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## Lectio Praecursoria

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Our climate is changing. There are risks that some places on Earth become unbearably hot, whereas islands may sink under water. There is also overwhelming scientific evidence that human activities have significantly contributed to this development.

In all this, is it evident that changes are needed with respect to the foundations of our economic system in order to deal with climate change. Companies and consumers may take some voluntary action, but it will not be sufficient. A broader change to reverse the current path will require the creation of the right incentives.

Governments can take action. Indeed, some governments are already taking some action. In particular, activities bad for the climate may be banned. Alternatively, incentives are created to give preference to environmental-friendly solutions. For example, there are programs to promote energy from renewable resources. Some programs establish a compulsory quota for renewables, while other programs offer renewables a so-called feed-in-tariff, which is a long-term contract that ensures the demand and a market price premium for renewables.

Electricity is an important field within the energy sector. The end product – electricity – is identical regardless of whether it is generated from fossil fuels, nuclear fission or renewables. What differs is the resource and thus the production method. The decision to promote energy from renewables is in other words a decision to promote a certain process and production method.

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Governments implement environmental criteria for products. The objective of these criteria may be to protect nature and public health. Traditionally, the criteria have targeted the physical characteristics of the products offered on the market. For example, there may be criteria on the toxicity of the good.

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Today, the focus of regulation is no longer limited to the physical characteristics of the end product. A more holistic approach, covering the full life-cycle, is often adopted. The environmental impacts of a product begin when the raw materials are collected and end with end-of-life treatment of the used product. It is in other words essential that criteria are adopted for process and production methods as well as for end-of-life treatment, such as recycling.

Criteria on environmental-friendly process and production methods are not only relevant for the energy sector. Producing any product – or service for that matter – may cause carbon emissions, other pollution or environmental harm that deserves the attention of the regulator. For example, criteria have been implemented for sustainable forestry as well as on fishing and hunting methods in order to protect animals. There have also been criteria on the size of cages in which farm animals are kept. Finally, there may be criteria to protect the working conditions, the health and the safety of workers.

Regulating process and production methods is about more than environmental protection. For example, while criteria on fishing and hunting methods can partly be about protecting biodiversity, they can also be about moral concerns. This of course raises the question of whether even measures against climate change could be viewed to contain a moral dimension.

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There are some legal risks with implementing environmental criteria or other criteria on process and production methods. A state may decide to apply the criteria on its in-state production. Such a measure may be politically controversial but does not yet constitute any major legal risk. However, only applying the criteria in-state will create a disadvantage for the in-state industry. Hence, states are likely to extend the criteria also to imports. It is with this step that legal questions arise.

The same criteria might apply for in-state production and imports. The criteria adopted by the state may still be viewed as designed to protect the in-state industries and disadvantage out-of-state products. Sometimes the discriminatory effect has not been the product of intentional efforts but is rather an incidental outcome of the measure.

There are also occasions where the state decides to explicitly favor its own industry by adopting less favorable criteria for imports. For example, states in Europe have adopted schemes that offer benefits to electricity generated from renewable resources. Imported electricity has as a rule been excluded from receiving these benefits.

Discriminatory measures adopted by states may run counter to trade law. The idea with trade law is that industries in each state can produce whatever they are best at producing. Making use of their comparative advantages in other words. The goods (and services) produced in different states may then be traded across a larger geographic area. In accordance with economic theory, this should enhance efficiency. Discriminatory measures again hinder the opportunities of free trade.

There has been some criticism that trade law puts too much emphasis on economic values. It is still important to remember that even discriminatory state measures may be justifiable with reference to environmental and moral objectives. Environmental criteria on process and production methods can be justifiable. It is, however, crucial to get their design right.

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What legal cases have then emerged specifically on criteria on process and production methods? And what type of criteria on process and production methods have states been adopting?

In the early '90s the US adopted criteria on the methods of fishing tuna in order to protect dolphins. The design of the measure was challenged under international trade law. The difficulty with respect to get the design right is illustrated by the fact that the latest decision in the lengthy series of disputes was published last December.

In the early '90s US criteria on methods to catch shrimp designed with the objective to protect turtles were also challenged. Other than that, cases on criteria on process and production methods were rare at that time.

In the late '90s a case was brought to the European Court of Justice on the German system for promoting electricity from renewables. Domestically generated electricity was offered benefits not available for imported electricity. The Court found that in this case even such explicit discrimination was justifiable. That is very rare. Hence, it may be argued that it underlined the power of the environmental argument in the context of an energy transition. Note that this was already 20 years ago.

For some reason major cases on process and production methods did not thereafter emerge for a while. It is only this decade that significant development has taken place. The question of whether it is acceptable for an EU Member State to limit the benefits of its system promoting electricity from renewable resources to domestic production has been re-litigated in two cases. The outcome was no different than 20 years earlier.

There has been a greater number of cases in the US on process and production method criteria. California's decision to adopt a minimum size for cages that

chickens are kept in has been challenged in court. Many other cases have concerned the energy sector. States in the US have adopted programs to promote energy from renewables that have been questioned by out-of-state parties with strong links to the fossil fuel industry. The claim has been that promoting renewables in one state discriminates against the fossil fuel industry in another state.

Similar cases have not emerged in the EU. However, when Austria planned to ban the import of electricity generated by nuclear power plants, the Commission put pressure on the state to change its plans. In the end, Austria decided to amend its program and discourage the import of nuclear power through less drastic means.

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On the international arena some new cases have also been initiated. The EU had adopted a ban on the import of seal products due to concerns with respect to the methods seals are hunted and killed. The design of this ban was litigated under the World Trade System.

In the field of energy, Argentina has claimed that the biofuel sustainability criteria adopted by the EU breach WTO law. Common forms of biofuels are bioethanol and biodiesel. These may be made out of different food and feed crops, such as US corn, Brazilian sugarcane, European rapeseed and Argentinian soybean. In Indonesia and Malaysia they in turn rely on palm oil. Biofuel may also be produced out of waste, algae and other biomass.

For biofuel to be regarded as sustainable, the feedstock must not have been collected from biodiverse and other sensitive land. Moreover, the estimated carbon emissions from producing the fuel must not exceed a pre-determined sustainability threshold. There is a lot of controversy surrounding the calculation methods relied on when estimating carbon emissions from producing biofuels. Cutting forests to grow energy crops may lead to emissions. This change in land use can also be indirect. For example, agricultural land for food crops is turned into land for energy crops and rainforests are then cut down to make new areas for agricultural crops. Is it fair to contribute such indirect effects to biofuels production, and biofuels production alone?

Only biofuel that meets all sustainability criteria may be promoted. The claim by Argentina is essentially that the EU has designed its criteria in order to favor its own biofuel production to the disadvantage of Argentinian soybean biofuel.

Federal biofuel sustainability criteria have also been adopted by the US and a separate scheme has been designed in California. The Californian model has been litigated in US courts for almost a decade and has been upheld so far. It remains to

be seen what its fate will be if the case ends up in the Supreme Court, with its current conservative majority.

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As just described, this decade there have been a growing number of cases on process and production method criteria. Courts have delicately through traditional legal tests reconciled economic objectives, environmental objectives and fundamental values, such as the right to due process.

One major question still remains unresolved. States have decided to adopt criteria on process and production methods that they apply also on imports. Those imports are naturally produced out-of-state. Pollution from the production out-of-state often has cross-border environmental impact. Imagine, however, that the negative effects of the production out-of-state remain local and do not spread to the importing state adopting the criteria. On what grounds, if any, may the state defend such criteria in case they have discriminatory effects? May it refer to environmental benefits occurring in another state? Or could it rely on moral objectives?

In the international context, it is particularly important to remember that strict criteria on process and production methods are now mostly being implemented by developed states. These states have historically gained an economic advantage by relying on dirty production methods. The decision by the EU or the US to now implement strict criteria on process and production methods will hinder less developed states from catching up economically, as exports to the EU and the US would be limited. A fair solution may be for the more developed states to offer technology transfers. There is, however, no legal obligation for that. The issue of criteria on process and production methods is not just about law, but also about politics.

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The question of how to design criteria on process and production methods has been raised on both sides of the Atlantic. When faced with difficult questions, it can be valuable to learn from various experiences across jurisdictions. Moreover, mutual learning may facilitate bilateral and multilateral trade talks. That objective is particularly important considering the current global political climate and the trend towards nationalism and trade wars.