D. Process and Production Methods

Products are not only defined by their physical properties, they end uses in a given market and consumers' tastes and habits. They may also be defined by way of how they are produced, i.e. on the basis of process and production methods (PPMs). The distinction is of importance in particular in relation to environmental and human or labour rights concerns. The question as to whether Article III of the GATT 1994 per se allows to differentiate between products that are physically similar but that are processed or produced differently is a highly controversial issue. In the case of PPMs, the 'like product' test does not focus on the products themselves but rather on the way they have been processed or produced. Therefore, an isolated comparison of the end-products might reveal any (physical) differences; it is the 'history' of the product that distinguishes it from other (physically similar) products. The PPM debate is equally relevant under the TBT Agreement (infra p. 762) and the Enabling Clause where tariff preferences are often granted to developing countries upon the fulfillment of certain conditionality (infra p. 562).

A very early GATT 1947 panel report, *Belgium Family Allowances*, is often interpreted, and cited as an important precedence, to the effect that discrimination on the basis of how (physically similar) products are produced or processed is prohibited under the GATT:

*Belgium Family Allowances (Allocations Familiales), Report of the Panel, adopted on 7 November 1952, BIRD 18/29 (1955)*

A Belgian law (the Royal Order of 19 December 1939) provided for levies on foreign goods purchased by public authorities when those goods originated in a country whose system of family allowances did not meet certain requirements. The proceeds of the levy, according to the law, "shall accrue to the National Compensation Fund with the view to compensating for the charge on domestic production resulting from this Act". Norway and Denmark requested the establishment of a panel, claiming a violation of Articles I and III of the GATT 1947.

After examining the legal provisions regarding the methods of collection of that charge, the Panel came to the conclusion that the 7.5 per cent levy was collected only on products purchased by public bodies for their own use and not as imports as such, and that the levy was charged, not at the time of importation, but when the purchase price was paid by the public body. In those circumstances, it would appear that the levy was to be treated as an "internal charge" within the meaning of paragraph 2 of Article III of the General Agreement, and not as an import charge within the meaning of paragraph 2 of Article II.

According to the provisions of paragraph 1 of Article I of the General Agreement, any advantage, favour, privilege or immunity granted by Belgium to any product originating in the territory of any country with respect to all matters referred to in paragraph 2 of Article III shall be granted immediately and unconditionally to the like product originating in the territories of all contracting parties. Belgium has granted exemption from the levy under consideration to products purchased by public bodies when they originate in Luxembourg and the Netherlands, as well as in France, Italy, Sweden and the United Kingdom. If the General Agreement were definitively in force in accordance with Article XXVI, it is clear that that exemption would have to be granted unconditionally to all other contracting parties (including Denmark and Norway). The consistency or otherwise of the system of family allowances in force in the territory of a given contracting party with the requirements of the Belgian law would be irrelevant in this respect, and the Belgian legislation would have to be amended insofar as it introduced a discrimination between countries having a given system of family allowances and those which had a different system, or no system at all, and made the granting of the exemption dependent on certain conditions.

The Panel wishes to stress that this undertaking to extend an exemption of an internal charge unconditionally is not qualified by any other provision of the Agreement. The Panel did not feel that the provisions of paragraph 8(a) of Article III were applicable in this case as the text of the paragraph referred only to laws, regulations and requirements and not to internal taxes or charges. As regards the exception contained in paragraph 2 of Article XVII, it would appear that it referred only to the principle set forth in paragraph 1 of that Article, i.e. the obligation to make purchases in accordance with commercial considerations and did not extend to matters dealt with in Article III.

The Panel then considered whether the fact that the General Agreement was applied only provisionally had a bearing on the Belgian obligations under Article I with regard to internal taxes. It recognized that the Interpretative Note to Article I allowed Belgium to observe those obligations "to the fullest extent not inconsistent with existing legislation", so long as Belgium was applying the Agreement pursuant to the Protocol of Provisional Application. The Belgian law on family allowances dated back to 1930, and the provisions now applicable were enacted in a Royal Decree of 19 December 1939, with the exception of the provision fixing the rate of the levy which was amended on 27 March 1951.

The Panel noted, however, that, in another case, the CONTRACTING PARTIES agreed that the Protocol of Provisional Application had to be construed so as to limit the operation of the provisions of paragraph 1(b) of the Protocol to those cases where "the legislation on which [the measure] is based is, by its tenor or expressed intent, of a mandatory character – that is, it imposes on the executive authorities requirements which cannot be modified by executive action".

The Panel, although recognizing that the relevant provisions of the Belgian royal decree appeared to be of a mandatory character, noted that, as pointed out by the Danish and the Norwegian representatives and admitted by the Belgian representative, it had been possible for the Belgian executive authorities to grant an exemption to a country whose system of family allowances did not meet fully the requirements of the law. Even if it might be difficult for the Belgian authorities to take similar action in similar cases, the panel did not feel that it had been proved to its satisfaction that the Belgian legislation fulfilled all the conditions laid down by the CONTRACTING PARTIES to justify an exception under the Protocol of Provisional Application.

The Panel felt that the legal issues involved in the complaint under consideration are such that it would be difficult for the CONTRACTING PARTIES to arrive at a very definite ruling. On the other hand, it was of the opinion that the Belgian legislation on family allowances was not only inconsistent with the provisions of Article I (and possibly with those of Article III, paragraph 2), but was based on a concept which was difficult to reconcile with the spirit of the General Agreement and that the CONTRACTING PARTIES should note with satisfaction the statements made at the Sixth and Seventh Sessions by the Belgian representatives and should recommend to the Belgian Government to expedite the consideration and the adoption of the necessary measures, consistent with the General Agreement, including a possible amendment of the Belgian legislation, to remove the discrimination complained of, and to refer to the CONTRACTING PARTIES not later than the first day of the Eighth Session.
In the (unadopted) GATT 1947 panel report *Tuna I*, the panel explicitly rejected to perceive as being different, for the purpose of determining “like-ness” pursuant to Article III of the GATT, products on the basis of their process or production methods. Instead, the panel expressed the view that Article III concerns domestic regulatory measures that apply to, and affect, the nature of products as such:


According to the U.S. Marine Mammal Protection Act (MMPA), tuna fishermen subject to U.S. jurisdiction must use certain fishing techniques to reduce the taking of dolphins incidental to the harvesting of fish. Furthermore, the act banned the importation of tuna (or products thereof) caught by fishermen of countries that could not prove to U.S. authorities that the average rate of dolphin incidentally taken by their tuna fleets was not in excess of 12.5% of that of U.S. ships. Additionally, U.S. authorities could also ban tuna imports from “whitish nations”, or they could ban imports of any other fish from non-complying nations or their intermediaries. After the provisions of this act had been applied to Mexico, that nation requested the establishment of a panel. The panel held, when elaborating on the categorisation of the import prohibition of certain tuna products as internal regulation (pursuant to Article III of the GATT) or as quantitative restrictions (pursuant to Article XII of the GATT), as follows:

5.10 The Panel noted that the United States had claimed that the direct import embargo on certain yellowfin tuna and certain yellowfin tuna products of Mexico constituted an embargo at the time or point of importation of the requirements of the MMPA that yellowfin tuna in the ETP be harvested with fishing techniques designed to reduce the incidental taking of dolphins. The MMPA did not regulate tuna products as such, and in particular did not regulate the sale of tuna or tuna products. Nor did it prescribe fishing techniques that could have an effect on tuna as a product. This raised in the Panel’s view the question of whether the tuna harvesting regulations could be regarded as a measure that “applies to” imported and domestic tuna within the meaning of the Note Ad Article III and consequently as a measure which the United States could enforce consistently with that Note in the case of imported tuna at the time or point of importation. The Panel examined this question in detail and found the following.

5.11 The text of Article III:1 refers to the application to imported or domestic products of “laws, regulations and requirements affecting the internal sale … of products” and “internal quantitative regulations requiring the mixture, processing or use of products”; it sets forth the principle that such regulations on products not be applied so as to afford protection to domestic production. Article III:4 refers solely to laws, regulations and requirements affecting the internal sale, etc. of products. This suggests that Article III covers only measures affecting products as such. Furthermore, the text of the Note Ad Article III refers to a measure “which applies to an imported product and the like domestic product and is collected or enforced in the case of the imported product at the time or point of importation”. This suggests that this Note covers only measures applied to imported products that are of the same nature as those applied to the domestic products, such as prohibitions on importation or on sale, processing, transportation, distribution or use of products, and that this standard has to be understood as applicable to each individual case of imported products. It was apparent to the Panel that the comparison implied was necessarily one between the measures applied to imported products and the measures applied to like domestic products.

5.12 A previous panel had found that Article III:2, first sentence, “obliges contracting parties to establish certain competitive conditions for imported products in relation to domestic products”. Another panel had found that the words “treatment no less favourable” in Article III:4 call for effective equality of opportunities for imported products in respect of the application of laws, regulations or requirements affecting the sale, offering for sale, purchase, transportation, distribution or use of products, and that this standard has to be understood as applicable to each individual case of imported products. It was apparent to the Panel that the comparison implied was necessarily one between the measures applied to imported products and the measures applied to like domestic products.

5.13 The Panel considered that, as Article III applied the national treatment principle to both regulations and internal taxes, the provisions of Article III:4 applicable to regulations should be interpreted taking into account interpretations by the CONTRACTING PARTIES of the provisions of Article III:2 applicable to taxes. The Panel noted in this context that the Working Party Report on Border Tax Adjustments, adopted by the CONTRACTING PARTIES in 1970, had concluded that

“... there was convergence of views to the effect that taxes directly levied on products were eligible for tax adjustment ... Furthermore, the Working Party concluded that there was convergence of views to the effect that certain taxes that were not directly levied on products were not eligible for adjustment, (such as) social security charges when on employers or employees and payroll taxes.”

Thus, under the national treatment principle of Article III, contracting parties may apply border tax adjustments with regard to those taxes that are borne by products, but not for domestic taxes that are not directly levied on products (such as corporate income taxes). Consequently, the Note Ad Article III covers only internal taxes that are borne by products. The Panel considered that it would be inconsistent to limit the application of this Note to taxes that are borne by products while permitting its application to regulations not applied to the product as such.

5.14 The Panel concluded from the above considerations that the Note Ad Article III covers only those measures that are applied to the product as such. The Panel noted that the MMPA regulates the domestic harvesting of yellowfin tuna to reduce the incidental taking of dolphin, but that these regulations could not be regarded as being applied to tuna products as such because they would not directly regulate the sale of tuna and could not possibly affect tuna as a product. Therefore, the Panel found that the import prohibition on certain yellowfin tuna and certain yellowfin tuna products of Mexico and the provisions of the MMPA under which it is imposed did not constitute internal regulations covered by the Note Ad Article III.

5.13 The Panel further concluded that, even if the provisions of the MMPA enforcing the tuna harvesting regulations (in particular those providing for the seizure of cargo as a penalty for violation of the Act) were regarded as regulating the sale of tuna as a product, the United States import prohibition would not meet the requirements of Article III. As pointed out in paragraph 5.12 above, Article III:4 calls for a comparison of the treatment of imported tuna as a product with that of domestic tuna as a product. Regulations governing the taking of dolphins incidental to the taking of tuna could not possibly affect tuna as a product, Article III:4 therefore obliges the United States to accord treatment to Mexican tuna no less favourable than that accorded to United States tuna, whether or not the incidental taking of dolphins by Mexican vessels corresponds to that of United States vessels.

The following authors challenge the approach developed by the panel in this report and argue that two products may well be considered “unlike” due to process-based differences in the pursuit of legitimate non-trade concerns:

The undrafted panel reports in Tuna/Dolphin I and II claimed that process measures were simply not covered by Article III (and were therefore required, in those cases, to Article XIV). It is perhaps worth remembering that the measures in those cases were country-based, but the panel’s arguments, if valid, would apply to origin-neutral measures as well.

The Tuna/Dolphin /panel’s argument is by no means clear, since the panel introduces without definition the notion of measures ‘affecting products as such’ and the notion of how a measure affects a product ‘as a product’. Still, the main line seems to go as follows. The panel makes much of the fact that various sections of Article III refer to laws and regulations that affect the sale, purchase, transportation, and so on, of ‘products’. This, it says, ‘suggests that Article III covers only measures affecting products as such’ (para. 5.11). The panel then implies that process-based measures do not ‘affect products as such’ or ‘affect the product as a product’, suggesting the following three reasons: (1) ‘products as such’ are defined by their physical constitution, and process-based measures affect differently products that have exactly the same physical constitution; and/or (2) regulation of the production process just is not regulation of products; and/or (3) the process-based measures do not affect the ultimate physical constitution of the product. It follows that Article III(4) does not cover process-based measures. (The panel does not focus on the issue of ‘like products’ which we will discuss below, presumably because that leads to an argument about the substance of Article III, not the coverage.)

Despite the panel, it should be obvious that the repeated reference to ‘products’ tells us nothing about the product/process distinction. It merely reflects the fact that GATT is about trade in goods, not about trade in services or the movement of capital or labour. We could show in detail that none of the panel’s three sub-arguments actually applies the text (as opposed to improving on one of its key terms), but a detailed treatment is unnecessary. The panel’s larger argument falls under its own weight if we simply compare the conclusion to the text and the argument purports to analyse. The text of Article III(4) says it applies to ‘internal laws, regulations and requirements affecting the international sale... of products’. Who could doubt that, giving terms their ordinary meaning, process-based measures ‘affect the sale of products’? This is true even of the ban on the use of dolphin-speed fishing techniques by United States fishermen (the panel’s prime example of a regulation not affecting tuna as a product), since the ban almost certainly affects the price and quantity of tuna sold. But more important, the whole complaint about the United States’ regime is that it affects the sale of products by reducing the sales of foreign tuna.

It might be objected that our ordinary language reading of ‘affecting the... sale’ is so broad that the text’s further references to ‘offering for sale, purchase, transportation, distribution, or use’ redundant. There is something in this. But the only way to avoid the redundancy would be to read ‘affecting’ so that it means ‘having its immediate regulatory impact on the precise activity of...’, and this reading, in conjunction with the text’s list of activities, would exclude from the coverage of the Article regulations about possession, storage, advertising, registration, post-purchase products liability, and so on. This is a case where one just has to admit that there is redundancy in the text of the Article. Overlap of similar terms in a series (which are often proliferated just to ensure complete coverage) is not at all the same thing as a pointless sentence or an inutile section.

The root of the problem lies in the claim that physically identical products that differ only in their processing histories are ‘like’ products. The opponent of process measures thinks this follows from the ordinary meaning of ‘like’. We disagree. ‘Likeness’ in this context is not pri-
would require focus on the characteristics of a product, instead of the process of producing the product. See, for example, the Belgian Family Allowances case (...) It is a very interesting case that bears upon this problem.

(...) The discussion by Howse and Regan about the product/process distinction generally misses the real issues that the trade policy institutions are forced to address. Sands and Jansen raise some of those issues. With respect to the product/process problem, the issue is not so much whether this distinction can be justified in all contexts (the authors rightly say that it cannot), but rather how to develop some constraints on the potential misuse of process-oriented trade barriers (i.e., the ‘slippery slope’). The real question is: If one abandons the product/process distinction or otherwise opens up the possibility of trade-creating measures tied to process of production, how does one draw an appropriate line to prevent abuse?

Jansen considers that the product/process distinction is worthwhile, even if it is somewhat artificial. It can prevent more harm than its demise might introduce as good. The harms could be pointed out by a series of hypothetical about how the term ‘process’ could be misused in dozens—even hundreds—of particular situations, to inhibit and depress international trade. These are issues that governments face all the time and that lawyers are paid to struggle with—namely, to get some kind of a rule or norm that is not only justifiable, but can, in fact, be administered in the institutional and factual context that it addresses. Some of the arguments or line-drawing processes in the Department of Commerce may seem a bit too simplistic, but a rule cannot be made viable in that context if only people with Ph.D.s can administer it. The procedure must enable ordinary people to come to grips with some of these issues. That is part of the problem here.

The debate on PPMs is closely related to the systemic value and relevance of the exceptions provided for in Article XX of the GATT 1944 and to the issue of extraterritorial application of trade-related measures by WTO members (see infra p. 462; see for PPMs in the context of the government procurement infra p. 1042). Overall, we note that the matter goes beyond interpreting Article III of the GATT 1994. With regard to developing countries, which potentially are mostly affected by process-based measures, the matter additionally needs to be placed in the broader context of technology transfer and financial support in bringing about state-of-the-art production methods.

**Further Reading (Process and Production Methods)**


E. State Trading Enterprises and Monopolies

The relevant rules governing non-discrimination between foreign and domestic products and producers typically lay down the legal framework within which private operators participate in competitive markets. They address regulations that member states impose on products and producers in the pursuit of a plurality of policy goals. However, these rules are not effective when the government itself acts as a trader or grants exclusive monopoly rights that other competitors do not enjoy. Both variants of state trading imply discriminations and market distortions. They need to be specifically addressed. It is important to stress that state trading has not been limited to planned economies. It still looms large in market and mixed economies where significant monopolies in goods and particularly in services are operated. The process of liberalizing such monopolies has in recent years raised new and complex issues. Moreover, we note by way of introduction that state trading must be distinguished from government procurement, i.e. the acquisition of goods and services by governmental agencies on the market. This topic will be dealt with infra (p. 1036).

The relevant provision in the GATT/WTO legal framework is Article XVII of the GATT 1944. Basically, it provides for a notification obligation and regulates the activities of state trading enterprises in substantive terms. Paragraph 1(a) stipulates that members shall act in a manner consistent with the general principles of non-discriminatory treatment of the GATT when governmental measures affect imports or exports of private traders. However, the exact confines of this provision are subject to controversy. The following texts give an overview of the use of state trading enterprises and comment on the necessity to specifically address them in Article XVII of the GATT 1994:


1. THE USE AND IMPORTANCE OF STATE TRADING ENTERPRISES

Governments make use of state trading enterprises for a variety of reasons. The WTO Secretariat’s background paper on “Operations of State Trading Enterprises as They Relate to International Trade” sub-divides state trading enterprises into several major categories: marketing boards; fiscal monopolies; channelizing agencies; foreign trade enterprises; and nationalized industries. A study of notifications to GATT revealed that most state trading enterprises are in the agricultural sector, where such enterprises are used to achieve a variety of agricultural-related policy objectives. In addition, state trading enterprises are found in industrial sectors. In the past, such enterprises have been particularly important in developing economies and in centrally planned, non-market economies.