, require that Members base their standards on a relevant international standard, unless the international standard would be inappropriate or ineffective due to specific circumstances, such as geographic or climatic conditions. It is for the complainant to prove that the international standard in question is both an effective and appropriate means to fulfill a legitimate objective.[44] If the national measure is in accordance with the international standard, there is a rebuttable presumption that it does not create an unnecessary barrier to international trade.[45]

57. TBT inconsistency and Article XX of GATT. Even if a violation were to be found, could the measure be justified under Article XX of the GATT? There is no certainty whether a TBT violation can be justified under Article XX. The Panel / Appellate Body has not yet had the chance to decide on this. However, in recent case law the Appellate body left the issue open

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[42] Appellate Body Report, *EC – Asbestos*, para. 174.

[43] « Where international standard exist or their completion is imminent, the standardization body shall use them, or the relevant part of them, as the basis for the standard it develops, excepted where such international standard or relevant part would be ineffective or inappropriate, for instance, because of an insufficient level of protection or fundamental climatic or geographical factors or fundamental technological problems".

[44] Appellate Body Report, *EC – Sardines*, para. 287.

[45] Article 2.5 of TBT Agreement.

and did not provide a final point of view on this issue. The Appellate Body seemed to admit the possibility of referring to GATT Article XX in order to justify a violation of the anti-dumping Agreement since it was an application of Article VI of the GATT. It assessed the measure in question, and concluded that the measure didn't pass the Article XX test and thus there was no need to rule on whether the Respondent has the right to invoke GATT Article XX to justify the Anti-dumping Agreement.[46] Therefore, in case of a violation of the TBT Agreement, a country could try to justify its measure under GATT Article XX. If the Panel or Appellate Body finds that this exception applies, the measure will be analyzed on its conformity with GATT Article XX. If compliance with Article XX is found, the measure violating the TBT Agreement could be justified under XX GATT. This seems however possible for a violation of Article 2.1, but it is less probable that a measure violating Article 2.2 of the TBT Agreement, can be in conformity with Article XX of GATT, in any case not under b) or d), since necessity test seems the same in these three provisions.

58. It must be noted that there is a direct relationship between anti-dumping Agreement and GATT Article VI, and also between the SCM Agreement and GATT Article XVI. The SCM Agreement and anti-dumping Agreement are *lex specialis* and prevail in case of conflict with

[46] Appellate body Report, *United States – Measures relating to shrimp from Thailand*; *United States – Custums bond directives for merchandises subject to anti-dumping/ countervailing duties*, WT/DS343/AB/R; WT/DS345/AB/R, 16 July 2008. "India's appeal raises systemic issues about the availability of a defence under Article XX(d) to justify a measure found to constitute "specific action against dumping" under Article 18.1 of the Anti-Dumping Agreement, and not to be in accordance with the Ad Note to Article VI:2 and 3 of the GATT 1994, as well as Article 18.1 of the Anti-Dumping Agreement. Assuming, argued, that such a defense is available to the United States, we proceed to consider the United States' appeal of the Panel's finding that the EBR, as applied to subject shrimp, is "necessary" to secure compliance with certain United States laws and Regulations within the meaning of Article XX(d). We examine the Panel's finding on this issue of "necessity" before we return to the question of availability of a defense under Article XX(d)" § 310; "We therefore uphold the Panel's findings, in paragraph 7.192 of the Panel Report in US - Shrimp (Thailand) and paragraph 7.313 of the Panel Report in US - Customs Bond Directive, that the EBR, as applied to subject shrimp, is not "necessary" to secure compliance with certain laws or Regulations within the meaning of Article XX(d) of the GATT 1994.", § 318; "In view of this conclusion that the EBR, as applied to subject shrimp, is not "necessary" within the meaning of Article XX(d), we do not express a view on the question of whether a defence under Article XX(d) of the GATT 1994 was available to the United States", §319.

GATT.[47] Note that on the contrary, there is no direct relationship between the TBT Agreement and the GATT. Hence, there is not really conflict between TBT and GATT. Again, because of the "single undertaking" character, the WTO Agreement must get effective application. To do so, it must be interpreted as a harmonious whole. All WTO obligations are generally cumulative and Members must comply with all of them simultaneously.[48] So when a measure is found to be TBT consistency, it will still be assessed under GATT provisions. If violation of one or several main GATT provisions is found, then it must be justified under Article XX GATT exceptions. If a measure is found to violate TBT objective obligations relating to harmonization, transparency or equivalence, it seems that it may not be justified under GATT Article XX, because GATT Article XX is applicable only when one of the main provisions is violated and these TBT Agreement provisions are clearly different from GATT ones. In sum, recall that there is not yet a definitive ruling on the issue.

C. Examination of the Swiss measure

59. The Swiss Regulation could fall under the scope of the TBT Agreement. It applies to an identifiable group of products, namely to fuels made from renewable resources. Furthermore, the Regulation lays out criteria that are taken into account and on the basis of which will be examined whether the biofuel can benefit from a lower tax. Even though the Regulation concerns a tax, the core of the Regulation is laying down criteria and standards for products, which if they fulfill these requirements can benefit from a lower tax. The tax credit is the result of compliance with the Regulation.

60. Since it is mandatory to comply with the Regulation in order to get a benefit, i.e. the tax exemption, one can think that the Swiss measure is a technical Regulation. However, compliance with the product characteristics is not mandatory, since if the producer does not meet the criteria, he will still be able to sell the product in the market. Compliance is the condition if producers want to receive the tax credit in the same way as it is a condition for a

[47] General Interpretative Note to Annex 1. A.

[48] Appellate Body Report, *Korea – Definitive safeguard measures on import of certain dairy products*, WT/DS98/AB/R, adopted 12[t] January 2000, para. 74.

producer to meet its criteria if that producer wants to receive a voluntary eco label. The tax exemption is similar to the competitive advantage that the voluntary label procures in the market place.[49] In sum, it seems to be a standard. It is however not certain whether a standard related to non product related PPMs or a life cycle approach falls under the scope of the TBT Agreement, as explained in the earlier section relating the npr-PPM issue.

61. The Regulation is based on npr PPMs and a life cycle analysis. The producer or importer needs to describe the production process of the fuel since the entire life cycle of the fuel will be taken into account. Furthermore, he needs to proof that the culture of the raw materials used in the production of the fuel will not endanger the rainforest or the biological diversity. The basis of the analysis of the fuel is a life cycle analysis (LCA) and hence a non –product-related production and process method (npr PPM). As discussed earlier, there is a doubt whether the TBT Agreement applies to measures based on non product related PPMs. If it does, the measure will be perceived as a standard and the TBT Agreement will apply.
62. Assuming the Agreement applies, the measure may not be applied in a discriminatory manner.[50] The Regulation applies to both domestic and imported biofuels, as Stated in Article 2 of the Regulation and is thus not *de jure* discriminatory. However, the TBT Agreement also covers *de facto* discrimination. Only in specific circumstances could the Regulation be found to be discriminatory.
63. First, in order to benefit from a lower tax, several criteria are taken into account. One of them is contained in Article 7 and a similar provision is found in Article 13. Article 7 States that the producer must provide evidence of the transportation methods of the fuel and of the distance it has covered. Article 13 States that an assessment will be made of the effects of carbon emissions and environmental achievements. On the contrary, the explanation of Article 6 mentions that carbon emissions created during the transport will not be taken into account. However, they might be taken into account through Article 7 and 13 and if done so, these

[49] Note that the benefit or advantage resulting of lower tax can be challenged only under Article III: 2 of GATT or under SCM Agreement.

[50] Paragraph D of the Code of practice and 5.1.1 of TBT.

Articles could potentially disadvantage foreign producers, since their fuels will in general have to cover a greater distance before reaching the consumer. They will most likely contribute to a higher amount of emissions. However, looking at transport emissions is not a *de jure* discrimination based on origin, since it is based on an objective, origin-neutral criterion. Perhaps it is so *de facto* but proof of discriminatory effect is not enough, because the competitive disadvantage is caused by the inherent nature of being foreign, not because the government specifically aims to disadvantage them.[51] Thus, whether this could be discriminatory would depend on the extent as to which producers are refused the exemption based on their higher emissions during transport. It would also depend on the importance of this criterion and the emphasis placed upon it as compared to the other criteria that the Regulation mentions.

64. Second, several fuels are presumed to fulfill the requirements for a tax exemption, while several other fuels are presumed to not fulfill the requirements. Only in the case that they are found to be like, could there be a violation of the TBT Agreement in the sense of discriminating between like products.

65. Third, if there are suspicions of violation, the products must be analyzed on likeness. If the products are like, it will be necessary to examine whether the imported product receives less favorable treatment. The Swiss measure, as a voluntary standard, cannot be *de jure* discriminatory. But since there is tax exemption for the products which comply with the criteria, it must not be applied in a manner that constitutes a *de facto* discrimination against the group of imported like products, modifying the competitive relationship in favor of the group of local products.[52] This does not mean that is it enough to find one imported product

[51] Footnote 10 of GATS: “Specific commitments assumed under this Article shall not be construed to require any Member to compensate for any inherent competitive disadvantages which result from the foreign character of the relevant service or service suppliers”

[52] Appellate Body Report, *EC - Asbestos*, para. 100: “Thus, even if two products are "like", that does not mean that a measure is inconsistent with Article III:4. A complaining Member must still establish that the measure accords to the group of "like" imported products "less favourable treatment" than it accords to the group of "like" domestic products. The term "less favourable treatment" expresses the general principle, in Article III:1, that

treated less favorably than the treatment of one national like product contrary to the finding of the Panel in Asbestos. We have to look at the effect of the measure on the competitive conditions of the different groups of like products in the market.

66. The commentary to the Regulation states that control will have to be paid for by the producers or importers, which risks to constitute a violation of Article 5.1.1 of the TBT Agreement if it results in disproportionately higher costs compared to the costs of control for native applicants.[53]

67. In addition to non discrimination, the Regulation must be the least restrictive means to reach a legitimate objective.[54] The Regulation is not mandatory and all products are allowed to be sold in the market. Moreover, the Swiss measure has been established to protect biodiversity and natural rainforests and must not be prepared, adopted, or *applied with a view to or with the effect of creating unnecessary obstacles to trade*. It shall not be *more trade-restrictive than necessary to fulfill a legitimate objective of protecting biodiversity.*

68. However, the Swiss measure must not be more trade restrictive than necessary to fulfill its legitimate objective. To make sure that it complies with this obligation, another means could be cooperation between Switzerland and the exporting States concerning the conformity assessment procedure. For instance, it can use the principle of mutual recognition and

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internal Regulations "should not be applied & so as to afford protection to domestic production". If there is "less favourable treatment" of the group of "like" imported products, there is, conversely, "protection" of the group of "like" domestic products. However, a Member may draw distinctions between products which have been found to be "like", without, for this reason alone, according to the group of "like" imported products "less favourable treatment" than that accorded to the group of "like" domestic products."

[53] *"This analysis is often easy, since it concerns products produced from raw materials. For the imported products, this is more complicated, at least until an international verification system has been established for products that have ecological advantages. A direct control of the production conditions on the site is impossible for the Swiss authorities, and also with regard to international law. But it is foreseen to charge private auditors to carry out controls that will have to be paid by the importers or producers and to cooperate with the local authorities where necessary.* Commentary concerning the edict of DETEC, p. 2.

[54] Paragraph E of Code of practice, Article 5.1.2 of TBT Agreement

equivalence.[55] In any case, a complaining party can argue that equivalence and mutual recognition are less trade restrictive alternatives reasonable available to Switzerland, since they are explicitly mentioned in TBT Agreement as a specific mean to avoid unnecessary obstacle to international trade. Switzerland must also take into account the specific situation and condition of developing countries, as well as their particular ecological and economic advantages in using the technologies they consider to be appropriated to their level of protection.[56]

69. Finally, the measure must be based on an international standard if there exists one. Switzerland does not have an absolute obligation to base its measure on an international standard, that is to say, to "employ or apply" the international standard as "the principal constituent or fundamental principle for the purpose of enacting…"[57] its measure. If another Member estimates that the harmonization obligation is violated, it will bear the burden of proving that an international relevant standard exists and is not inappropriate or ineffective means to achieve the legitimate objective pursued by the Swiss measure. It can for example demonstrate *prima facie* that the "Draft Global Principles for Sustainable Biofuels Production" (from the Ecole Polithechnique Fédérale de Lausanne Roundtable for Sustainable Biofuels)[58] is an international standard or its completion is imminent; that Switzerland does

[55] Article 6.1 of the TBT Agreement: " without prejudice to the provisions of paragraphs 3 and 4, Members shall ensure, whenever possible, that results of conformity assessment procedures in other Members are accepted, Even when those procedure differ from their own, provided they are satisfied that those procedure offer an assurance of conformity with applicable technical Regulations or standards equivalent to their own procedures…" In any case, a complaining party can argue that equivalence and mutual recognition are less trade restrictive alternatives reasonable available to Switzerland, since they are a expressly mentioned in TBT Agreement as a specific mean to avoid unnecessary obstacle to international trade.

[56] Article 12 of TBT Agreement. Since they might not have the human, financial and technological capacities to comply with the same high standards, Switzerland could grant them technical assistance

[57] Panel Report, *EC – Sardines*, §7.110.

[58] For more information: http://www. cgse.epfl.ch/page65660-en.html ; Also UNCTAD, "Making Certification Work for Sustainable Development: The Case of Biofuels", UNCTAD/DITC/TED/2008/1, p. 18 & 19. RSB is an international initiative which aims to bring together famers, companies, NGO, experts, Government and intergovernmental agencies concerned with sustainability of biofuels production and processing.

not use this standard or its relevant parts as the basis of its measure and such international standard or relevant parts are effective or appropriate means for the fulfillment of the legitimate objective pursued by it measure. Then Switzerland bears the burden of proving the contrary. If Switzerland proves that its measure is in accordance with the international standard, such measure is reputably presumed not to create unnecessary obstacle to international trade.

70. In sum, there is not a reason to conclude that Switzerland measure cannot be in compliance with TBT Agreement. But it is very important to respect all its provisions relating transparency and cooperation with WTO other Members. The compliance of the measure will depend solely on the manner that Switzerland will apply the measure in practice.

IV Assessment of the positive incentive measures under the SCM Agreement

71. The WTO does not prohibit subsidies per definition. Subsidies are allowed unless a) if they are contingent upon export performance, b) if they are contingent upon the use of domestic over imported goods or c) if they are specific and cause serious injury to another Member, in which case the subsidy must be withdrawn or adapted so as to remove the adverse effects.

A. The scope of the SCM Agreement

72. Article 1 of the SCM Agreement States that a subsidy is ‘a financial contribution by a government or any public body within the territory of a Member’ whereby ‘a benefit is conferred’. The financial contribution has to make the producer better off than he would have been without the subsidy. To determine this, the marketplace is used as a comparison. If the financial contribution is on more favorable terms than the producer would have been able to receive in the marketplace, a benefit is conferred.
73. The financial contribution can take one of the following forms, it must be a government practice which involves:

a) ‘a direct transfer of funds’ or a ‘potential direct transfer of funds or liabilities’[59],

b) ‘government revenue that is otherwise due is foregone[60] or not collected’ (for example a tax credit),

c) ‘a government provides goods or services other than general infrastructure, or purchases goods’,

d) ‘a government makes payments to a funding mechanism, or entrusts or directs a private body to carry out one or more of the functions illustrated in a), b) and c) above which would normally be vested in the government and the practice in no real sense differs from practices normally followed by governments’.

B. Substantive rules of the SCM Agreement

1. Prohibited Subsidies

74. Article 3 SCM States that subsidies within the meaning of Article 1 are prohibited if they are subsidies a) ‘subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance’ (export subsidies) or b) ‘subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic products over imported products’. Both a) and b) cover *de facto* and *de jure* contingency.[61] The contingency does not have to be the ‘sole’ condition governing the grant of a prohibited subsidy, it may be ‘one of several other conditions’.[62]

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[59] A financial contribution exists not only when a direct transfer of funds or a potential direct transfer of funds has actually been effectuated. It is sufficient that there is a government practice involving the transfer of funds. This has also been specified in Appellate Body Report, *Brazil –Export Financing Programme for Aircraf*, WT/DS46/AB/R, 2 August 1999, para.154-159.

[60] The term otherwise refers to a normative benchmark as established by the tax rules applied by the Member concerned. Appellate Body report *Unites States – Tax Treatment for Foreign Sales Corporations,* WT/DS108/AB/R / DSR 2000:III, 20 March 2000, paras. 85-95.

[61] De facto contingency is shown if it is in fact tied to actual or anticipated exportation or export earnings. A subsidy to an export oriented company is not per se an export subsidy. The export orientation of a recipient may be taken into account, but it is only one of several facts and cannot be the only fact supporting a finding of de facto export contingency.

[62] Appellate Body Report, *Unites States – Tax Treatment for Foreign Sales Corporations, Recourse to Article 21.5 of the DSU by the European Communities,* WT/DS108/AB/RW, DSR 2002:I, 29 January 2002, para. 111.

75. If a country believes that a prohibited subsidy exists and if consultations fail, the dispute may be referred to a Panel. If a Panel finds a prohibited subsidy, the subsidy must be removed without delay.

2. Actionable subsidies

76. Assuming that a measure is a subsidy within the meaning of the SCM Agreement, it is nevertheless not subject to the SCM Agreement unless it has been specifically provided to an enterprise or industry or group of enterprises or industries. The exception to this is a prohibited subsidy, Article 2.3 SCM provides that 'Any subsidy falling under the provisions of Article 3 shall be deemed to be specific.' The basic principle is that a subsidy that distorts the allocation of resources within an economy should be subject to discipline. Where a subsidy is widely available within an economy, such a distortion in the allocation of resources is presumed not to occur. Thus, only "specific" subsidies are subject to the SCM Agreement disciplines. As provided by Article 2.1, 2.2 and 2,3 SCM, there are four types of "specificity" within the meaning of the SCM Agreement:

    a) enterprise specificity: the subsidy is meant for a certain company/companies

    b) industry specificity: the subsidy is meant for a certain sector/sectors

    c) regional specificity: the subsidy is meant for producers within a certain region of the territory of the authority granting the subsidy.

    d) prohibited subsidies: a subsidy is deemed to be specific if it falls under Article 3, a situation in which the government targets export goods or goods using domestic inputs for subsidizing.

77. Article 2.1 (b) provides that 'where the granting authority (..) establishes objective criteria or conditions governing the eligibility for, and the amount of, a subsidy, specificity shall not exist, provided that the eligibility is automatic and that such criteria are strictly adhered to.' Footnote 2 to the SCM Agreement specifies that objective criteria and conditions are 'criteria and conditions, which are neutral, which do not favor certain enterprises over others, and which are economic in nature and horizontal in application, such as number of employees or

size of enterprise.' The SCM Agreement also covers subsidies that are not specific at first sight, but that might operate in a specific manner.[63]

78. In *US-Upland Cotton,* the Panel stated that the breadth of the concept of industry is not necessary to determine a fixed scope of the concept. A subsidy would cease to be specific because it is sufficiently broadly available throughout an economy as not to benefit a particular limited group of producers of certain products.[64] The Panel in *US-Softwood Lumber IV* added that the availability of a subsidy which is limited by the inherent characteristics of the good cannot be considered to have been limited by 'objective criteria'.[65]
79. If all above mentioned conditions are fulfilled, the subsidy could be contested if it causes adverse effects to the interests of another Member. Article 5 SCM provides that 'No Member should cause, through the use of any subsidy (..) adverse effects to the interests of other Members, i.e.: (a) injury to the domestic industry of another Member; (b) nullification or impairment of benefits accruing directly or indirectly to other Members under GATT 1994 (..); (c) serious prejudice to the interests of another Member.' Thus, to be actionable, a subsidy must be a) specific and b) cause one of the three types of adverse effects to the interests of another Member and (c) causation has to be proven, the fact that the subsidy is the cause of the adverse effects.
80. If a subsidy is actionable and the Complaining party can show that the subsidy has one of the above mentioned effects, the subsidy must be either withdrawn or its adverse effects must be taken away.

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[63] Thus, the SCM Agreement covers both de facto and *de jure* specificity. De facto specificity can be identified by a) the use of a subsidy by a limited number of certain enterprises, b) predominant use of a subsidy by certain enterprises, c) granting of disproportionately large subsidies to certain enterprises or d) the manner in which the authority granting the subsidy exercises discretion.

[64] Panel Report, *United States-Subsidies on Upland Cotton*, (WT/DS267/R) / DSR 2005:II- III- IV- V- VI, 21 March 2005, para. 7.1142.

[65] Panel Report, *United States-Final Countervailing Duty Determination With Respect to Certain Softwood Lumber From Canada,* WT/DS257/R, 17 February 2004, para 7.116, footnote 179.

81. Finally, if a violation were to be found, the measure might be justified under Article XX of the GATT. There is no certainty whether a violation of SCM might be justifiable under Article XX, because the Panel / Appellate Body has not yet had the chance to decide on this. However, as explained in recent case law the Appellate Body left the issue open.
82. Since the GATT also contains a provision on subsidies, namely in Article XVI GATT, the SCM Agreement could also be seen as an application or extension of Article XVI GATT. Thus, there is a direct relationship between the GATT and SCM. Furthermore, since a country could try to justify any violation of a GATT Article under Article XX GATT (and thus a country could also justify a violation of GATT Article XVI under GATT Article XX), and since Article XVI GATT is linked to the SCM Agreement and deals with the same matters, it is be imaginable that the exceptions of the GATT would apply to the SCM Agreement.[66] Moreover, production subsidies are generally regarded as less trade restrictive than for example quantitative restrictions, bans or higher tariffs and therefore could be seen as a preferable way to protect such legitimate values as the environment. However, the SCM Agreement no longer has an exception since the exception contained in Article 8 has elapsed. Therefore, one could argue that the exceptions of Article XX GATT should and could apply to the SCM Agreement since a) there is a direct link between the GATT and SCM, b) SCM does not have an exception of its own any more, c) subsidies are the less trade restrictive.

C. Examination of the measures

83. Now that the requirements for subsidies have been set out, the positive incentive measures as adopted by Brazil and Switzerland can be analyzed on probable compliance with the SCM Agreement.

[66] It seems imaginable that since a violation of Article XVI GATT can be justified under Article XX GATT, as well as a violation of Article III:8(b) (an Article dealing containing provisions on subsidies exclusively given to domestic producers), the SCM Agreement as an elaboration of Article XVI GATT would have access to GATT Article XX since the Agreement itself does not have any exception provisions that are still in effect.

1. The Brazilian and Swiss measure

84. Both the Swiss and Brazilian measures allow for a tax reduction, if certain criteria and/or conditions are fulfilled, as explained in Section II A and II B.[67] Both measures can be considered a subsidy in the sense of 'government revenue otherwise due that is foregone or not collected'. In the case of Switzerland and Brazil, the tax collected if the Regulation had not been in place (but for the measure) would be the normal tax without any reductions. Thus in the case of Switzerland, the tax would be the same as for the other biofuels. Since the Regulation taxes normally the biofuels/products that do not meet the criteria, while the other fuels/products are taxed differently, the government can be seen to forego revenue.[68] In addition to tax credits, the Brazilian measures also provides for the grant of loans.

85. The foregoing of revenue confers a benefit. The lower tax makes the product receiving the subsidy cheaper and thus puts the producer in a more beneficial position in the market. It makes the producer better off than he would have been without the tax reduction. The grant of loans confers a benefit as well, if the loans are provided on more favorable terms than the marketplace would have.[69]

86. The measure will only be prohibited if the grant of the subsidy is conditional upon either export performance, or upon the use of domestic over imported goods.

87. In the first case, the grant of the subsidy must be tied to export performance, either in law or in fact. Concerning the Brazilian measure, in order to receive the tax credit, a producer has to

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[67] For the Brazilian measure, it is necessary to comply with three out of ten criteria, while the Swiss measure allows for a tax reduction is certain sustainability criteria are met.

[68] There are two ways of proving revenue foregone. First, the tax reduction can be examined against a 'normative benchmark'. The normative benchmark has to be the Swiss legislation, since every State has the right to decide on its own taxation scheme. Thus, this specific reduction has to be compared to other Swiss tax rules to see if the government is not refraining from collecting taxes that it should collect. Another possible analysis is to examine what the taxation would be 'but for' the measure, thus how the fuels would be taxed if the measure would not be into force. If the Complaining party cannot proof that the government is not collecting this tax while it should, there is no subsidy and thus SCM does not apply.

[69] It can be presumed that this will be the case, otherwise the producers could also turn to the marketplace and there would not be a need for governmental loans.

comply with three out of ten criteria. One of the criteria provides that the production should contribute to the increase in exportations to the national and international market. This criterion involves *de jure* export requirements. Article 3.1 (a) SCM states that the contingency does not have to be the 'sole' condition governing the grant of a prohibited subsidy, it may be 'one of several other conditions'. The Panel in *US-Cotton* has interpreted the cases of *US-FS, Article 21.5* and *Canada-Aircraft* 'to stand for the proposition that export contingency in respect of a discrete segment of payments in one set of circumstances may not be vitiated by the existence of other discrete segments of payments which may not be conditioned upon exportation'.[70] In this particular case, the Panel concluded that 'the fact that the subsidies granted in the second situation may not be export contingent does not dissolve the export contingency arising in the first situation.'[71] This leads to the presumption that the Brazilian measure could constitute a prohibited subsidy under Article 3.1(a).

88. However, the measure must be 'contingent' upon export performance. Contingent can also be defined as conditional, which means that the subsidy must be conditional or dependent upon export performance. In this case, the subsidy will not be granted only on the basis of export performance, since three criteria need to be fulfilled. Thus, it is also possible to receive the subsidy without complying with the export requirement. Therefore, it is not certain how the Panel would decide, but the mentioned case law and the wording of Article 3.1(a) imply that the measure might be found to constitute a subsidy contingent upon export performance.

89. The Swiss measure does not constitute a *de jure* subsidy contingent upon export performance. The AB in *Canada-Aircraft* Stated that proving *de facto* export contingency is a more difficult task. The existence of the relationship between contingency must be inferred from the total configuration of the facts constituting and surrounding the granting of the subsidy.[72] Concerning *de facto* export contingency, footnote 4 of the SCM Agreement provides that

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[70] Panel Report, *US-Cotton Subsidies*, Paras. 7.710-720.

[71] Panel Report, *US-Cotton Subsidies*, Paras 7.739.

[72] AB Report, *Canada-Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, 20 August 1999, para. 167.

'This standard is met when the facts demonstrate that the granting of a subsidy, without having been made legally contingent upon export performance, is in fact tied to actual or anticipated exportation or export earnings.' Thus the footnote makes clear that *de facto* export contingency must be demonstrated by the facts, a relationship of conditionality or dependence must be demonstrated.[73] The subsidy must be tied to or contingent upon actual or anticipated exports. It does not suffice to demonstrate solely that a government granting a subsidy anticipated that exports would result.

90. The Swiss measure does not appear to constitute a *de jure* subsidy contingent upon export performance. Any *de facto* contingency must be inferred from the facts. The requirements of the Regulation appear to be origin neutral. The measure will most likely not constitute a *de facto* export performance subsidy, unless in its application the subsidy is only granted to producers that export biofuels.
91. The subsidy will also be prohibited if it is contingent upon the use of domestic over imported products. First, the Brazilian Regulation States in Article 19 that if the conditions are similar in the sense of prices, logistic costs, quality and time and delivery of the products, in order to receive the subsidy, preference should be given to the purchase of products, product parts and secondary products that are produced in the territory of Amazonas. This Article directly favors the use of domestic over imported goods if the circumstances are similar. If producers do not comply with this requirement, the subsidy will not be granted.[74] Therefore, this subsidy could be considered to be contingent upon the use of domestic over imported goods.[75]
92. In the Swiss measure sustainable biofuels will receive the lower tax. The criteria appear to be objective and origin neutral. *De jure* there is no contingency. However, *de facto* contingency is also covered by Article 3.1 (b). The subsidy will only be prohibited if in the application of

[73] AB Report, *Canada-Aircraft,* para. 169, 171.

[74] Article 4 contains a list of 10 criteria of which 3 have to be met in order to receive the subsidy. One of the criteria favours the use of domestic over imported products. However, producers will never receive the subsidy if they only comply with one criteria, nor will they be refused the subsidy if they comply with three other criteria.

[75] A violation of Article 3.1(b) might also be justifiable under Article XX GATT, since the measure seems to be adopted with the view of protecting the biodiversity and stimulate regional development.

the Regulation, only domestic fuels receive the tax credit. Thus, if for example due to the transport criteria all imported fuels are refused the tax credit and only domestic producers receive the subsidy, the measure will be prohibited under Article 3.1 (b). The Swiss subsidy will most likely not be prohibited under Article 3.1 (b) SCM, but it will depend on whether the application of the measure is so as to exclude imported fuels from the tax credit.

93. Additionally, the measure provides that fuels made from waste whereby the latest technology has been used, are presumed to fulfill the requirements and will be granted the lower tax. Contrary, fuels made from soya, cereals or palm oil are presumed to not fulfill the requirements. If fuels made from waste are primarily produced by Swiss producers and not by foreign producers, and if other foreign fuels are in general not accorded a lower tax, this might be considered contingency upon the use of domestic over imported products.
94. However, if both imported and foreign producers equally benefit from a lower tax, there will not be a subsidy contingent upon the use of domestic over imported products and the subsidy will not be prohibited under Article 3 SCM. It does not seem likely that the before mentioned situation will occur, in which case the subsidy will not be prohibited under Article 3 SCM.
95. If the subsidy is not prohibited, it will only fall under SCM if the subsidy is specific. The Brazilian tax credit is specifically provided to an enterprise or industry or group of enterprises or industries. The government targets producers in Amazonas, which constitutes regional specificity.
96. The Swiss measure applies to all biofuel producers that fulfill the sustainability criteria. The Panel in *US-Softwood Lumber IV* further recalled that a subsidy is specific if it is "specific to an enterprise or industry or group of enterprises or industries." In this regard, the Panel noted that "industry" is defined as "a particular form or branch of productive labor; a trade, a manufacture," and it said that the term "industry" in Article 2 is not used to refer to enterprises producing specific goods or end-products.
97. Moreover, the Panel *US-Softwood Lumber IV* stated that ‘In the case of a *good* that is provided by the government - and not just money, which is fungible – and that has utility only

for certain enterprises (because of its inherent characteristics), it is all the more likely that a subsidy conferred via the provision of that good is specifically provided to certain enterprises only. We do not consider that this would imply that any provision of a good in the form of a natural resource automatically would be specific, precisely because in some cases, the goods provided (such as for example oil, gas, water, etc.) may be used by an indefinite number of industries.' Thus, the Panel stated that the provision of fuels may not be specific, since everyone uses energy. However, in the Swiss measure fuel is not provided, but a subsidy is given to sustainable fuel producers of alternative fuels.[76] On the one hand, this can be considered as a broad group of receivers and thus not specific. On the other hand, the subsidy is not given to all alternative fuel producers, but only certain producers, namely the ones producing sustainable biofuel. Thus, the tax credit excludes all other fuels. If the (sustainable) biofuel producers are found to be a limited group of industries, the measure will be found to be specific.[77] The measure might be found to be specific, since it is granted only to the sustainable producers of the biofuels, which could be considered to constitute a limited group of industries.

98. If the subsidy is found to be specific, it can be contested if it causes adverse effects to the interests of another Member. The Swiss government stresses the importance of the tax reduction in the explication of the Articles. Several fuels will most likely not benefit from a lower tax, namely fuels made from palm oil, soya or cereals. In the event that this lowers demand for these fuels dramatically and in the event that a country thereby is severely harmed, the subsidy might be actionable, meaning that if the measure would be contested, it might need to be withdrawn or changed.
99. While both measures can be found to be a subsidy, he Swiss measure most likely does not constitute a prohibited subsidy. Thus it can only be contested if it causes such adverse effects

[76] It only has a direct impact on certain sustainable fuel users, and a potentially indirect impact on most producers using alternative fuel in the sense of lower prices.

[77] In *US Softwood Lumber IV*, the Panel considered that the "wood products industries" constitutes "at most only a limited group of industries" under "any definition" of the term "limited." (Para. 7.121)

to the interests of another Member, in which case any violation might be justifiable under Article XX GATT. The Brazilian measure might constitute a prohibited subsidy in the sense of Article 3.1 (b) or possibly Article 3.1 (a). This measure might be justifiable under Article XX (b) or (g).

V Assessment of the positive incentive measures under the GATT Agreement

100. The GATT Agreement deals with rules for trade in goods. The Agreement contains several important principles that will be explained in this part.

A. Article III:2 GATT, National Treatment

101. Article III:2 GATT contains a national treatment obligation, 'the products of the territory of any contracting party imported into the territory of any other contracting party, shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly to like domestic products.'

102. Thus, the measure must be an 'internal tax or other charge which is applied directly or indirectly on products'. Second, the national treatment obligation applies to 'like products' national and imported products have to be like for paragraph 2 to apply, or at least they have to be directly competitive or substitutable ("DCS").

103. Likeness is examined by analyzing the following criteria: physical characteristics, end uses, consumer habits and preferences, tariff classification.[78] The same criteria are analyzed for competitiveness and substitutability, but more emphasis will be put on the market place. If imported and national products are found to be like, the imported products cannot be taxed in excess of national products.

104. If the imported product affected by the tax measure is not a like product but rather a direct competitive and substitutable product ("DCS"), the requirements for a possible violation are different. In fact, the requirement of "excess" in the taxation of the imported product is replaced by the broader requirement of "not similar taxation": this means that, in the case of

[78] As defined in the Border Tax Adjustment Report and as defined by the Appellate Body in *Japan-Alcohol.*

two DCS products, to meet a violation of GATT Article III:2 the difference in the level of taxation should be bigger than in the case of like products.[79] The dissimilar taxation should be above 'the minimis' that is to say so high as to shift consumption from one product to the other. In addition, in the case of DCS products a fourth requirement should be met, the different level of taxation should be applied "so as to afford protection to domestic production". To establish whether this fourth requirement is met, attention should be paid to the way the tax measure operates with regard to the two domestic and imported products: in particular it should be established if the tax has a discriminatory effect on the imported product.[80]

B. Article III:4 GATT, National Treatment

105. Article III:4 GATT provides that 'the products of the territory of any contracting party imported into the territory of any other contracting party shall be accorded treatment no less favorable than that accorded to like products of national origin in respect of all laws, Regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use'. Thus, for this paragraph to apply, the measure must be a 'law, Regulation or requirement which affects the internal sale of products.' Second, the national treatment obligation applies to like products. Likeness is examined in the same way as likeness in paragraph two, only this definition of likeness is broader. It will be easier to find products like under paragraph 4 than under paragraph 2.

106. If imported and national products are found to be like, the imported products cannot be treated less favorably than domestic products. The Appellate Body Stated in *EC-Asbestos* that the term "less favorable treatment" expresses the general principle, in Article III:1, that internal Regulations "should not be applied (…) so as to afford protection to domestic production."

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[79] Appellate Body Report, *Japan – Taxes on Alcoholic Beverages* II, WT/DS8/10/11/AB/, 4 October 1996, 118.

[80] Whether a measure is so as to afford protection can be discerned from the design, structure and application of the measure.

C. Article I:1 GATT, Most Favored Nation

107. The Most Favored Nation principle contained in Article I:1 GATT provides that any advantage that is granted to an imported product of a Member, should be granted immediately and unconditionally to the like product of another Member.

D. Examination of the measures

1. The Brazilian measure

108. The Brazilian measure could fall under Article III paragraph 2 of the GATT. The laws states that one of the mandatory conditions for granting these incentives is (Article 19 VII) that the enterprise in similar conditions of competition may guarantee the preference for the purchase of local intermediate products and raw materials deriving from or manufactured in the State.

109. This provision could be examined under Article III, the national treatment obligation, because the State would grant a tax incentive depending on whether the beneficiaries give preference to local raw materials or intermediate products. This measure might violate the National Treatment Principle of the GATT.

110. This is a tax measure addressed from (a) to (b), but benefiting also (c): national industries. First, there is a tax measure issued at the national or sub-national level. In this case the measure at issue is the ICMS, corresponding to the Value Added Tax (VAT). Secondly, the products will be examined on their likeness. If they are found to be like, any differential taxation that is in the disadvantage of the imported product is prohibited.

111. In the case at issue the law 2826/2003 may provide a different level of taxation between products covered by the incentives and products that do not fall into the requirements established by the law. The concession of the incentive is limited to the production of limited categories of products listed in art. 10. The list also includes “agro-industrial products and similar, forestry and animal products, pharmaceuticals, cosmetics and perfumes that use raw materials that are produced inside or around the region […]”. In addition, Article 13.3

provides that for this category of products, if they are produced into the State of Amazonas, they may benefit of a credit of 100%.

112. This provision might be discriminatory in the application of the measure since the condition for the grant of the tax incentive is the place of production, in fact, if the enterprise (b), under the same conditions and at the same price, gives preference to the local raw materials instead of foreign raw materials, it will be granted the tax incentive. In this case, the level of taxation of the domestic product would differ from the level of an imported like product or an imported direct competitive or replaceable product. However, there will only be a violation if the taxation is above the minimis, for which it would be necessary to examine the effect of the dissimilar taxation. In the case Japan-Alcohol, a 5% tax differential was considered to be above the minimis.

113. Moreover, it has to be shown that the measure is so as to afford protection to domestic industry. This is the key point of the analysis of the measure, since one argument that could be used to justify the measure could be that the measure is aimed at the protection and conservation of the biodiversity. In this regard, the AB established in *Japan – Alcoholic Beverages* that "It is not necessary for a panel to sort through the many reasons legislators and regulators often have for what they do and weight the relevant significance of those reasons to establish legislative or regulatory intent […]. It is irrelevant that protectionism was not intended objective if the particular tax measure in question [is applied so as to afford protection]".

114. Therefore, according to the AB, there is not any possibility to use policy objectives as elements which allow establishing that the measure has not been issued "as to afford protection". However, in *Canada – Periodicals*, the AB "did seem to give at least some importance to Statements of representatives of the Canadian Government about the policy objectives of the tax measure at issue".[81]

[81] P. Van Den Bossche, Law and policy of the World Trade Organization, Cambridge University Press, second edition, 2008, p. 367.

2. The Swiss measure

- Article III:2 GATT first sentence

115. The Swiss measure falls under Article III:2 GATT.[82] The measure is a taxation Regulation that applies directly to the biofuels. If a domestically produced biofuel is granted the tax credit, while the imported biofuel is not granted the tax credit, these products will be examined on their likeness. It is not certain whether the Panel will find biofuels to be like products. It will be a case-by-case examination. When the fuels are made from the exact same material, for example from the same waste or both from palm oil, they will probably be found to be like[83], unless the fourth criteria, consumer preferences, would allow for distinctions to be made. Unlikeness between two similar products made of the same materials might be found as a result of a distinction made by consumers between the products in the marketplace. In the *EC-Asbestos* case, the products were not considered as like, because consumers would make a distinction between the products based on their health effects. If in this case the consumers, backed up by market studies, would make a clear distinction between two fuels based on their environmental sustainability, a Panel could find the products to be unlike. However, it would have to be demonstrated that the consumers make the distinction between the products themselves and not as a result of the measure. Furthermore, it must be noted that in the case of *EC Asbestos* it involved a product that constituted a danger to the consumer in and of itself, which does not seem to be the case with biofuels. It is therefore uncertain whether a Panel would find a distinction made by the consumer to be enough evidence of unlikeness. The market perception has more value and weight in the examination of directly competitive or substitutable (second sentence of Art. III:2 further examined below).

116. A Panel might find products to be unlike if they are not from the same materials, since in that case they will, besides their sustainability and possibly the consumer preferences, differ in their physical characteristics and in some cases in their tariff classification.

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[82] Alternatively, the measure could also fall under Article III:4 GATT

[83] since their physical characteristics will be the same as well as their tariff classification and end use.

117. However, as explained in paragraph … distinguishing between two products, solely based on their production and process method (a PPM) is a debated issue. A distinction based on a PPM was made and accepted in *EC-Asbestos*, but the production method left traces that were incorporated in the product which made that the product itself constituted a danger to consumers. In this case, the biofuels do not seem to present a danger in and of themselves, nor do they seem to incorporate traces of the production method. The danger or harmful effects are rather in the country of production. The Regulation clearly specifies that the tropical rainforests should be protected as well as the biodiversity and the conditions in the country of production. For example, one of the criteria the Regulation will take into account is the way the land is used in the country of production. However, the use of land in an unsustainable way affects the biodiversity in the country producing the fuel and does not directly have an impact on Switzerland.

118. The chance of being able to distinguish between two of the same products solely based on their production process is limited. The only possibility is when consumers prefer the more environmentally friendly fuel or if the market clearly distinguishes between the fuels, and thus does not perceive them as being like. This leads to the presumption that, if fuels are made from the same materials, but only differ in the sense that one uses the latest technology and the other an older technology, this will most likely not be enough of a basis to consider them unlike, but a violation of this Article might be justifiable under Article XX of the GATT. Furthermore, the issue of PPM is still controversial in the WTO and there is no final answer yet.

119. If products are found to be like, any taxation of imported products in excess of taxation of domestic products is prohibited.

- **Article III:2 GATT, second sentence**

120. If the products are not found to be like, then the second paragraph will involve an analysis of whether the products are directly competitive or substitutable. This test is easier to pass, since the products do not have to be exactly alike. (Most) Biofuels will probably be considered to

be directly competitive or substitutable, unless the difference in sustainability makes the products uncompetitive to the consumers. This distinction made by consumers would have to be made by them independently and not as a result of the taxation measure.

121. A violation will not be found if the differential taxation is not above the minimis. In *Japan – Alcohol* a 5% difference was accepted. Since the commentary concerning DETEC underlines the 'big economic advantage' of the tax reduction, the tax differential might be considered above the minimis. Finally, a violation can only be found if the measure is applied so as to afford protection. The requirements of the measure appear to be origin neutral. There is only a small possibility that a violation will be found since several biofuels are likely to be excluded, while others are per definition considered to fulfill the requirements. The measure will only be prohibited if these distinctions result in protection to the domestic industry, thus if due to these distinctions almost only, or predominantly, domestic producers can benefit from the lower tax while most or a large share of importers are excluded from the tax.

122. Moreover, the control will have to be paid by the producers or importers, which if it results in disproportionately higher costs for imported products than compared to the costs of control for native applicants, might be considered evidence of protectionism.

Article I:1 GATT

123. The same analysis will be done for the most favored nation principle. The imported products will be examined under likeness. Likeness under Article I (most favored nation principle) is most likely broader than under paragraph 2 of Article III GATT. Thus, it will be most likely closer to the likeness test under the 4th paragraph. The same likeness analysis will be done, except that a foreign product will be compared to another foreign product instead of a domestic one. If the two imported products are found to be like and one receives the tax reduction, while the other does not, there will be a violation of Article I GATT. A violation may be justifiable under GATT Article XX.

VI Exceptions

124. If a measure of a WTO Member is found to be inconsistent with one or more provisions of the GATT, the same Member can invoke an exception to protect some important non-economic values, such as social and environmental values and public health (GATT Article XX). In particular GATT Article XX (b) and (g) concern the protection of the environment and natural resources.

125. First, GATT Article XX (g) provides an exception for the application of the rules of the GATT in case of application of protectionist measures for the "[…] conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption"; Second, GATT Article XX (b) establishes an exception in case of the application of a measure for the protection of human, animal, plant life and health.

126. Once is shown that the measure is in conformity with the requirements of one or several paragraphs such as XX b) or g), a country needs to show that the measure does not violate the requirements of the chapeau of Article XX of the GATT, whose purpose and object is the prevention of abuse or misuse of the exceptions of Article XX[84].

127. First, the measure needs to fall under one of the exceptions contained in the paragraphs. The paragraphs dealing with environment are b) and g). Concerning Article XX (b), a measure must meet the following criteria to fall under this justification.

a) The policy objective pursued by the measure must be the protection of life or health of humans, animals or plants.

b) The measure must be necessary to fulfill the policy objective. This involves a necessity test, in order to pass the necessity test, three factors may be taken into account, weighed and balanced: 1) The importance of the protected value 2) The extent of the contribution of the measure to the goal is meaningful 3) There is no less trade restrictive alternative[85]..

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[84] Appellate Body Report, *United States –Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R, 29 April 1996, para. 22.

[85] The necessity test of has been analyzed above under the TBT Agreement.

128. Concerning Article XX (g), a measure must meet the three tier test.

a) The policy objective pursued by the measure at issue is the conservation of exhaustible natural resources.

b) The measure at issue must relate to the conservation of exhaustible natural resources.

c) The measures are made effective in conjunction with restrictions on domestic production or consumption.

129. Second, if the measure meets the requirements of either Article XX (b) or (g), in order to apply art. XX exceptions, the measure at issue should comply with the chapeau. The measure applied may not constitute: a) either arbitrary or unjustifiable discrimination between countries where the same conditions prevail, nor b) a disguised restriction on international trade. This provision aims at avoiding the abuse of the exceptions as a pretext to raise the level of protectionism. At this regard the Appellate Body found that the call for an exception should be the result of a balance between the values protected by art. XX and the rights of the other Members under the GATT 1994[86]. Moreover, the evaluation of consistency of the measure with the *chapeau* should be made taking into account its practical application.

A The Swiss and Brazilian measure

130. In the Swiss and Brazilian measures, in order to invoke the art. XX, the government must show that the measure does not constitute an arbitrary or unjustifiable discrimination between countries where the same condition prevails[87], or disguised restrictions on international trade. It is generally more difficult to comply with these requirements than with the paragraphs. However, to do so, the party should not apply its measure to countries where different

[86] Appellate Body Report on US-Shrimps, par. 159.

[87] A measure violates this requirement if three elements exist: "First, the application of the measure must result in discrimination. As we stated in United States – Gasoline, the nature and quality of this discrimination is different from the discrimination in the treatment of products which was already found to be inconsistent with one of the substantive obligations of GATT 1994, such as Articles I, III, XI. Second, the discrimination must be arbitrary or unjustifiable in character… Third, this discrimination must occur between countries where the same conditions prevail. In United States – Gasoline, we accepted the assumption of the participants in that appeal that such discrimination could occur not only between different exporting Members, but also between exporting Members and the importing Members concerned"; AB Report, *US – Shrimp*, para. 150.

conditions prevail without inquiring into the appropriateness of its measure for the conditions prevailing in other exporting countries. It must take into account different conditions which may occur in the territories of other Members. The measure shall not be applied in a rigid or inflexible manner.[88] It shall give equivalence to foreign measures that are comparable in effectiveness[89], for example measures which aim at enforcing the CBD.

131. Under Article XX g), the party that invokes the exception should first demonstrate that the aim of the measure is the conservation of exhaustive natural resources[90]. In the US – Gasoline, the panel recognized that pure air was an "exhaustive natural resource". Can the protection of biodiversity fall within the scope of art XX g)? In other words, is it possible to include the CBD into the scope of the conservation of exhaustible natural resources?

132. In the Shrimp case the AB referred to non-WTO law and in particular to the CBD, to define the notion of exhaustible resources. The AB has not limited the notion of natural resources to the "non living" or mineral resources; instead, it considered that "exhaustible" natural resources and "renewable" natural resources are [not] mutually exclusive. One lesson that modern biological sciences teach us is that living species, though in principle, capable of reproduction and, in that sense, "renewable", are in certain circumstances indeed susceptible of depletion, exhaustion and extinction, frequently because of human activities"[91].

133. The AB could reach this conclusion adopting an evolutionary interpretation of the notion of exhaustible resources: "From the perspective embodied in the preamble of the WTO Agreement, we note that the generic term "natural resources" in Article XX (g) is not "static" in its content or reference but is rather "by definition, evolutionary". It is, therefore, pertinent

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[88] Appellate Body Report, *Unites States –Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, 12 October 1998, paras. 164, 165, 177.

[89] Appellate Body Report, *Unites States –Import Prohibition of Certain Shrimp and Shrimp Products* (Recourse to Article 21.5 of the DSU by Malaysia), WT/DS58/AB/RW, 22 October 2001, para 144.

[90] Panel Report, *United States –Standards for Reformulated and Conventional Gasoline*, WT/DS/R 20 May 1996, para. 6.37; AB Report, p. 16.

[91] Appellate Body Report, *US – Shrimp*, para. 128.

to note that modern international conventions and declarations make frequent references to natural resources as embracing both living and non-living resources" [92].

134. Therefore the AB interpreted the notion of exhaustible resources in the light of other international conventions, such as the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES). The legal basis of this kind of interpretation is the ordinary meaning of the treaty (Article 31.1 of the VCLT).

135. Therefore it is possible to admit that in the case of the Swiss and Brazilian measures a Panel could refer to the CBD when applying Article XX g GATT. It should be underlined that the preamble of the WTO Agreement clearly mentions the objective of sustainable development, which is the objective of the CBD. This approach would be clearly conforming to the principle of effectiveness in the interpretation of the treaties.

136. In the two cases at issue, the party that would invoke the exception before a Panel should most likely not have any difficulties to demonstrate that its measure is "relating to … conservation of natural resources", meaning that the measure is primarily aimed at the conservation of natural resources[93]. According to AB in US – Shrimp, Article XX g) requires "a close and real" relationship between the measure and the policy objective.[94] Thirdly, the party must demonstrate that its measure meets "[…] a requirement of even-handedness in the imposition of restrictions for both domestic and imported, in the name of conservation, upon the production or consumption of exhaustive natural resources".[95]

137. In the Swiss and Brazilian measures, in order to invoke the art. XX, the government must show also that the measure does not constitute an arbitrary or unjustifiable discrimination between countries where the same condition prevails [96], or disguised restrictions on

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[92] *Ibidem*, para. 130.

[93] Appellate Body Report, *US – Gasoline*, 18-19.

[94] Peter Van den Bossche, Nico Schrijver, Gerrit Faber, *Unilateral measures addressing non-trade concerns*, published by the Ministry of Foreign Affairs of the Netherlands, the Hague, 2007, p. 113.

[95] Appellate Body Report, *US-Gasoline*, par. 20.1; also Appellate Body Report, *US- Shrimp*, par. 144.

[96] A measure violates this requirement if three elements exist: "First, the application of the measure must result in discrimination. As we states in United States – Gasoline, the nature and quality of this discrimination is

international trade. It is generally more difficult to comply with these requirements than with the paragraphs. However, to do so, the party should not apply its measure to countries where different conditions prevail without inquiring into the appropriateness of its measure for the conditions prevailing in other exporting countries. It must take into account different conditions which may occur in the territories of other Members. The measure shall not be applied in a rigid or inflexible manner.[97] It shall give equivalence to foreign measures that are comparable in effectiveness[98], for example measures which aim at enforcing the CBD. This approach will not be contrary to the CDB and will be in right line with the general principle of Common but Differentiated Responsibility in environment protection concern.[99]

VII Conclusion

138. After having analyzed the measures at issue and inserted them into the context of the WTO law and the CBD, some conclusions can be drawn. The measures themselves do not seem to be incompatible with the WTO Covered Agreements. In fact, in these cases, the WTO gives a sufficient freedom to its Members to apply the provisions of the CBD. Therefore Brazil or Switzerland could justify their measures within the application of the Agreements, such as

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different from the discrimination in the treatment of products which was already found to be inconsistent with one of the substantive obligations of GATT 1994, such as Articles I, III, XI. Second, the discrimination must be arbitrary or unjustifiable in character… Third, this discrimination must occur between countries where the same conditions prevail. In United States – Gasoline, we accepted the assumption of the participants in that appeal that such discrimination could occur not only between different exporting Members, but also between exporting Members and the importing Members concerned"; Appellate Body Report, *US – Shrimp*, para. 150.

[97] Appellate Body Report, US – Shrimp, paras. 164, 165, 177.

[98] Appellate Body Report, *US – Shrimp (Article 21.5 – Malaysia*), para. 144.

[99] See Principle 7 of the Rio Declaration on Environment and Development: "States shall cooperate in a spirit of global partnership to conserve, protect and restore the health and integrity of the Earth's ecosystem. In view of the different contributions to global environmental degradation, States have common but differentiated responsibilities. The developed countries acknowledge the responsibility that they bear in the international pursuit to sustainable development in view of the pressures their societies place on the global environment and of the technologies and financial resources they command"

TBT, SCM and the GATT, since they seem to fulfill the conditions required by these treaties. In the cases analyzed in this work, the conditions required by the WTO Covered Agreements do not seem to be as rigorous as to create an inextricable conflict between the CBD and the WTO.

139. The conditions and the limits for the application of the elements of flexibility of the WTO law are made to avoid the adoption of a disguised protectionist measure and to protect the domestic products. Hence, the CBD could be taken into consideration by a Panel in the application of the WTO law, as the US-Shrimp case demonstrated, as an element of context for the interpretation of the meaning of the provisions of the WTO, and therefore include the conservation of the biological diversity into the general exception of GATT Article XX. Moreover, since the report of the Panel of the EC - Biotech case has neither been uphold by the AB (yet) nor is incontestably acceptable, it can be argued that a direct inclusion of the biodiversity protection and conservation into the scope of the Article XX GATT exception is still possible.

140. The Swiss and Brazilian measures can be estimated as compatible with the WTO if the principle of good faith is respected: the good faith will be recognized if the measures demonstrate a concerted and multilateral approach in the protection of the biological diversity. This approach has the advantage to lend more transparency and flexibility in the enforcement of the national measures.

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