TESTIMONY OF
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BEFORE THE
UNITED STATES SENATE COMMITTEE ON FINANCE
FEBRUARY 14, 2008

Good morning, Chairman Baucus, Senator Grassley, and Members of the Committee. My name is Abraham Breehey and I serve as the Assistant Director of Government Affairs for the International Brotherhood of Boilermakers, Iron Ship Builders, Blacksmiths, Forgers and Helpers. The Boilermakers Union represents workers in the manufacturing and construction sectors. On behalf of our members, I greatly appreciate the opportunity to express our views on this important topic.

Our union and others in the labor movement have longstanding concerns about the impact of policies designed to reduce our nation's greenhouse gas emissions on the competitiveness of our economy and workers, particularly those whose work relates to the manufacturing of energy-intensive products. However, we are committed to finding a solution that protects American workers while allowing the United States to demonstrate much needed global leadership on this pressing environmental challenge.

In 1997, the delegates to the Twenty-Second Convention of the AFL-CIO affirmed very clear objectives on the issue of climate change. They included assuring environmental repair of the carbon dioxide concentration problem with the formal participation of the entire international community committed to a mutually agreed upon, binding solution; protecting the industrial base of the United States with no movement of jobs or pollution to other countries because of perverse incentives resulting from a flawed

international agreement; and providing a just transition so that no American worker loses economic ground in our pursuit of more sustainable global practices.

A decade later, our goals remain the same. However, climate science makes it increasingly clear that we delay reducing greenhouse gas emissions at our own peril. Our union believes there are potentially effective ways to ensure that carbon mitigation policies do not place American workers at a further disadvantage in the global economy, while maintaining leverage on major emitters in the developing world to join us. At the very least, we must ensure that their delay does not undermine our efforts.

Congress should seek to make certain that necessary and environmentally responsible action on the issue of climate change is not yet another reason why domestic industries relocate their production off-shore, as so many have already in search of low-wage workers. It serves neither the goals of the labor movement, nor the environment goal of reducing greenhouse gas emissions, if the American industrial base and the emissions that result from industrial processes shifts to nations that have resisted carbon restrictions. Domestic reduction efforts should be coupled with a global strategy.

Effective climate change polices by the United States must recognize that we cannot solve this problem alone. According to the International Energy Agency, global CO_2 emissions related to energy production will increase by 57% from 2005-2030. Developing countries will account for more than 75% of this increase. China's CO_2 emissions are the fastest growing in the world and they have surpassed the United States as the leading annual emitter. Including provisions in a domestic greenhouse gas reduction policy that encourage major trading partners in the developing world to join us in a global agreement or internalize the cost of greenhouse gas emissions in their exports to the U.S. makes both environmental and economic sense.

While there are other well-intentioned proposals to address the issue of competitiveness, we believe the proposal of the International Brotherhood of Electrical Workers and American Electric Power that was incorporated into the legislation

introduced by Senators Bingaman and Specter, and Senators Lieberman and Warner is the best approach. To be clear, we have a few remaining concerns about the provisions as currently included in S. 2191 and S. 1766, and I will offer some suggestions for improving them later in my testimony. However, these provisions form the framework for a sound and effective policy.

The international provisions of S. 2191 and S. 1766 seek to avoid the negative trade impacts of a domestic cap-and-trade program by requiring importers of bulk energy intensive primary goods to purchase "allowances" to cover the emissions associated with their production. Failure to do so would disqualify the entry of these products from import into the United States.

It is appropriate in terms of establishing a level playing field for American producers and within our rights under the World Trade Organization (WTO) to apply this requirement on certain covered imports – including iron, steel, aluminum, cement, glass, and paper – from a country that has not taken comparable action. The international reserve allowance requirement would correspond to the greenhouse gases emitted when the imported goods were produced in the country of origin, with an adjustment ratio to account for allowances allocated at no cost to domestic producers. The price of international reserve allowances would be pegged to the price for domestic allowances, assuring the close association between the cost of compliance for both foreign and domestic producers. While I am not an expert on trade law, I have attached to my testimony a detailed analysis supporting the conclusion that such a requirement is fully in compliance with the requirements of the WTO (Appendix A).

As proposed in the Lieberman-Warner Climate Security Act and the Bingaman-Specter Low Carbon Economy Act, the United States would commence good faith efforts to negotiate with all major greenhouse gas emitters – consistent with our obligations under the WTO – immediately following enactment of domestic cap-and-trade legislation. Upon the implementation of the U.S. cap-and-trade program, the Administration would begin an interagency review process to determine which, if any,

major emitters have failed to take comparable steps. This determination requires the President to quantify the annual emissions reductions achieved by the United States under the domestic program, and compare those reductions to emissions from other major emitters. This process is based on results, not the policy design a particular country may choose to implement. Following that determination, energy-intensive primary goods imported into the United States from a major emitting nation that has not taken comparable action would be required to account for the "carbon footprint" of those imports through the purchase of international reserve allowances or an allowance distributed by another foreign country pursuant to a cap-and-trade program that represents comparable action.

While this requirement would apply to imports from the nations in the developing world that have not taken comparable action, the provisions are focused only on those that contribute substantially to global emissions and are not intended to hinder development in the world's poorest countries. Least developed nations and those whose greenhouse gas emissions are below a *de minimis* percentage of global emissions would not be bound by this requirement.

Our union believes there are two primary reasons the "international reserve allowance" requirement is the best mechanism to avoid negative impacts on the U.S. competitiveness. First, it could potentially provide valuable leverage to U.S. climate negotiators in their efforts to establish a global framework that includes other major emitting nations. We are hopeful that when our major trading partners know that the price of their exports headed for U.S. shores would be adjusted by the cost of its carbon content, they would recognize that there are no benefits to be gained from further delay. In fact, if utilized effectively by climate negotiators, these provisions might never take effect. Indeed, it is our hope that a global framework is reached that includes all the major emitters in the developing world and these provisions are never triggered. As pressure mounts for truly global action on climate change, including commitments from the fastest growing nations in the developing world, the leverage provided by the international reserve allowance requirement increases.

Second, and no less importantly, this requirement is consistent with the environmental goals of domestic climate action. We agree with the statement included in the Stern Review that climate change "is the greatest and widest-ranging market failure ever seen." The international reserve allowance requirement helps address this market failure in the context of a global economy without weakening or short-circuiting domestic efforts. It is time to account for the significant negative externality of carbon emissions in both domestic and foreign products. International reserve allowances are separate from those allocated under the domestic program. The use of such allowances will not increase the U.S. emissions cap or undermine our own environmental goals and they can only be used for meeting the requirements that would apply to imported covered energy-intensive goods.

However, we believe the timely application of an international requirement is essential to its effectiveness. As drafted, the provisions of S. 2191 require importers of greenhouse gas intensive goods to hold and submit allowances starting in 2020, while domestic regulations would take effect in 2012. American workers and firms cannot afford to wait eight years for the playing field to be leveled. We believe this mechanism can and must be triggered soon after the implementation of a domestic cap-and-trade program. We believe the requirement should be triggered no later than 2015, if not sooner, recognizing the need for an interagency review process, and a determination on whether nations are taking action comparable to the United States.

In addition, we believe Congress should clarify what exactly constitutes "comparable action" on the part of other major emitters. We recognize the differentiated responsibilities and respective capabilities of developing countries to reduce their carbon emissions, while pursuing necessary economic development and alleviating poverty. However, "comparable action" must mean more than token gestures or statements of good faith. Efforts undertaken by major emitters in the developing world must be real, measurable, and verifiable in order to be considered comparable.

We believe that the international provisions included in the Lieberman-Warner and Bingaman-Specter bills serve the interests of American workers, but also reflect the political reality confronting efforts to enact comprehensive, mandatory climate change legislation. As you know, in 1997, the Senate unanimously voted against unilateral U.S. action to cap domestic emissions when it adopted the Byrd-Hagel resolution. That resolution stated that no treaty mandating greenhouse gas reduction commitments should be ratified unless it required developing countries to reduce their emissions within the same time frame. The labor movement strongly supported this resolution. However, like so many Members of the Senate, we recognize that the longer we wait to act, the more difficult – and expensive – that action will be. The importance of effective provisions to encourage action from China, India, and other fast developing countries can not be understated. The Boilermakers Union believes that imposing an allowance requirement on energy intensive imports is the best mechanism for achieving the policy objectives reflected in the Byrd-Hagel resolution.

Thank you very much for your consideration of my views on this matter. I look forward to answering any questions you might have.

APPENDIX A

WTO Analysis of International Provisions of U.S. Climate Change Legislation

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JANUARY 25, 2008

WTO Analysis of International Provisions of U.S. Climate Change Legislation

The United States Congress is contemplating legislation that would impose a mandatory cap-and-trade program for U.S. greenhouse gas (GHG) emissions. This legislation must also provide leverage to ensure that emissions in other countries, particularly rapidly developing countries such as China or India, do not undermine these efforts to protect the environment. To provide effective leverage, the U.S. legislation must be compliant with the Agreement Establishing the World Trade Organization (WTO). To that end, the International Brotherhood of Electrical Workers (IBEW) and American Electric Power (AEP) have proposed that the United States impose an allowance requirement on imports of carbon-intensive goods from countries that fail to take action on GHG emissions comparable to that of the United States.[1] Counsel for AEP has prepared the following legal analysis on the WTO-consistency of such a requirement.

I. Summary

Where governments take action to address environmental protection, WTO law favors doing so through consensual and multilateral procedures, rather than unilateral trade measures. However:

- if the United States made **good faith efforts** to negotiate with **all** nations on a non-discriminatory basis but was unable to reach agreement on procedures to reduce greenhouse gas emissions, then
- the United States could **require imports** of goods to be accompanied (electronically) by emissions **allowances**,
- in the context of a broader requirement that **domestic producers** have emission allowances.

[1] A summary of the IBEW-AEP proposal is attached.

Analyzing the WTO-consistency of an allowance requirement on imports is a two-step process: (1) is the requirement, as a measure, **consistent** with the relevant obligations of the WTO, and if not; (2) is it covered by a WTO **exception**?

One could argue that an allowance requirement on imports should be considered as part of the overall U.S. cap-and-trade program. As such, it would be consistent with the WTO national treatment obligation set forth in GATT Article III:4, because it would be administered to accord imported goods treatment no less favorable than the treatment accorded "like" domestic goods. If the allowance requirement on imports were not considered as part of domestic regulation, then it would be governed by the obligations set forth in GATT Article XI or II regarding border measures. Even if the measure were not consistent with applicable WTO obligations, however, the allowance requirement would be covered by the WTO exception set forth in GATT Article XX(g) for measures relating to the conservation of exhaustible natural resources or the exception set forth in GATT Article XX(b) for measures relating to the protection of human, animal or plant life or health. The allowance requirement, under which allowances submitted with imports would be retired from further use, just as allowances assigned to domestic production would be, is closely related to the conservation objective of the overall climate change program. It is also an important part of a comprehensive regulatory scheme that is apt to cause substantial benefits to health and life.

The relevant WTO provisions are included in an Appendix attached to this memorandum, and the following chart illustrates the results of the WTO analysis:

WTO ANALYSIS	**ALLOWANCE REQUIREMENT ON IMPORTS**
1. Is measure consistent with WTO obligations?	
(a) Issue	**Either** it is considered as a border measure . . .
- Applicable provisions	GATT Articles II or XI
- Outcome	Not WTO-consistent if the measure imposes charges in excess of scheduled duties or border restrictions.
(b) Issue	. . . **or** it is judged as part of internal regulation
- Applicable provision	GATT Article III
- Outcome	WTO consistent if judged in the context of overall domestic regulation, affords national treatment, *i.e.*, treatment to imported goods no less favorable than that accorded to "like" domestic goods
2. If the measures is not WTO consistent, then is measure covered by a WTO exception?	
(a) Issue	**Either** measure relates to the conservation of exhaustible natural resources . . .

- Applicable provision	GATT Article XX(g)
- Outcome	Yes, it is closely related to the objective of conservation
(b) Issue	**Or** measure is necessary to the protection of human, animal or plant life or health . . .
- Applicable provision	GATT Article XX(b)
- Outcome	Yes, even though in the short term it may be difficult to isolate the contribution of a single measure to reducing climate change, it is part of a comprehensive regulatory scheme that is apt to induce sustainable change.
(c) Issue	**And** the measure applied in a manner that does not arbitrarily or unjustifiably discriminate between countries where the same conditions prevail, or is not a disguised restriction on trade.
- Applicable provision	Article XX chapeau
- Outcome	Yes, focusing on top emitting countries, and only those that had not addressed GHG emissions, would be justified because of clear link to GHG emission reduction goals; the measure is flexible and not "capricious" or "random" and the rationale for discrimination relates to the policy objective.
3. Result?	**YES, MEASURE IS PERMISSIBLE UNDER WTO RULES**

II. Description of Measure

The domestic context for GHG-related trade measures would be a **cap-and-trade program** under which the U.S. Government would determine a **quantitative cap** for GHG emissions, and establish quantitative **emission allowances,** the sum of which would equal the U.S. GHG emissions cap. This system would be modeled on the EPA's existing U.S. cap-and-trade program in its Acid Rain Program,[2] with some differences. The government would issue electronic allowance certificates (each with a unique serial number for tracking and safeguards against counterfeiting) to show the amount of GHG emissions allowed. The certificates could then be transferred or sold in an **allowances market**. A firm emitting more GHGs than its existing allowances would permit would need to procure additional allowances or would be penalized for exceeding its allowances. All firms generating GHGs would have to continually monitor and report their emissions.

A domestic cap-and-trade program, implemented without measures to address GHG emissions from outside the United States, would be ineffectual in addressing the full range of GHG emissions affecting the environment. An allowance requirement imposed on imports would help to secure the environmental benefits of the overall program.

[2] Described at http://pubweb.epa.gov/air/clearskies/captrade.html, last visited January 25, 2008.

Under the IBEW-AEP proposal, the U.S. Government would **negotiate** with GHG emitting countries to secure internationally agreed disciplines on GHG emissions. After U.S. implementing regulations were promulgated, the U.S. Government would begin to measure on an annual basis the reduction of GHG emissions in sectors under the U.S. cap and use those data to determine whether and to what extent key sectors in other countries had taken comparable action. The determination would be based, therefore, on the impact on GHG emissions rather than the precise form of the regulatory program used to achieve those effects. The U.S. Government would focus its determination on those countries that contribute most to global GHG emissions – least developed countries and countries with less than a *de minimis* volume of GHG emissions would be excluded.

If the U.S. Government determined that a country did not take comparable action, then an importer of certain goods from that country would be required to provide allowances to the U.S. Government corresponding to the GHGs emitted when the imported goods were produced in the country of origin. The U.S. Government would use an **adjustment factor** in setting the number of allowances required for imported goods. This adjustment factor would reflect the portion of allowances that domestic producers receive at no cost in relation to the allowances that domestic producers procure by auction. The adjustment factor would also reflect the conditions prevailing in different countries.

Which imported goods would be subject to the requirement? The scope of imported goods subject to the allowances requirement could be set to match as nearly as possible the scope of the domestic requirement. Thus, if the requirement were to apply only to the production of **carbon-intensive goods**, or only to "upstream" rather than "downstream" products, then the scope of imports covered by the requirement could be set accordingly. This contributes to ensuring non-discriminatory treatment of imports.

What would be the source of these certificates? Under one approach, importers would secure allowances from the normal supply of allowances made available for U.S. entities to satisfy their obligations under the U.S. cap-and-trade system. Thus, importers could obtain U.S. emissions allowances from the producer/exporter or brokers operating generally in the marketplace. Alternatively, the U.S. Government could establish a separate (unlimited) supply of allowances that would only be used by importers. Finally, the U.S. Government could **permit importers to satisfy their obligations using allowances (and credits) generated under the cap-and-trade systems of other countries**. The Bingaman-Specter and Lieberman-Warner bills combine the last two approaches.

III. Is the Measure Compliant with U.S. International Obligations?

In order to effectively persuade major newly industrializing economies to participate in GHG reduction, U.S. legislation must be permissible under WTO rules.[3] Two key principles of WTO law are germane to assessing the WTO legality of measures that could be used as part of a cap-and-trade program:

- each WTO Member government must obey its market access commitments on import tariffs, and cannot otherwise block imports (GATT Articles II, XI);

- it also may not use its domestic taxes, or **any** domestic regulations, so as to discriminate in favor of domestic goods compared to like imported products, or in favor of imported goods from one foreign country rather than another (GATT Articles I, III).

In accordance with these principles, the legal status of a measure under the GATT may be different depending on whether it is a border measure or whether it is an internal measure enforced at the border. GATT Article II:1(b) prohibits new import charges, and Article XI:1 prohibits bans or quantitative restrictions on imports. A measure that comes under either GATT article would likely be WTO-inconsistent. However, under GATT Article III, a WTO Member is entitled to regulate all products that are sold in its market provided that internal regulation does not afford protection to domestic over imported goods.

Thus, notwithstanding the prohibitions embedded in Articles XI:1 and II:1(b), a restrictive internal regulation (such as a residue limitation or product ban) or a prohibitive internal excise tax can be enforced on imports at the border, and be judged under GATT Article III, rather than Articles XI or II. In other words, the border-enforced internal measure would be completely GATT-consistent as long as it is non-discriminatory. The Note to Article III shows how the GATT draws the line between border measures and border-enforced internal measures. The Note identifies two issues that must be considered: does the tax, charge or regulatory requirement apply **both** to an imported product and to the like domestic product, and is it collected or enforced "at the time or point of importation"? The stated policy purpose of a measure is not relevant, nor is its categorization by domestic law.[4]

The following analysis examines whether the allowance requirement on imports is consistent with the WTO market access commitments and non-discrimination obligations for trade in goods. GATT law considers the regulation of imported goods either as a border measure, or as part of an overall program of internal regulation, but not both. There are good arguments that the allowance requirement is best understood as part of internal regulation, but it is a very close question. We review both sets of arguments below.

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[3] We focus here only on WTO rules, as the WTO Agreement is the only agreement that binds both the United States and major countries of concern to Congress. Other U.S. treaties would also apply to climate change legislation, but the basic principles would not differ.

[4] *EC – Regulation on Imports of Parts and Components*, GATT BISD 35S/37 (1990), paras. 5.6-5.7.

A. Consistency with WTO Market Access Commitments

To simplify this analysis, we consider an allowance requirement as it applies to a hypothetical ton of steel produced and exported from Country X and a "like" ton of steel (*i.e.*, same physical characteristics and uses) produced in the United States. Of course, actual trading patterns may be more complex, involving multi-stage processing across borders, and some imported products are not produced in the United States.

As stated above, Articles II:1(b) and XI:1 are the GATT provisions that are relevant in assessing whether an allowance requirement on imports is a border measure, and as such, whether it is consistent with the WTO **market access** commitments of the United States. First, GATT Article II:1(b) prohibits the imposition of any new extra charges or surcharges on products that are subject to tariff concessions—and close to 100 percent of U.S. imports are now under such concessions. If the allowance requirement program mandated that only importers—as opposed to importers and domestic producers—buy allowance certificates or pay an extra charge, it would constitute a new border charge, and as such, it would violate GATT Article II:1(b). Second, GATT Article XI:1 prohibits any border measure restricting imports other than duties, taxes or other charges. By requiring that importers present allowance certificates as a condition for importation, the allowance requirement program could cause a decrease in the volume of imports. As a result, the program would constitute a border measure that imposes a quantitative limitation on imports in violation of GATT Article XI:1.

If the allowance requirement on imports is a border measure under either GATT Article II or Article XI, it will not be consistent with the WTO market access commitments of the United States. To have a chance of surviving WTO scrutiny at this first level of analysis, the allowance requirement must be justifiable as an internal measure that falls in line with the WTO non-discrimination obligations of the United States.

B. Consistency with WTO Non-Discrimination Obligations

GATT Article III is the most important provision, for the purposes of this analysis, embodying the non-discrimination principle of the WTO.

In contrast to the interpretation described above, the United States could argue that the allowances requirement should be considered an internal regulation subject to the national treatment obligation set forth in GATT Article III:4. To ensure compliance with Article III:4, the United States could adjust the scope of imported goods covered by the allowances requirement, and the number of allowances required to be submitted for particular imported goods. A WTO dispute settlement panel might point out, however, that the allowances program is a regulation on U.S. **producers**, whereas, the allowances requirement on imports is a regulation on imported **products**. On that basis, the Note to Article III might rule out classifying the allowances requirement on imports as an internal regulation subject to Article III.[5] But the United States could

[5] The distinction between a regulation of U.S. *producers* and a regulation of imported *products* is based on the product-process doctrine. Under the doctrine, the line is not drawn between regulations of

respond that the scope of Article III has been interpreted more flexibly than a hard-and-fast, line-drawing exercise would permit. For example, a measure, such as this one, regulating whether and how products, including domestic products, can be sold constitutes an internal regulation for purposes of Article III.

As an internal regulation, the allowance requirement on imports would be subject to GATT Article III:4, under which the United States must accord to imported products "treatment no less favourable 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." A note to Article III provides that "[a]ny internal tax or other internal charge, or any law, regulation or requirement . . . which applies to an imported product and to the like domestic product and is collected or enforced in the case of the imported product at the time or point of importation, is nevertheless to be regarded as an internal tax or other internal charge, or a law, regulation or requirement . . . and is accordingly subject to the provisions of Article III."[6] When an internal tax (such as VAT or an excise tax) is collected on imports at the border, that is called a *border tax adjustment*.

These provisions mean that if the U.S. imposes a regulation (such as the EPA's rules on gasoline composition under the Clean Air Act), the regulation must treat imported products no less favorably than like U.S. products. The internal U.S. measure can be enforced on imports at the border, but it must not discriminate against imports. In determining whether a measure discriminates against imports, WTO panels look to its effect on the conditions of competition between the domestic product and imported like products.[7]

Finally, there are two more non-discrimination requirements in the GATT that would be relevant. The most-favored nation (MFN) clause in GATT Article I:1 prohibits discrimination between foreign sources of supply. The MFN clause applies to border charges of any kind, to internal taxes or regulations, and to border enforcement of internal taxes or regulations. Under Article I:1, whenever a WTO Member grants an advantage, favor, privilege or immunity to a product from any country, it must accord that advantage, favor, privilege or immunity to the like product of any WTO Member. In addition, GATT Article XIII requires non-discriminatory application of any quantitative restrictions on imports.

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products on the one hand and regulations of producers and production processes on the other. Rather, it is drawn between regulations of products and regulations of producers and production processes that affect characteristics of the product on the one hand, and regulations of producers and production processes that do **not** affect characteristics of a product on the other. See Robert Hudec, *The Product-Process Doctrine in GATT/WTO Jurisprudence* in M. Bronckers and R. Quick, *eds.*, NEW DIRECTIONS IN INTERNATIONAL ECONOMIC LAW,187, 191-92.

[6] GATT, Note *Ad* Article III. The "*Ad* Notes" to the GATT have coequal status with the main GATT text.

[7] The focus on "conditions of competition" is a consistent theme in cases applying GATT Article III since 1957; as one example, *see Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef* ("*Korea – Beef*"), WT/DS161/AB/R, WT/DS169/AB/R, 11 December 2000, at para. 135, finding that treatment no less favorable under Article III "means…according *conditions of competition* no less favourable to the imported product than to the like domestic product."

If all imported steel from any foreign country were equally subject to the allowances program and received equal treatment, then the measure would be consistent with Article I:1. If an imported ton of steel from Country X were subject to the allowances measure but a "like" ton of steel from Country Y were not (for example because Country Y has a different set of arrangements with the U.S. to meet the objectives of GHG emission reduction), then it would raise questions under GATT Article I:1. However, the United States could argue that, under GATT Article I:1, it is entitled to impose conditions on the importation of products, provided that those conditions apply in the same way to imported products from all sources.[8] The United States could exclude from the allowance requirement of imports from WTO Members whose GHG emissions are below a *de minimis* threshold, which would capture most of the WTO Members that are considered by the United Nations to be least-developed countries.[9] With respect to the largest GHG emitting countries, the United States might point out that the climate change-related objective is the same, but the treatment of Country X and Country Y steel differs because the objective is being met in different ways. The Appellate Body might consider this argument under GATT Article I:1, just as it has in cases applying GATT Article III:4.[10] However, this would be a novel argument in relation to Article I:1, and textual differences between Articles I and III would need to be taken into account in applying this argument to Article I.

IV. Applicability of WTO Exceptions

This portion of the analysis focuses on whether any of the general WTO exceptions for trade in goods would permit the United States to maintain the allowance requirement on imports.

Even if a government measure would ordinarily conflict with the market access and non-discrimination provisions of the GATT, the violation may be excused by one of the ten special policy-based exceptions provided in GATT Article XX. These exceptions apply when a measure is taken for particular purposes or under particular circumstances listed in Article XX. To prevent abuse, these exceptions are all subject to two safeguards provided in a general opening clause ("*chapeau*") to Article XX. The WTO Appellate Body has developed a standard "two-tiered" method for applying Article XX: first, examine whether a measure falls within one of these policy-based exceptions;

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[8] *Panel* Report, *Canada – Certain Measures Affecting the Automotive Industry*, WT/DS139/R, WT/DS142/R, adopted 19 June 2000, modified by Appellate Body Report, WT/DS139/AB/R, WT/DS142/AB/R, DSR 2000:VII, 3043, paras. 10.23-10.24.

[9] Described at http://www.unctad.org/Templates/Page.asp?intItemID=3618&lang=1, last visited January 25, 2008.

[10] For instance, in one case, the WTO Appellate Body found that the detrimental effect of a measure on imports may be "explained" – and thereby justified under Article III – "by factors or circumstances unrelated to the foreign origin of the product." Appellate Body Report, *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes*, WT/DS302/AB/R, adopted 19 May 2005, at para. 96. To recall, the Appellate Body here was expanding on a line of reasoning it started in *Chile - Alcohol* and *Korea – Beef* in which it found that "[a] formal difference in treatment between imported and like domestic products is…neither necessary, nor sufficient, to show a violation of Article III:4. [Rather, the question is] whether a measure modifies the conditions of competition…to the detriment of imported products," at para. 137.

second, determine whether it complies with the anti-abuse safeguards in the *chapeau*.[11] The following analysis concentrates on paragraph (g) of Article XX, which has been used in similar situations. Paragraph (b) of Article XX, covering measures "necessary to protect human, animal or plant life or health," could also apply to the measures described above. The "necessary" condition under paragraph (b) has been interpreted strictly in WTO jurisprudence although the Appellate Body has recently suggested that it should provide additional flexibilities when the measure is part of a comprehensive regulatory scheme or where there is a long-lead time between implementation and the expected result.[12]

A. Does an Exception in GATT Article XX Apply?

1. Article XX(g)

Article XX(g) provides an exception for "measures . . . relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption." The United States has already successfully argued in WTO dispute settlement that U.S. import restrictions on shrimp, which are tied to domestic restrictions on shrimp harvesting designed to protect sea turtles, are justified under Article XX(g). Article XX(g) would be the logical focus for justifying any trade measures on climate change that are otherwise inconsistent with GATT's market access or non-discrimination rules. Under the analysis used in the *US-Shrimp* case, the United States would need to demonstrate that:

- the resources to be protected, *e.g.*, clean air or dry land, are "**exhaustible**,"
- the measures at issue are measures "**relating to**" the conservation of the resource, and
- these measures are "made effective in conjunction with restrictions on domestic production or consumption."

First, in current circumstances, we believe that a WTO dispute settlement panel would agree that clean air and dry land are "exhaustible natural resources" in the sense of Article XX(g). The panel in *U.S. – Gasoline* explicitly found that clean air is a resource that is natural and capable of depletion, even if it is renewable.[13] Later, in *U.S. – Shrimp*, the Appellate Body stated "[w]e do not believe that 'exhaustible' natural resources and 'renewable' natural resources are mutually exclusive."[14] It also found that paragraph (g) must be "read … in the light of contemporary concerns of the community of nations about the protection …of the environment."[15] At present, no

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[11] Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products ("U.S. – Shrimp (AB)")*, WT/DS58/AB/R, 12 October 1998, paras. 118-119 (citing *US—Gasoline* case).
[12] In Appellate Body Report, *Brazil – Measures Affecting Imports of Retreaded Tyres* ("*Brazil – Tyres*"), WT/DS332/AB/R, December 3, 2007 (not yet adopted), at paras. 150-1, 172.
[13] Panel Report, *US – Gasoline*, at para. 6.37.
[14] *US – Shrimp (AB)*, at para. 128.
[15] *Id.*, para. 129.

concern about the protection of the environment is more important and uniting than the need to reduce GHG emissions, and the fact that the Convention on Climate Change was ratified by all but four UN Members States bears witness to that.[16]

Next, to be a measure "relating to" conservation, the allowance requirement must be crafted to bear a relationship with its stated goals, and must be designed to achieve those goals. Indeed, the Appellate Body has interpreted the phrase "relating to" to mean "primarily aimed at",[17] or evidencing a means and ends relationship.[18] In *U.S. – Gasoline*, the Appellate Body found that the measure at issue permitted "scrutiny and monitoring" of compliance with its environmental objectives. It therefore concluded that the measure, although inconsistent with national treatment, was truly designed to achieve clean air conservation and thus fell within the exception.[19] Likewise, in *U.S. – Shrimp*, the Appellate Body focused on the "design and structure" of the measure at issue and was satisfied to find that the measure was narrow enough in scope that it did not constitute a "simple, blanket prohibition" against importation. Consequently, the measure bore a "close and real relationship" with its stated objectives.[20]

Finally, to show that the allowance requirement program is "made effective in conjunction with restrictions on domestic production or consumption," the U.S. would have to show that if and where a requirement for allowances burdens imports, these allowances also burden domestic goods.[21] This test requires only "even-handedness,"[22] not "equality of treatment."[23] If a measure did not accord less favorable treatment to imports than it did domestic goods, it would not offend Article III, and therefore, would not need to be justified under an exception. On the other hand, a measure that solely burdens imports is not likely to be considered as even-handed, and would not find shelter under paragraph (g).[24] The import component of the allowances program is not intended to impose on foreign producers all or a disproportionate amount of the program's costs—it is intended to achieve appropriate burden-sharing in the shared fight against global warming, ideally through measures negotiated and adopted by governments. And even-handedness, because of the balance it strikes, sets a standard that the United States can meet in crafting climate change legislation.

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[16] See Status of Ratification, available at http://unfccc.int/files/essential_background/convention/status_of_ratification/application/pdf/unfccc_ratification_22.11.06.pdf, last visited April 23, 2007.
[17] Appellate Body Report, *US- Gasoline*, WT/DS2/AB/R, 29 April 1996, p. 16, 18-19.
[18] *US – Shrimp (AB)*, at para. 141.
[19] *US – Gasoline (AB)*, p. 19.
[20] *US – Shrimp (AB)*, at para.141.
[21] For example, in *U.S. – Shrimp*, the United States required shrimp trawlers to use turtle excluder devices (TED) to exclude turtles from their nets when fishing in waters that are likely to be turtle habitat. Exporting countries had to demonstrate their use of TEDs in order to be certified to export to the United States. Domestically, the United States required that shrimp trawlers use TEDs and imposed civil and criminal penalties (later changed to civil penalties and monetary sanctions) on offenders. See *U.S. – Shrimp (AB)*, at para. 144.
[22] *U.S. – Gasoline (AB)*, p. 20-21; *US-Shrimp (AB)*, at paras. 144-45.
[23] *U.S. – Gasoline (AB)*, p. 21.
[24] *U.S. – Gasoline (AB)*, p. 21.

An emissions allowances requirement falls within the policy-based exception for conservation in Article XX(g). As discussed above, the United States should encounter no difficulty arguing that clean air or dry land or other environmental resources put at risk by climate change are exhaustible natural resources threatened with depletion by GHG emissions. As for the second element under Article XX(g), "relating to," the Appellate Body has interpreted it in the *U.S. – Gasoline* and *U.S. – Shrimp* cases in a way that leads us to conclude that the United States could satisfy the standard it sets—since the allowances requirement is designed to effectively limit emissions by requiring presentation of allowance certificates.

Lastly, the United States could meet the requirement of even-handedness by applying the allowances requirement to domestic industry and enforcing the domestic program to compel producer reporting and compliance with the emissions caps. No WTO panel will accept a U.S. GHG reduction program that shifts all or a disproportionate part of the burden of GHG reduction to foreign producers, by restricting imports while giving a break to domestic producers. Even-handedness also rules out free rides—the United States must exempt from the allowances requirement all those countries that have adopted meaningful and satisfactory (i.e., comparable) emission reductions. On the other hand, the United States could exempt from coverage countries whose GHG emissions are below some *de minimis* level, as imposition of the allowance requirement to goods of such countries would not contribute to the non-trade policy objective of the program.

2. Article XX(b)

Article XX(b) offers an additional defense. It provides an exception for measures that are "necessary to protect human, animal or plant life or health." The United States would need to demonstrate:

- that the *policy* in respect of the measures for which the provision was invoked fell within the range of policies designed to protect human, animal or plant life or health; and

- that the inconsistent measures for which the exception was being invoked were *necessary* to fulfill the policy objective.[25]

First, we believe that a WTO dispute settlement panel would agree that a measure designed to curb climate vulnerability and its resulting effect on the spread and increased susceptibility of populations to disease and death would be a measure to protect human, animal and plant life or health within the meaning of Article XX(b). The World Health Organization has made a number of explicit findings linking climate change to significant public health problems that support this conclusion.[26] The Panel in *U.S. – Gasoline* found that Clean Air Act gasoline standards were designed to protect

[25] Panel Report, *US – Gasoline*, at para. 6.20.

[26] *See, e.g.,* Bulletin of the World Health Organization, *Global Climate Change: Implications for International Public Health Policy* (March 2007), available at: http://www.who.int/bulletin/volumes/85/3/06-039503/en/index.html, last visited January 25, 2008.

health and life.[27] Similarly, in *Brazil – Tyres* the Appellate Body found that Article XX(b) is satisfied by a measure to ban the importation of used tires because the accumulation of used tires contributed to the spread of disease and toxic tire fires.[28]

Second, in order to demonstrate that a trade-restrictive measure is "necessary" a country must show ""that the measure is apt to make a material contribution to the achievement of its objective."[29] To this end, the Appellate Body has recognized that "certain complex public health or environmental problems may be tackled only with a comprehensive policy comprising a multiplicity of interacting measures."[30] As an example of the type of objective that may require a longer time frame to demonstrate a contribution, the Appellate Body noted that "for instance, measures adopted in order to attenuate global warming and climate change, or certain preventive actions to reduce the incidence of diseases that may manifest themselves only after a certain period of time—can only be evaluated with the benefit of time."

Additionally, where the measure at issue is part of a comprehensive policy , the Appellate Body has noted that "[s]ubstituting one element of this comprehensive policy for another would weaken the policy by reducing the synergies between its components, as well as its total effect."[31]

An emissions allowance requirement for imports meets these criteria because it is part of a comprehensive policy that has synergies between its components and because it is apt to materially contribute to the reduction of carbon emissions, even if proof of that fact requires the benefit of time to demonstrate.

B. Does the Measure Satisfy the GATT's Safeguards Against Abuse?

As discussed above, all of the GATT's policy-based exceptions are subject to two safeguards provided in a general opening clause ("*chapeau*") to Article XX. This clause provides that measures that fall within the policy-based exceptions in Article XX may not be **applied in a manner** which would constitute **arbitrary or unjustifiable discrimination** between countries where the same conditions prevail, or a **disguised restriction on international trade**. The issue here is not the substance of a measure, but how it is applied. A WTO panel or the Appellate Body may agree entirely that a measure is a legitimate use of Article XX, but at the same time find that the way this legitimate measure is applied constitutes arbitrary or unjustified discrimination or disguised protectionism.

"Arbitrary or unjustifiable discrimination" in this context is discrimination not between products, but between countries where the same conditions prevail. The discrimination in question can be discrimination between the United States and one or more foreign countries, or it can be discrimination between different foreign countries.

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[27] Panel Report, *US – Gasoline*, at para. 6.21.
[28] Appellate Body Report, *Brazil – Tyres*, at para. 136.
[29] Appellate Body Report, *Brazil – Tyres*, at para. 150.
[30] Appellate Body Report, *Brazil – Tyres*, at para. 151.
[31] Appellate Body Report, *Brazil – Tyres*, at para. 172.

Different treatment of countries is permissible and even appropriate where these countries have objectively different conditions.[32] In practice, this proviso has been interpreted to bar an importing country from using an economic embargo to require its trading partners to adopt "essentially the same comprehensive regulatory program, to achieve a certain policy goal, as that in force within the Member's own territory, *without* taking into account different conditions which may occur in the territories of those other Members."[33]

The ban on arbitrary discrimination has also been interpreted to require that advantages offered to one trading partner must be equally available to other similarly situated trading partners. For instance, in the *US—Shrimp* case, the United States adopted a cooperative approach and negotiated an agreement on sea turtle protection with Caribbean nations, but did not pursue any negotiations with other WTO Members, including nations of the Western Pacific. The Appellate Body found that to avoid arbitrary or unjustifiable discrimination, the United States had to provide all exporting countries similar opportunities to negotiate an international agreement, by engaging in "serious, across-the board negotiations with the objective of concluding bilateral or multilateral agreements" on sea-turtle protection.[34] Nevertheless, although the United States had to make good faith efforts to reach agreements that are comparable from one forum of negotiation to another, its failure to reach comparable agreements did not constitute arbitrary or unjustifiable discrimination.[35]

Additionally, the discrimination must be evaluated based on its rationale rather than its effect.[36] That is, discrimination must have a rational connection to the objective of the measure, as described in one of the separate paragraphs of Article XX.[37]

The transparency and predictability of a measure are also relevant. In the *U.S. – Shrimp* case, the Appellate Body found the "informal" and "casual" nature of the certification process deprived it of basic fairness and due process, tarnished its transparency and predictability, and therefore, rendered it discriminatory in an arbitrary and unjustifiable manner.[38]

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[32] For example, in *Brazil – Tyres*, Brazil initially applied an import ban on tires from all origins, but then provided an exemption for tires from MERCOSUR countries. The panel found that the exemption constituted discrimination, but that the discrimination "[did] not seem to be motivated by capricious or unpredictable reasons." It found rather that the discrimination was due "to a ruling within the MERCOSUR framework [with] binding legal effects for Brazil." Panel Report, *Brazil – Tyres*, at para. 7.272. More importantly, the panel found that notwithstanding the ban, retreaded tires from non-MERCOSUR countries were still entering Brazil along with tires from MERCOSUR countries. The panel thus concluded that the discrimination resulting from the ban was arbitrary or unjustifiable under Article XX. Panel Report, *Brazil – Tyres*, at para. 7.306.

[33] *U.S. – Shrimp (AB)*, at para. 163-164; see also para. 177.

[34] *U.S. – Shrimp (AB)*, para. 166.

[35] *U.S. – Shrimp (AB)*, para. 166; Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products: Recourse to Article 21.5 of the DSU by Malaysia ("US – Shrimp (21.5 AB)*, WT/DS58/AB/RW, 22 October 2001, at paras. 122-134.

[36] Appellate Body Report, *Brazil – Tyres*, at para. 229.

[37] Appellate Body Report, *Brazil – Tyres*, at para. 227.

[38] *U.S. – Shrimp (AB)*, at paras. 180-81.

The requirement that the measure not constitute a "disguised restriction on international trade" has been defined as including restrictions that are actually discriminatory but are taken under guise of a legitimate Article XX exception: in effect, a form of stealth protectionism.[39]

As proposed by IBEW-AEP, U.S. climate change legislation would treat imports of products of countries that have *not* taken comparable action on GHG emissions less favorably than imports from a country that have done so. This difference in treatment would be justified under Article XX(g) of the GATT, for the reasons (and under the circumstances) described above. But in that case, the ban on arbitrary discrimination in the opening clause (*chapeau)* of Article XX would require that, if the United States were to negotiate with some countries before imposing the measure, it undertake "serious, across-the board negotiations with the objective of concluding bilateral or multilateral agreements" on GHG reduction, with *all* concerned parties. The United States would not have to reach agreements with these other countries, but it would have to make a non-discriminatory, good faith effort with each one. Second, the United States would have to take its trading partners' differences in circumstances into account in devising and implementing its measures. Finally, the U.S. measures would have to be implemented with due process and fairness. The IBEW-AEP proposal for U.S. climate change legislation meets these standards.

As we have discussed, the United States would appear to be in a strong position to defend a requirement that importers of goods from a country must present emission allowance certificates to cover the GHG emissions represented by the goods. First, such a measure is clearly linked to the purpose of GHG emissions reduction. Second, this would be a flexible measure adaptable to the circumstances of each exporting country, and therefore devoid of arbitrary or unjustifiable discrimination. Each exporting country would have a choice to implement any GHG emission reduction program as an alternative to forcing importers into presenting allowance certificates, and trading partners would be given a predictable standard in advance with which to achieve compliance. Third, the design, architecture, and structure of such an allowances requirement would demonstrate that the system has no purpose other than to cause the reduction of GHG emissions. Consequently, the *chapeau* of Article XX would pose no obstacle to deployment of a U.S. allowances program to combat climate change.

Attachment

[39] *U.S. – Gasoline (AB)*, p. 25.

APPENDIX OF RELEVANT WTO PROVISIONS

1. GATT Article I: General Most-Favored-Nation Treatment

1. With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation…any advantage, favour, privilege or immunity granted by any [Member] 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 [Members].

2. GATT Article II: Schedules of Concessions

1. (a) Each [Member] shall accord to the commerce of the other [Member] treatment no less favorable than that provided for in the appropriate Part of the appropriate Schedule.

(b) The products described in Part I of the Schedule…shall, on their importation into the territory to which the Schedule relates…be exempt from ordinary customs duties in excess of those set forth and provided therein. Such products shall also be exempt from all other duties or charges of any kind imposed on or in connection with the importation in excess of those imposed thereafter by legislation in force in the importing territory on that date.

3. GATT Article III: National Treatment on Internal Taxation and Regulation

1. The [Members] recognize that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products, . . . should not be applied to imported or domestic products so as to afford protection to domestic production.

2. The products of the territory of any [Member] imported into the territory of any other [Member] 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. . . .

4. The products of the territory of any [Member] imported into the territory of any other [Member] shall be accorded treatment no less favourable 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. . . .

4. GATT Note Ad Article III

Any internal tax or other internal charge, or any law, regulation or requirement of the kind referred to in paragraph 1 which applies to an imported product and to the like domestic product and is collected or enforced in the case of the imported product at the

time or point of importation, is nevertheless to be regarded as an internal tax of other internal charge, or a law, regulation or requirement of the kind referred to in paragraph 1, and is accordingly subject to the provisions of Article III.

5. GATT Article XI: General Elimination of Quantitative Restrictions

1. No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences or other measures, shall be instituted or maintained by any [Member] on the importation of any product of the territory of any other [Member] or on the exportation or sale for export of any product destined for the territory of any other [Member].

6. GATT Article XIII: Non-Discriminatory Administration of Quantitative Restrictions

1. No prohibition or restriction shall be applied by any [Member] on the importation of any product of the territory of any other [Member] or on the exportation of any product destined for the territory of any other [Member], unless the importation of the like product of all third countries or the exportation of the like product to all third countries is similarly prohibited or restricted.

7. GATT Article XX: General Exceptions

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any [Member] of measures:

* * *

(b) necessary to protect human, animal or plant life or health;

* * *

(g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption.