

## ***Reassessing 'Like Products'***

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### **Introduction**

The issue of process and production methods (PPMs) in the trade regime has vexed the environmental community since the first tuna–dolphin panel claimed that distinctions between products based on their production methods were not permitted under GATT. The reason for its distress is straightforward: an open trading system, which does not provide for distinctions between products produced sustainably and those produced unsustainably, is unacceptable from an environmental perspective.

Unless the issue of PPMs is resolved reasonably, the environmental community will ultimately oppose trade liberalization. It is up to those interested in trade policy to decide whether they are willing to pursue their goals against environmental opposition; in essence whether they can persuade voters in democratic societies that the economic benefits they promise outweigh not only the inevitable economic costs to those who do not enjoy comparative advantage, but also the risks to the environment, and to communities.

### **'Like Products' in WTO dispute settlement**

Before addressing possible solutions to the issue of PPMs within the trading system, it is necessary to dispose of the myth that no such distinctions are possible, either because this is contrary to fundamental principles of the trading system or simply because the current text of GATT forbids it. Frequent repetition of this error, including repetition by those responsible for managing the trading system and by many eminent commentators, makes it no more correct than it was to begin with.

The issue of PPMs in the GATT/WTO revolves around the interpretation of the word 'like,' as in 'like products.' The concept of like products is in many ways the linchpin of the GATT/WTO system. Its two central principles, most-favoured nation treatment (MFN) and national treatment are critically dependent on this concept. The key passages in GATT read as follows:

'any advantage, favour, privilege or immunity granted by any contracting party to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other contracting parties.' (Article I.1).

‘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 the like domestic products.’ (Article III.2).

The English word ‘like’ has no perfect counterpart in French or Spanish. The French version of GATT speaks of ‘equivalent,’ which actually expresses something different again since it derives from ‘value’ rather than focusing, as the word ‘like’ does, on the inherent characteristics of a product. Consequently, ‘equivalent’ expresses more clearly the valuation of products, and of distinctions between products, by certain economic actors.

The drafters of the original GATT text (in practice those drafting the Havana Charter) were presumably well aware of the ambiguities of the term ‘like’ and of the inherent dangers in using such an ambiguous term in passages so critical to the text. They chose the word ‘like’ precisely because its ambiguities reflected a problem in the real world. Some products are equivalent but not like (for example, whisky and sake). Some products are like but not equivalent (for example, wild caught salmon and the rancher version). In the modern trading system, some products are identical but not alike (for example, genetic and branded pharmaceuticals). In short, the term ‘like’ requires careful interpretation to ensure that GATT does not produce unacceptable results.

Given its importance it is reasonable to expect extensive analysis of the concept of ‘like’ products in dispute-settlement proceedings of GATT and in the general literature. In fact, not much is to be found, presumably because the significance of the ambiguity appeared intuitively obvious and because, surprisingly, countries have rarely attempted to use criteria viewed as spurious by other countries to distinguish between otherwise like products.

The most important dispute to date revolving around interpretation of ‘like’ concerned liquor taxes in Japan. The dispute panel struggled hard with the problem, not least because the equivalence of sake and many liquors imported to Japan was intuitively obvious, but also because the protectionist intent of Japanese tax rules was hard to overlook. Even still, it was difficult to develop an argument that was free from internal contradictions and did not open the door to a Pandora’s box of other problems. The Appellate Body, reviewing the panel report on appeal, was seduced by the outlandish view that Article III.1 should be read as a chapeau to the entire Article III, possibly because a more obvious distinction between Article III.1 and III.2 seemed unpalatable since it opened the door wide to PPMs, including PPMs in other countries: that Article III.1 deals with production while Article III.2 addresses products in trade.

At the very least it should be clear that GATT contains no explicit prohibition on the use of PPMs in general. This view is the result of a process of interpretation, which sometimes resembles the rule-making committee of a club rather than that of an international body with global responsibilities. There is, however, a more direct way in which to approach

the issue of PPMs in the trading system. To prove that PPMs are possible within GATT, it is sufficient to show that they are currently being utilized.

### **Like products and intellectual property rights**

It may come as a surprise to some observers that in several areas GATT handles PPMs without apparent difficulty. The most dramatic application of PPMs in the GATT/WTO to date is in the field of intellectual property rights. The Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS Agreement) is in effect an agreement on PPMs. It distinguishes between products in trade, not based on their inherent characteristics, but on whether certain rules have been observed in the production process—namely, whether the rights of the holders of intellectual property have been respected.

A compact disc with a pirated version of music, a film or computer software is indistinguishable from a disc with the same (not 'like'!) materials: otherwise as often as not it would not function properly. A generic pharmaceutical product can be identical with its branded equivalent; sometimes it is legally required to be identical so as not to endanger the health of users. Indeed, some generic pharmaceuticals are manufactured on the same machines as their branded equivalents, yet they are clearly distinguished in the trade regime. The difference between PPMs arising from intellectual property rights and those needed for environmental purposes is that the former benefit the most powerful interests in the global economy while the latter appear to benefit nobody in particular, merely 'the environment.'

The economic effect of intellectual property rights (IPRs) is to assign a temporary monopoly to the holder of these rights. Most of these monopolies are of course worthless because there is no market demand for the vast majority of patents, manuscripts, recordings or software. When such demand exists, however, the profits can be staggering and many major multinational corporations derive a significant proportion of their income from IPRs, most dramatically companies like Microsoft, Philips or Toyota.

It is interesting to note that only one environmental dispute has arisen concerning the products of producers such as these: the dispute over CAFE standards and the gas-guzzler tax, which pitted Daimler-Benz and BMW against the U.S. automobile industry, one of the more unusual GATT disputes in terms of its outcome. The vast majority of environmental disputes in the GATT/WTO concern commodities; that is products, which are produced and traded to a non-proprietary standard: tuna, shrimp, forest products, fish, gasoline, soy beans, beef. The environmental concern for PPMs focuses primarily on the need to segment commodity markets in such a manner that the environmental impact of the extraction process becomes transparent to subsequent users—and the environmental costs can be successfully internalized. One way to test the free trade fervour of those who deny the possibility of introducing necessary environmental PPM distinctions is to suggest that all products currently being traded with IPR protection should be traded as commodities, that is to a single, universally accepted specification.

This brief discussion is not the occasion to discuss the role of commodity markets in pricing the environment or in promoting (or obstructing) the internalization of environmental costs in products traded on international markets. This is a matter requiring much more research and public debate than it has received to date.

### **Taking the debate forward**

Since 'like' products are at the heart of the GATT/WTO system, changing the definition of what will be recognized as valid distinctions between otherwise 'like' products is a matter of great concern to those responsible for managing the trading system. In particular, it raises the spectre of disguised forms of protectionism, precisely because it relates to the central principles of the regime designed to keep protectionists at bay. What worries many proponents of trade liberalization is the prospect of disguised forms of protection, which are particularly insidious when wedded to seemingly legitimate environmental goals, such as protecting dolphins, improving air quality, or strengthening the ecological management of forests—alliances which David Vogel has called baptist–bootlegger coalitions.

It is important for those concerned primarily with the environment to recognize the legitimacy of such fears. Indeed, the shrimp–turtle dispute is the only one where I am unaware of any significant commercial interest allied with the surface environmental concern. On the other hand, the existence of some protectionist effect of a measure must not in and of itself invalidate it. Sometimes the environmental need clearly outweighs the economic costs of protectionism.

It seems to me that it is in the interests of everyone concerned that we move beyond the absurd debate about PPMs, as if they were some form of original sin in the trade regime. We must seek a way to ensure that the use of environmental PPMs occurs in a rule-based manner. That, after all, is what the trading system is supposed to be about. So the correct question relative to environmental PPMs is not whether they are permissible but whether they are needed, and if they are needed what rules should apply.

The importance of PPMs for attaining sustainability has not yet been conclusively demonstrated. The significance of PPMs in this context is highly intuitive; nevertheless it resides on a critical notion related to the characteristics of commodity markets, namely that without certain PPMs producers of commodities will be confronted with an invidious choice: degrade the environment or lose market share.

This is a restatement of one of the most persistent of all ideas in the environment–trade debate, namely that rules are required to avoid the creation of 'pollution havens.' No clear evidence has yet been adduced to show that pollution havens exist. In part that is attributable to the fact that researchers have been asking the wrong question: Is there any risk of a general move of production from 'high-regulation' to 'low-regulation' jurisdictions. Enterprises with significant profit margins, in particular those benefiting from IPRs, will not make location decisions based on the cost of environmental protection. The reasons are complex, ranging

from the modest cost of environmental measures relative to other factors of production, to the importance of proximity to major markets, to the need to protect a brand's image. On the other hand some evidence suggests that the production of commodities, and to a lesser degree the production of certain commodity manufactures, has shifted away from high-regulation jurisdictions to those with lower regulation. The reasons are again complex, ranging from the availability of higher-value uses of scarce environmental resources in locations close to the value-added centres of the world, to the resistance of highly urbanized societies in Europe and Japan to further destruction of the landscape, and to the availability of cheap labour for labour-intensive phases of the product chain. With these few observations we are again in the relatively unexplored area of commodity production and the environment, which also happens to be the prime domain for environmental PPMs.

Interestingly, viewing the TRIPS Agreement for what it is—an agreement on the application of certain PPMs—provides some guidelines on how to address PPMs in the trading system. It is true that national environmental protection measures are the first step toward any international structure. It is also so obvious as to be trite that national measures alone cannot suffice. Consequently, the GATT/WTO needs an agreement on how to develop and apply environmental PPMs at all levels where they are needed: local, regional, national, international and global.

This is not a task for the GATT/WTO. Just as the TRIPS Agreement rests on a broad base of preparatory work undertaken by those whose concern is the development of IPRs, so an environmental PPMs Agreement must originate with those whose primary concern is the environment. They must specify what is needed, and how they plan to go about putting it in place. The role of GATT is then to insert such an agreement into the rule-based structure of the trading system in a manner that respects the needs of both those concerned with the environment and those whose focus is trade liberalization.

That sounds simple. It is not. But it is straightforward and may contribute to shortening a debate that seems to be going nowhere even while the underlying issues get more urgent with every environmentally related trade dispute.