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US Position on Tobacco in the TPPA
Prepared for Action on Smoking and Health
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During the week of August 12, 2013, the U.S. Trade Representative (USTR) vetted a revised U.S. position on treatment of tobacco in the Trans-Pacific Partnership Agreement (TPPA). According to published accounts, USTR plans to scrap its previous proposal for a limited exception to protect tobacco-control measures from litigation under the TPPA. In its place, the USTR proposes (1) a statement on the TPP health exception, and (2) a consultation process for TPP trade disputes that challenge tobacco-control measures.¹ This note responds to questions about whether the revised U.S. position would have any legal effect if implemented. Our conclusion is that the U.S. proposal manages to insert the word *tobacco* into the TPPA without legal effect.

1. Health statement

In the chapter on exceptions, USTR proposes to insert a statement similar to this:

“TPP members agree that measures referred to in Article XX(b) of the General Agreement on Tariffs and Trade (GATT) and in Article 14 of the General Agreement on Trade in Services (GATS) include measures ‘necessary to prevent or reduce tobacco use or its harms.’”²

a. Legal context

In order to explain whether the USTR’s health statement has any legal significance, it is necessary to explain the legal context into which the statement would be inserted.

(1) *The model* – The proposed TPP health statement appears to be modeled after similar statements in the Korea-U.S. FTA (KORUS), for example:

“The Parties understand that the measures referred to in Article XIV(b) of GATS include environmental measures necessary to protect human, animal, or plant life or health.”³

(2) *The drafting context* – The TPP chapter on exceptions has not been disclosed. Assuming that it replicates the KORUS exceptions chapter, it would operate as follows:⁴

- (a) First, the exceptions would apply to only some TPP chapters.
 - (i) Chapters to which the exceptions apply include those on goods, services, and technical barriers to trade, among others.
 - (ii) Chapters to which the exceptions do not apply include investment and intellectual property.

(b) Second, rather than define its own terms of exception, the chapter incorporates by reference the general exceptions of GATT and GATS. This approach

¹ USTR Prepares To Table Revised TPP Tobacco Proposal, Briefs Congress, *Inside U.S. Trade*, August 16, 2013.

² *Id.*

³ Korea – United States Free Trade Agreement, art. 23:1.2 (General Exceptions). (Hereafter, KORUS)

⁴ KORUS, art. 23:1.

incorporates not only the text of the exception, but also the WTO jurisprudence that interprets the text. The WTO health exception is the same in both GATT and GATS. It reads:

- (i) "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 like conditions prevail, or a disguised restriction on trade in services, 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; . . .⁵ (emphasis added)
- (ii) The underlined portion of the exception is the necessity test for a health measure; the preceding portion – often called the *chapeau* – sets out additional restrictions on applying the exception.

(c) In KORUS, the statement that environmental measures come within the scope of health exceptions follows immediately after the sentence that incorporates the exceptions of GATT and GATS. This is also the logical place to insert USTR's proposed health statement regarding tobacco measures.

(d) The implicit purpose of USTR's health statement on tobacco measures is to guide interpretation by a dispute panel of whether a tobacco-control measure satisfies the first and least onerous of the five tests that a measure must pass in order to qualify for the GATT/GATS health exception. The following chart provides an overview.

5 Stages of Analysis – the GATT/GATS Health Exception

Three stages of the necessity test: Is a measure necessary?

1. Is the challenged measure a health measure? (i.e., is it within the scope of the exception?)
2. If so, is there a *prima facie* defense of necessity? This requires weighing and balancing of:
 - a. Importance of values or interests at stake.
 - b. Contribution of the measure to its health objective.
 - c. Restrictiveness in terms of trade.
3. If there is a *prima facie* defense, are less-restrictive measures reasonably available?

Two chapeau tests: These apply if a measure is found to be necessary.

4. Is the measure arbitrary as applied? (E.g., do other policies that contrary results?)
5. Is the measure unjustifiably discriminatory as applied?

b. *Legal significance*

USTR's proposed health statement on tobacco measures is not legally significant for two main reasons, but even if it were helpful, the additional elements of an exception would neuter its impact.

(1) *General exceptions do not cover investment*

Assuming that TPPA drafters follow the KORUS model, general exceptions do not apply at all to the chapters on investment and intellectual property (and perhaps other new chapters such on regulatory coherence and state-owned enterprises). The greatest litigation threat to tobacco-control measures is posed by the chapter on investment, with some investment claims potentially reinforced by the chapter on intellectual property. For example, in the investment disputes against Uruguay and Australia, Philip Morris International is seeking compensation for expropriation of its

⁵ GATT art. XX; GATS art. XIV.

trademarks and denial for fair and equitable treatment (interference with its expectations of profit).⁶ The Government of New Zealand estimates that the cost of investment arbitration is in the range of \$2.4 to \$4.8 billion U.S. dollars (USD) (which is \$3 to \$6 billion New Zealand dollars (NZD)), and the cost of defending a WTO dispute is in the range of \$1.26 to \$1.68 million USD (\$1.5 to \$2 million NZD).⁷ A recent survey by the Organization for Economic Co-operation and Development (OECD) found that legal and arbitration costs averaged over \$8 million USD, exceeding \$30 million in some cases; tribunals usually required parties to share tribunal and administrative costs equally and absorb their own legal costs.⁸ Another recent survey found that in approximately 80 per cent of investment cases surveyed, governments had to cover their own costs, even though they succeeded in getting the investment claim dismissed.⁹

(2) *Health-relevance of tobacco controls is not an issue*

Second, the USTR's proposed health statement – that tobacco-control measures are health measures – states the obvious. As the WTO dispute panel remarked in the clove cigarettes dispute, “It is self-evident that measures to reduce youth smoking are aimed the protection of human health ...”¹⁰

(3) *Health-relevance alone does not establish necessity*

Before a WTO dispute panel, the analysis of whether a measure is necessary involves a three-stage analysis. The first asks whether a measure fits within the scope of protected health measures.¹¹ This is the question addressed by the U.S. proposal. But after a defending country establishes that a tobacco-control measure is a health measure, two stages remain. The second stage “balances and weighs” three factors to determine *prima facie* whether a measure is necessary: the importance of values or interests at stake, the contribution of the measure to the objective, and the restrictive

⁶ See Jane Kelsey, *The Trans-Pacific Partnership Agreement—A Gold-Plated Gift to the Global Tobacco Industry?*, 39 AM. J.L. & MED 237, 252-262 (2013); Robert Stumberg, *Safeguards for Tobacco Control: Options for the TPPA*, 39 AM. J.L. & Med. 382, 385-390 (2013).

⁷ N.Z. MINISTRY OF HEALTH, REGULATORY IMPACT STATEMENT: PLAIN PACKAGING OF TOBACCO PRODUCTS 11 (Mar. 28, 2012), available at <http://www.health.govt.nz/system/files/documents/pages/regulatory-impact-statement-plain-packaging-tobacco-products.pdf>.

⁸ ORG. FOR ECON. CO-OPERATION & DEV, INVESTOR-STATE DISPUTE SETTLEMENT, PUBLIC CONSULTATION: 16 MAY – 9 JULY 2012 37 (2012), at 17, available at <http://www.oecd.org/daf/inv/internationalinvestmentagreements/50291642.pdf>.

⁹ Mahnaz Malik, *The Stakes of States in Defending Investment Treaty Arbitrations: A Game of luck and chance?*, Background Paper, IV Annual Forum for Developing Country Investment Negotiators (New Delhi, October 27-29, 2010), at 3.

¹⁰ Panel Report, United States – Measures Affecting the Production and Sale of Clove Cigarettes, WT/DS406/R (2 Sept. 2011) ¶ 7.347. The clove cigarette dispute did not involve the health exception of GATT or GATS because Indonesia based its challenge on the TBT Agreement, which has no exceptions. However, the dispute raised an analogous issue when Indonesia claimed that the U.S. ban on cigarette flavorings, except for menthol, did not pursue a legitimate health objective under art. 2.2 of the TBT Agreement. Art. 2.2 provides that “technical regulations shall not be more trade-restrictive than necessary to fulfil a legitimate objective ... Such legitimate objectives are, inter alia: ... protection of human health or safety, animal or plant life or health ...” (emphasis added) It was in this context that the panel cited the legislative purpose reported by Congress (“to protect the public health and to reduce the number of individuals under 18 years of age who use tobacco products”), and concluded that “[i]t is self-evident that measures to reduce youth smoking are aimed the protection of human health ...”. Panel Report, at ¶¶ 7.336, 7.347.

¹¹ See Appellate Body Report, China – Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audiovisual Entertainment Products, WT/DS363/AB/R (Dec. 21, 2009), ¶ 230.

effects of the measure on international trade.¹² If a measure passes the second stage as *prima facie* necessary, the third stage requires an evaluation of whether less-restrictive measures are reasonably available.¹³ The challenging country carries the initial burden of identifying alternative measures, and if it does, the burden shifts to the defending country to show that the alternatives are not “reasonably” available.¹⁴ To summarize, a country can defend its tobacco-control measure as necessary if it passes the first, second and third stages of analysis. However, the many balancing and comparison tests make the proof of necessity unpredictable – somewhere between *indispensable* and *making a contribution*.¹⁵ Establishing that a tobacco-control measure is a health measure merely leads to the more challenging two stages of proving necessity.

(4) *Necessity alone does not satisfy an exception*

Even if a measure passes the necessity test, it still needs to satisfy the additional restrictions in the chapeau, which require that 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 trade”¹⁶ The necessity test considers the substance of a measure, while the additional restrictions consider how the measure is applied. A measure may well be necessary on its face but then fail to satisfy the additional considerations as applied.¹⁷ This was the case in two recent decisions, *Brazil – Tyres* and *United States – Gambling*,¹⁸ where the Appellate Body found that bans (on importing retreaded tires and Internet gambling) were necessary to protect health, but the measures failed the test of arbitrary or unjustifiable discrimination.¹⁹ The chapeau tests are particularly difficult for tobacco-control measures that seek to freeze the market by prohibiting new entrants (e.g., clove flavorings or electronic cigarettes) without banning existing products to which smokers are already addicted.

(5) *Summary*

To summarize, the U.S. proposal for a health statement would amend a TPP exception that does even not apply to investor-state arbitration, the most significant risk of litigation. In the context of trade disputes between TPP governments, it adds

¹² *Id.* ¶ 237-38; Appellate Body Report, *Brazil--Measures Affecting Imports of Retreaded Tyres*, WT/DS332/AB/R (Dec. 3, 2007), ¶ 178.

¹³ ABR, *China – AV Products*; ABR, *Brazil – Tyres*; ABR, Appellate Body Report, *United States – Measures Affecting the Cross-Border Supply of Gambling and Betting Services*, ¶ 292, WT/DS285/AB/R (Apr. 7, 2005); Appellate Body Report, *European Communities – Measures Affecting Asbestos and Asbestos-Containing Products*, ¶ 171, WT/DS135/AB/R (Mar. 12, 2001).

¹⁴ ABR, *Brazil--Tyres*, ¶ 156; Panel Report, *Dominican Republic--Measures Affecting the Importation and Internal Sale of Cigarettes*, ¶ 7.22, WT/DS302/R (May 19, 2005) (stating that the Dominican Republic failed to meet in burden of showing that its tax scheme was less restrictive than alternatives identified by Honduras); Panel Report, *United States--Clove Cigarettes*, *supra* note 177, ¶ 7.422 (Indonesia must do more than merely list alternatives, it must establish that alternatives make a contribution to the health objective).

¹⁵ See Appellate Body Report, *Korea--Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, ¶ 161, WT/DS161 /AB/R, WT/DS169/AB/R (Jan. 10, 2001).

¹⁶ GATT art. XX; GATS art. XIV.

¹⁷ Appellate Body Report, *United States--Import Prohibition of Certain Shrimp and Shrimp Products*, ¶¶ 118-119, 160, 19WT/DS59/AB/R (Oct. 12, 1998); Appellate Body Report, *United States--Standards for Reformulated and Conventional Gasoline*, 22, WT/DS2/AB/R (Apr. 29, 1996).

¹⁸ ABR, *U.S.--Gambling*, ¶¶ 367-69.

¹⁹ See ABR, *China--AV Products*, ¶¶ 237-38.

nothing that is not already self-evident. The most challenging stages of proving an exception come after a tobacco-control measure is established as a health measure. These involve the balancing and alternative tests of necessity and the more formidable discrimination test of the chapeau.

2. Consultation

In the chapter on dispute resolution, USTR proposes language similar to this:

Before one party may launch a trade dispute against another, health authorities from the TPP countries involved in the dispute must consult and discuss whether the contested measure is “appropriate.” Even if the health ministers agree that a measure is appropriate, however, they are not empowered to block a dispute from going forward.²⁰

a. *Legal context*

In order to explain whether the USTR’s consultation proposal has any legal significance, it is necessary to explain the legal context into which the statement would be inserted.

- (1) As with the chapter for exceptions, the TPP dispute settlement chapter is expected to mostly replicate the KORUS dispute settlement chapter. This consultation is for disputes between governments under trade rules. The proposal does not apply to consultation with investors under the investment chapter.
- (2) Based on its similarity, the model for USTR’s tobacco dispute consultation appears to be the consultation provision already contained within the KORUS dispute chapter, which means that the model is already in the draft TPP dispute settlement chapter. KORUS includes two articles that apply to parties before formal dispute settlement begins:
 - (a) First, “Parties shall endeavor to agree on the interpretation and application of this Agreement, and shall make every attempt through cooperation and consultations to arrive at a mutually satisfactory resolution of any matter that might affect its operation.”²¹
 - (b) Second, either Party to an imminent dispute may request consultations, and the other Party must respond. Most likely, it is this consultation article into which USTR’s tobacco consultation would be inserted. The entire article reads as follows:²²

ARTICLE 22.7: CONSULTATIONS

1. Either Party may request consultations with the other Party with respect to any matter described in Article 22.4 by delivering written notification to the other Party. The complaining Party shall set out the reasons for the request, including identification of the measure or other matter at issue and an indication of the legal basis for the complaint. The other Party shall reply promptly to the request and enter into consultations.

2. Promptly after requesting or receiving a request for consultations pursuant to this Article, each Party shall seek the views of interested parties

²⁰ USTR Prepares To Table Revised TPP Tobacco Proposal, Briefs Congress, *Inside U.S. Trade*, August 16, 2013.

²¹ KORUS, art. 22:3 (Cooperation).

²² KORUS, art. 22:7 (Consultation).

and other members of the public on the matter in order to draw on a broad range of perspectives.

3. Each Party shall:

(a) provide sufficient information in the consultations to enable a full examination of how the matter subject to consultations might affect the operation of this Agreement; and

(b) treat any confidential information exchanged in the course of consultations on the same basis as the Party providing the information.

4. A Party may request the other Party to make available during consultations under this Article personnel of its government agencies or other regulatory bodies who have expertise in the matter subject to consultations.

b. Legal significance

- (1) Assuming that the draft TPP dispute chapter is modeled on the KORUS chapter, it already requires Parties to cooperate and consult on “any matter,” and it requires one party to consult in response to a request from another party. In the consultation process, it requires parties to provide information for a full examination, including consultation with their expert personnel and regulators.
- (2) USTR’s proposal is redundant with these pre-existing consultation provisions except for these differences:
 - (a) The “matter” in dispute is more specific, namely a tobacco-control measure.
 - (b) The health authorities from both countries must consult with each other and discuss whether the challenged measure is appropriate.
- (3) The only consultation step that might not occur in the absence of USTR’s proposal is the consultation between the health authorities of both countries. This expansion of participants might produce a more balanced conversation, but that would depend on the standard for “appropriateness,” which USTR has not publicly disclosed, and whether the consultation is transparent. An agreement by health authorities from both Parties that a measure is appropriate *could* be legally significant, but only if they agree that a measure is appropriate, and only if their joint position blocks a dispute or creates deference or a presumption in favor of a measure.²³ That is not part of USTR’s proposal, however. Nor is it proposed that the health consultation be transparent with a public report of findings or disagreements. Without transparency, the consultation becomes a black box. There is no way to know whether the health authorities have a meaningful dialogue or a staged exchange of scripted positions.

²³ For an example of consultation that is legally significant, see KORUS article 23.3 on treatment of tax measures:

- *Tax conventions* – KORUS art. 23.3.2(a) provides, “In the event of any inconsistency between this Agreement and any such convention, that convention shall prevail to the extent of the inconsistency.” To implement that deference, art. 23.3.2(b) provides, “In the case of a tax convention between the Parties, the competent authorities under that convention shall have sole responsibility for determining whether any inconsistency exists between this Agreement and that convention.” While this article is vague in some respects, at the very least, it empowers tax authorities to consult, and if they agree, to block a dispute based on KORUS from going forward on grounds that the convention is inconsistent with KORUS.
- *Expropriation claims* – Before filing a claim for expropriation based on a tax measure, KORUS art. 23.3.6(b) requires an investor to first notify tax authorities of both countries. If both tax authorities agree that the measure is not an expropriation, the claim may not go forward.

- (4) Compared to the consultation process that already exists, USTR's proposal carries no legal weight or significance. Nor does USTR's proposal apply to disputes in which a private investor (e.g., a tobacco company) challenges a tobacco-control measure.²⁴

3. Conclusion

The U.S. proposal manages to insert the word *tobacco* into the TPPA without legal effect. But even if the proposals had marginal value, it would only be in the context of exceptions that do not even apply to investor-state arbitration, the most significant threat of litigation. Countries invoke exceptions to defend their measures – after they are found to violate a trade rule – at the end of a multi-year and multi-million dollar litigation process. While the GATT/GATS health exception provides an opportunity for governments to defend a health measure, it requires litigation of each element of necessity and the chapeau tests. Win or lose, the threat of costly litigation has long been part of the tobacco industry's strategy to defeat, divert, or delay implementation of tobacco-control measures. The more elegant alternative to a complex exception is to simply exclude ("carve out") tobacco-control measures from the TPPA. A carve out is better protection than an exception because it would preclude litigation.

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²⁴ Note that the consultation process in KORUS for tax measures does apply to investors' expropriation claims.

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