


# TACKLING DEFORESTATION AND THE TRADE IN FOREST RISK COMMODITIES: CONSUMER-COUNTRY MEASURES AND THE WTO

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A range of consumer-country measures have been deployed by governments as part of the global effort to combat illegal logging and the trade in illegal timber. These include regulations which affect imports, such as the EU Timber Regulation, which makes it an offence to place illegally sourced timber products on the EU market, whether from domestic or foreign production, and the US Lacey Act, which prohibits the import of illegally sourced timber. Similar measures are being contemplated as means to reduce deforestation associated with the production and trade of agricultural commodities such as palm oil, soy or cocoa – most notably by the EU under its recent proposed framework to protect and restore the world’s forests.

Any measures taken by consumer countries to discriminate in trade between products based on the ways in which the products are produced, rather than their inherent characteristics, raises potential questions of compatibility with the trade disciplines of the World Trade Organisation (WTO).

This brief analyses the potential issues that could arise from any such new government policy. Since there has never been a WTO dispute case involving trade measures taken against illegal or unsustainable timber or agricultural commodities, it is not known exactly how the WTO’s dispute settlement system would rule. It is possible, however, to reach some conclusions from examining other disputes. The arguments around the application of these trading rules are slightly different in the case of trade measures based on standards of sustainability and those based on standards of legality.



## Background: the WTO system and its approach against trade discrimination

The WTO agreements lay down general rules for governments to follow in liberalising international trade. They cannot possibly deal with every specific traded product or service, so they set out broad principles which must be interpreted and applied in particular dispute cases where one WTO member believes that another is failing to

comply with them. (It should be noted that WTO rules apply only to governments and public policy, not to private enterprises and their purchasing and sourcing policies.)

The WTO system is based around opposition to discrimination in trade. Its core principles, found in its central agreement, the General Agreement on Tariffs and Trade (GATT), include GATT Articles I ('most favoured nation' treatment) and III ('national treatment'): WTO members are not permitted to discriminate between traded 'like products' produced by other WTO members, or between domestic and international 'like products'. GATT Article XI ('elimination of quantitative restrictions') forbids any restrictions other than duties, taxes or other charges on imports from and exports to other WTO members. Essentially the same principles are built into the other WTO agreements that have developed alongside the GATT, such as the Agreement on Technical Barriers to Trade or the Agreement on Sanitary and Phytosanitary Standards. It was always recognised, however, that some circumstances justified exceptions to this general approach, permitting governments to apply unilateral trade restrictions in particular circumstances; these are set out in GATT Article XX, and similar provisions are included in other WTO agreements.

The bodies that carry out the interpretation of these rules in trade disputes are the dispute panels (generally composed of trade experts), which issue an initial set of findings, and the WTO Appellate Body (mostly international lawyers), to which dissatisfied parties can appeal. Since their decisions can only be overturned if all WTO members (other than those involved in the dispute) agree – which has never happened – this system is a powerful means of resolving conflicts and ensuring that trade rules are interpreted and applied consistently around the world. If the loser in any given case does not modify its policy accordingly, the winner is entitled to take trade-restrictive measures (e.g. apply tariffs) against it to the estimated value of the trade lost because of its action.

It should be noted that interpretations can change, even if the wording that is being interpreted does not. Since the founding of the WTO, decisions by the Appellate Body in particular have clearly helped to shift the way in which the system is applied, especially in environment-related disputes. It is this key role for interpretation that often leads to uncertainty and disagreement over what the WTO rules might mean in practice.

## **Sustainability-based trade measures**

The question of whether products possessing identical physical characteristics but grown, harvested or processed in different ways are 'like products' – for example, certified sustainable timber and timber not so certified – was extensively discussed in the early years of the trade–environment debate. It was triggered in particular by a GATT panel ruling (in the tuna–dolphin dispute case in 1991) which suggested that this kind of discrimination was not compatible with the GATT – a conclusion which became conventional wisdom and which, in some quarters, is still regarded as such.



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In fact, however, no such language exists in the GATT or other WTO agreements, and a number of later WTO disputes (in particular the shrimp–turtle disputes of 1998 and 2001 and the asbestos case of 2001) comprehensively undermined the conclusion that discrimination is not permitted on the basis of 'processes and production methods' (PPMs). The final outcome of the shrimp–turtle dispute, for example, saw the US permitted to maintain its embargo on imports of shrimp caught in ways which killed endangered species of sea turtles – a PPM.

This long-running dispute, involving two separate cases, led to a number of conclusions with important implications for PPM-based trade discrimination. These included the conclusion that discrimination on the basis of PPMs could be permitted as long as it is carefully targeted (e.g. on a shipment rather than a country-of-origin basis) and as long as it is enforced evenly between domestic and foreign products; and that while bilateral or multilateral agreements covering the traded products in question are always preferable, unilateral environmental measures which restrict trade may still be lawful even in their absence.

How could 'sustainable' agricultural products be defined? In general, WTO agreements such as the Technical Barriers to Trade Agreement require criteria to be expressed in terms of performance rather than design or descriptive characteristics. So trade preferences given to 'sustainable palm oil', for example, might be permissible, but specifying 'sustainable palm oil' as only those products certified by the Round Table on Sustainable Palm Oil (RSPO), or any other specific scheme, would not be. The government applying the measure would have to draw up a list of criteria (which, in this example, could be equivalent to, or even exactly the same as, those of the RSPO standard) which any supplier could potentially meet, regardless of its membership of RSPO. There are now many examples of potential deforestation-related criteria, both in certification schemes such as RSPO and in voluntary company commitments – including, for example, prohibiting planting on high conservation value and high carbon stock forests and peatlands – which can be drawn on.

The government applying the measure would also have to devise a means of judging whether products satisfied the criteria without the process imposing undue costs on the companies exporting and importing the product. There is no reason to think that this could not be done; the same challenges have been faced, successfully, in implementing public procurement policies for timber, for example.

There is an additional problem for oilseeds such as palm oil, soybean oil or rapeseed oil which, it can be argued, are 'like products' to each other; they are equally usable, for example, as a base for frying, a food additive or a component of biodiesel. If this is the case, any restrictions placed on one type – requirements for sustainability for palm oil, for example – would need to be extended to other oils.

In other ways, however, oilseeds are different from one another: palm oil, for example, is more energy-dense than other vegetable oils (one reason why it is such a successful crop) and the various oilseeds grow in different conditions and, usually, different countries. They also possess different tariff classifications under the Harmonised System of customs codes, and consumers have often expressed a preference to avoid, in particular, palm oil. The EU is currently proposing to treat palm oil differently from other vegetable oils (because of its impact on forests) in terms of its eligibility for regulatory and financial support in its use as a biofuel; Indonesia and Malaysia (the main palm oil producers) have threatened action under the WTO in retaliation. This helps to illustrate how difficult the question of ‘likeness’ is to judge; it would have to be determined in relation to the trade measure in question if it came to a WTO dispute.

## Legality-based trade measures

Measures targeting illegal products, such as the US Lacey Act, the EU Timber Regulation or the Australian Illegal Logging Prohibition Act, should raise fewer WTO issues, though in this case there are no relevant dispute cases to provide precedents.

It has been argued by some commentators that legal and illegal timber should be considered to be ‘like products’ and therefore any discrimination between them would be a violation of GATT Article I, though it could possibly be justified under the exemptions in Article XX (which permit governments to apply unilateral trade restrictions in particular circumstances). However, it is not at all clear whether in reality a GATT dispute panel would conclude that legal and illegal timber are like products. One of the conclusions in the asbestos dispute case mentioned above was that a determination of ‘likeness’ rests on the nature and extent of the competitive relationship between the products in question – and there should of course be no competitive relationship between legal and illegal products, because the latter should not be on the market in the first place. More broadly, arguably, legality is a universal requirement that any product must possess to be put on sale in a market (at least, a legal market). There is no experience at all of how a WTO dispute would consider this issue.

It is of course virtually inconceivable that any country would mount a challenge under the WTO on the basis that illegal products exported from its own territory should not be excluded from international trade – in effect, it would be arguing that its own laws should be broken. What is more possible is that a country could mount a challenge against measures taken against illegal products that it felt unfairly discriminated against its own exports of legal timber – for example if they faced requirements for documentary proof of legality that timber produced domestically in the importing nation did not. Indeed, this concern was raised by a number of timber-exporting countries, including Canada and New Zealand, during the Australian parliament’s hearings on the draft Australian Illegal Logging Prohibition Bill. It could be argued that these kind of requirements violate GATT Article XI, as they represent restrictions other than duties, taxes or other charges on imports from other WTO members. The Australian government did not agree with them, however, and to date there is no evidence to suggest that imports are treated less favourably than domestic production under Australian Act, or the EU Timber Regulation or the US Lacey Act.

As mentioned above, there is no experience of how a WTO dispute would consider this issue, and

commentators are divided on whether such measures would violate any of the provisions of the GATT or, even if they do, whether they could be justified under the exemptions in Article XX. What is clearly important – and is spelled out explicitly in Article XX – is that any unilateral measure should not lead to arbitrary or unjustifiable discrimination in trade.

### The WTO and the EU Timber Regulation and FLEGT-Licensed Timber

As well as its prohibition on illegally sourced timber, the EU Timber Regulation also places a requirement on those companies first placing timber products on the EU market to have in place a due diligence system designed to minimise the chance of their handling illegal products. This requirement applies equally to timber produced domestically within the EU as well as to imports, so it should raise no question of discrimination.

It is still too early to assess the practical outcomes of operators' implementation of their due diligence systems, but care will need to be taken to ensure that the risk assessment process they must carry out as its first step does not in practice lead to entire countries being treated as high-risk sources. If more extensive (and therefore potentially more costly) documentary evidence were routinely demanded of all products originating in some countries and not others, regardless of the company or area of production, the regulation could be found to be operating in effect to give protection to some countries' products at the expense of others'. The EU Timber Regulation itself, and its implementing regulation setting out details of the due diligence procedure, are careful to specify that operators should seek information not just about the country of origin and its level of illegal logging, but also about the sub-national region and concession of origin, including the prevalence of illegal activity in the sub-national region, where these vary within the country.

While there has to date been no systematic study of the impacts of the EU Timber Regulation, anecdotal evidence suggests that EU importers are not abandoning sources just because they may be more high risk; instead, they appear to be increasing their scrutiny of their supply chains and tending to place more reliance on certification schemes. In general, however, exports of timber from developing countries to the EU have fallen significantly since the early 2000s – even before the implementation of the EUTR – while exports to China and other emerging economies have risen, so it is difficult to pick out any specific impact of the regulation. Major timber certification schemes do not systematically track exports and imports of certified products (unlike FLEGT licenses – see below).

The timber legality licensing systems to be set up under the FLEGT Voluntary Partnership Agreements between the EU and timber-exporting countries raise no WTO issues. Countries can impose any conditions on trade between themselves – such as the requirement for a license – through bilateral agreements such as these, as long as no other WTO member country is affected by the measure. In practice, the introduction of Indonesia's FLEGT licensing scheme in 2016 has led to a small increase in sales in the EU (mainly in the UK) since its inception.

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## Conclusion

No one can say for sure what would be the outcome of a WTO dispute case involving measures taken to exclude illegal or unsustainable timber or agricultural commodities from international trade. Since the case would rest on the interpretation of various clauses of the GATT and other WTO agreements, and as there is little experience to date of WTO dispute cases dealing with similar issues, it is only possible to speculate.

Partly because of this, the WTO agreements can still create a problem for these kind of trade measures (and environment-related trade measures in general). The image and perception of the WTO, the fact that very few people really know how the system works, and the general consensus that barriers to trade are undesirable, can create a 'chilling effect', through which environment policy-makers are dissuaded (sometimes by interventions from their trade policy-maker colleagues) for arguing for any kind of consumer-country measure even when they would almost certainly be permitted under WTO rules.

This would be a mistake. In designing environmental policies with trade impacts, it is clearly important to be aware of the broad constraints placed by WTO rules. The more the measure diverges from the core WTO principle of non-discrimination in trade, and the more trade-disruptive it is, the more vulnerable it could be to challenge. Within these constraints, however, governments have plenty of flexibility to adopt measures which do affect trade, and policy-makers should not allow themselves to be dissuaded from exploring them.



## FURTHER READING

For a more detailed discussion of these issues, see:

- Duncan Brack, Controlling Imports of Palm Oil: Interaction with WTO Rules (Global Canopy Programme, 2013)
- Duncan Brack, Combating Illegal Logging: Interaction with WTO Rules (Chatham House, 2013)
- Dylan Geraets and Bregt Natens, The WTO Consistency of the European Union Timber Regulation (Leuven Centre for Global Governance Studies, 2013)