

Job No. 5929

Working Party on Domestic Regulation

19 March, 2001

**APPLICATION OF THE NECESSITY TEST: ISSUES FOR CONSIDERATION***Informal Note by the Secretariat***I. INTRODUCTION**

1. At the request of the Working Party on Domestic Regulation, the Secretariat has prepared this Note on necessity tests in existing WTO agreements, focusing on the Agreement on Technical Barriers to Trade (TBT) and the Agreement on the Application of Sanitary and Phytosanitary Measures (SPS).

2. The necessity test -- especially the requirement that regulatory measures be no more trade restrictive than necessary -- is the means by which an effort is made to balance between two potentially conflicting priorities: promoting trade expansion versus protecting the regulatory rights of governments.

3. The GATS preamble specifically recognizes "the right of Members to regulate, and to introduce new regulations, on the supply of services within their territories in order to meet national policy objectives and, given asymmetries existing with respect to the degree of development of services regulations in different countries, the particular need of developing countries to exercise this right".<sup>1</sup> At the same time, the GATS preamble also recognizes "the growing importance of trade in services for the growth and development of the world economy", and aims "to establish a multilateral framework of principles and rules for trade in services with a view to the expansion of such trade under conditions of transparency and progressive liberalization".

4. Acknowledging these objectives, GATS Article VI:4 specifies that Members shall develop any necessary disciplines to ensure that "measures relating to qualification requirements and procedures, technical standards and licensing procedures do not constitute unnecessary barriers to trade in services." Sub-paragraph (b) of Article VI:4 further specifies that such disciplines shall aim to ensure that regulatory measures are "not more burdensome than necessary to ensure the quality of the service".

**II. EVOLUTION OF NECESSITY TESTS IN WTO AGREEMENTS****TBT Agreement**

5. Article 2.2 of the TBT Agreement contains a necessity test for technical regulations and standards:

"Members shall ensure that technical regulations are not prepared, adopted or applied with a view to or with the effect of creating unnecessary obstacles to international trade. For this purpose, **technical regulations shall not be more trade-restrictive than necessary to fulfil a legitimate objective, taking account of the risks non-fulfilment would create.** (emphasis added) Such legitimate objectives are, *inter alia*: national security requirements; the prevention of deceptive practices; protection of human health or safety, animal or plant life or health, or the environment. In assessing such risks, relevant elements of consideration

<sup>1</sup> In the goods context, respect is also given to legitimate policy objectives.

are, *inter alia*: available scientific and technical information, related processing technology or intended end-uses of products."

6. Article 2.3 of the TBT Agreement contains another major provision, i.e. "Technical regulations shall not be maintained if the circumstances or objectives giving rise to their adoption no longer exist or if the changed circumstances or objectives can be addressed in a less trade-restrictive manner". (emphasis added) Article 5 of the TBT Agreement also includes a necessity test, as well as a number of practical administrative requirements, in regard to conformity assessment.

7. The current necessity test in Article 2.2 was added during the Uruguay Round negotiations.<sup>2</sup> The previous Agreement on Technical Barriers to Trade of the Tokyo Round Agreements had instead contained the following provision (Article 2.1):

"Parties shall ensure that technical regulations and standards are not prepared, adopted or applied with a view to or with the effect of creating unnecessary obstacles to international trade. Furthermore, products imported from the territory of any Party shall be accorded treatment no less favourable than that accorded to like products of national origin and to like products originating in any other country in relation to such technical regulations or standards. They shall likewise ensure that neither technical regulations nor standards themselves nor their application have the effect of creating unnecessary obstacles to international trade." (emphasis added)

8. The main change to the TBT text was the requirement that government regulations meet a legitimate objective, thereby clarifying and strengthening the prohibition against creating unnecessary obstacles to trade. As noted in *An Analysis of the Proposed Uruguay Round Agreement, with Particular Emphasis on Aspects of Interest to Developing Economies* (MTN.TNC/W/122, 29 November 1993, p. 69), "The Uruguay Round Agreement on Technical Barriers to Trade (TBT) clarifies and expands upon the Tokyo Round Agreement, but does not fundamentally alter its objectives or principal obligations."<sup>3</sup>

#### SPS Agreement

9. Articles 2.2 and 5.6 of the SPS Agreement contain necessity tests in respect to sanitary and phytosanitary measures:

"Members shall ensure that any sanitary or phytosanitary measure is applied only to the extent necessary to protect human, animal or plant life or health, is based on scientific principles and is not maintained without sufficient scientific evidence, except as provided for in paragraph 7 of Article 5." (Article 2.2 -- emphasis added)

"Without prejudice to paragraph 2 of Article 3, when establishing or maintaining sanitary or phytosanitary measures to achieve the appropriate level of sanitary or phytosanitary protection, Members shall ensure that such measures are not more trade-restrictive than

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<sup>2</sup> For example, the proposal by Canada (MTN.GNG/NG8/W/77, 8 May 1990, p. 2) contained the provision that Parties shall ensure that technical regulations and standards "do not contain requirements that are greater than necessary to meet objectives consistent with this Article and the specific circumstances giving rise to their adoption". This formulation was replaced by the current wording in a July 1990 draft text. ISYS searches, and talks with WTO staff, have confirmed there is little written information on the discussions related to the TBT and SPS necessity tests.

<sup>3</sup> The document further notes (p. 70), "The Uruguay Round Agreement improves on the Tokyo Round Agreement by (i) tightening obligations to ensure that technical regulations and conformity assessment procedures to not create unnecessary non-tariff barriers to trade; (ii) extending those obligations more clearly to sub-national government authorities and non-governmental bodies; (iii) encouraging mutual recognition of other countries' own technical regulations, standards, and conformity assessment procedures; and (iv) imposing new disciplines on voluntary standard setting".

required to achieve their appropriate level of sanitary or phytosanitary protection, taking into account technical and economic feasibility.<sup>4</sup> (Article 5.6 -- emphasis added)

10. The origin of the provision in the SPS Agreement that measures should be the minimum necessary and the least restrictive of trade is apparently the European Communities' *Working Paper - Drafting of an Appropriate Framework of Rules for Sanitary and Phytosanitary Regulations* (MTN.GNG/NG5/W/56, 20 April 1988), stating,

"National regulations should systematically take the form least restrictive to trade, whilst ensuring an equal level of health protection. Consideration should be given to the possibility and appropriateness of limiting protective measures to the minimum strictly necessary to guard against actual risk occurring in modern conditions of production and trade".<sup>5</sup> (emphasis added)

#### GATS Annex on Telecommunications

11. Paragraph 5 (e) of the GATS Annex on Telecommunications states, "Each Member shall ensure that no condition is imposed on access to and use of public telecommunications transport networks and services other than as necessary:

- (i) to safeguard the public service responsibilities of suppliers of public telecommunications transport networks and services, in particular their ability to make their networks or services available to the public generally;
- (ii) to protect the technical integrity of public telecommunications transport networks or services; or
- (iii) to ensure that service suppliers of any other Member do not supply services unless permitted pursuant to commitments in the Member's Schedule. (emphasis added)

#### GATT Article XX / GATS Article XIV

12. Article XX of the GATT, the General Exceptions, requires that measures adopted by Members as exceptions to the agreement be "necessary" to achieve certain policy objectives. A similar necessity test is also contained in Article XIV of the GATS (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 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:

- (a) necessary to protect public morals or to maintain public order;
- (b) necessary to protect human, animal or plant life or health;

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<sup>4</sup>"For purposes of paragraph 6 of Article 5, a measure is not more trade-restrictive than required unless there is another measure, reasonably available taking into account technical and economic feasibility, that achieves the appropriate level of sanitary or phytosanitary protection and is significantly less restrictive to trade."

<sup>5</sup>The Nordic Countries proposed draft SPS Agreement (MTN.GNG/NG5/WGSP/W/21, 28 May 1990) also contained the statement, "When preparing sanitary or phytosanitary regulations, parties shall choose to present the necessary requirements in the ways which are least trade restrictive, except in cases when this, for technical or economic reasons, is not feasible".

- (c) **necessary to secure compliance with laws or regulations which are not inconsistent with the provisions of this Agreement ...**" (emphasis added)

#### Contrasts between Necessity Tests

13. In comparing the various necessity tests, it may readily be observed that nearly all of the legitimate objectives specified in the TBT and SPS Agreements are already covered under GATS Article XIV (e.g. protection of human, animal or plant life or health).<sup>6</sup> Therefore, the task of the Working Party might be to focus primarily on new policy objectives unrelated to these existing provisions.

#### Application of the Necessity Test in Dispute Settlement

14. The necessity test has two main aspects of relevance to the Working Party on Domestic Regulation: the first aspect is the general requirement that regulations not be more trade restrictive than necessary; the second aspect is to examine whether an individual measure is actually necessary to achieve the specified legitimate objective.<sup>7</sup>

15. As has been the practice to date in the goods sector, future dispute settlement cases in the services area will undoubtedly be resolved on a case-by-case basis. W/96 presents a summary of relevant panel decisions involving necessity tests: further detailed information can be found in the *WTO Guide to GATT Law and Practice* (especially Volume I, 1995 Edition, pp. 562-596). Many current panel cases also make reference to necessity provisions.

#### Information from WPPS discussions

16. The necessity test initially contained in the accountancy disciplines was revised, to a limited extent, during the early stages of the editing and drafting process in the Working Party on Professional Services (WPPS). Based on Members' suggestions, the initial wording was:

"Members shall ensure that such measures are not more trade-restrictive than necessary to fulfil a legitimate objective, taking account of the risks non-fulfilment would create. Legitimate objectives include, *inter alia*, consumer protection; ensuring the quality of the service; ensuring the integrity of the profession; and preventing a default on service contracts". (Job No. 5711, 10 October 1997)

17. In the third revision of the disciplines (Job No. 6534, 14 November 1997), the phrases "taking account of the risks non-fulfilment would create" and "preventing a default on service contracts" were deleted, while "professional competence" was added to the listing of legitimate objectives. In the fourth revision (Job No. 246, 13 January 1998), the objective "protection of consumers" was further specified as "which includes all users of accounting services and the public generally".

18. Among the (informal) comments made by Members during WPPS discussions, one delegation noted that Article VI:4 contains the wording "to ensure the quality of the service", and wondered if "consumer protection" could actually be considered a subset of this. Another Member was of the view that "consumer protection" would have been sufficient as the sole legitimate objective specified in the accountancy disciplines. Some delegations had wished to replace the "consumer

<sup>6</sup>S/C/W/96, *Article VI:4 of the GATS: Disciplines on Domestic Regulation Applicable to all Services* (1 March 1999, para 22 also points out that measures taken under Article XIV exceptions can be discriminatory and inconsistent with GATS obligations; measures taken under Article VI:4 cannot.

<sup>7</sup>As noted in WTO document S/WPPS/W/9, *The Relevance of the Disciplines of the Agreements on Technical Barriers to Trade (TBT) and on Import Licensing Procedures to Article VI:4 of the General Agreement on Trade in Services* (11 September, 1996, p. 5), "A measure that has the effect of restricting trade can be considered "necessary" only if there is no alternative measure less disruptive of trade which a Member may reasonably be expected to employ to achieve the same policy objective".

protection" objective with "public interest". In the end, however, many Members felt this term was too broad and difficult to define precisely. As for the deleted phrases, "taking account of the risks non-fulfilment would create" was not considered useful in the services context, while "preventing a default on service contracts" was considered to be a subset of consumer protection.

#### General applicability of legitimate objectives from the accountancy disciplines

19. The legitimate objectives specified in the accountancy disciplines created by the WPPS (S/L/64, 17 December 1998) included, *inter alia*: 1) The protection of consumers (which includes all users of accounting services and the public generally); 2) The quality of the service; 3) Professional competence; and 4) The integrity of the profession.

20. Of these four specified objectives, the protection of consumers and (ensuring) the quality of the service are the most obviously applicable at the general level.<sup>8</sup> The definition of consumer given in parentheses in the accountancy disciplines could potentially be used in general disciplines with only minor modification, e.g. "which includes the users of a particular service and the public generally". The third and fourth objectives specified in the accountancy disciplines are widely, but not universally, applicable.

#### Additional examples of potential legitimate objectives

21. As noted above, the legitimate objectives listed in the TBT and SPS agreements would generally not be useful for the development of general disciplines in services. W/9 (p. 6) mentioned "safeguarding the public interest", but a similar provision was rejected earlier by the WPPS.

22. Among the objectives and rationales for regulatory measures stated in TBT notifications in 1998 were the following which may be useful for consideration by the Working Party: "protection of the environment"; "quality requirements"; "harmonization"; "lowering or removal of trade barriers"; "cost savings"; and "increasing productivity".<sup>9</sup>

23. Potential additional legitimate objectives for consideration by the Working Party might include "economic efficiency" (or perhaps "promoting competition"), "administrative efficiency", or "economic development".<sup>10</sup> A recent WTO ERAD research report (TISD-98-02), after noting the panel cases where "reasonably available" alternatives are discussed, asks how the set of measures which are reasonably available could be defined. An option suggested is use of the efficiency principle, i.e. "it may well be politically more acceptable to countries to accept international obligations which give primacy to economic efficiency in the attainment of objectives".

#### Potential role of international standards

24. As noted in W/9 (p. 6), "In principle, all technical standards are meant to serve legitimate policy objectives, a concept that has already been codified in the TBT agreement and is also inherent in the underlying logic of Article VI:4".<sup>11</sup> GATS Article VI:5(b) specifically states that "In

<sup>8</sup>It should be pointed out that consumer protection is a very broad concept, and potentially subject to abuse for protectionist purposes.

<sup>9</sup>*Fourth Annual Review of the Implementation and Operation of the Agreement (G/TBT/7, 3 March 1999, p. 9)*. Information on determining whether a regulation is necessary is contained in *Requirements of the Agreement on Technical Barriers to Trade Concerning the Preparation, Adoption and Review of Technical Regulations (G/TBT/W/44, 13 June 1997, pp. 4-5)*, as well as in *First Triennial Review of the Operation and Implementation of the Agreement on Technical Barriers to Trade (G/TBT/5, 19 November 1997, pp. 7-8)*.

<sup>10</sup>In this regard, Members may find it useful to review WTO document S/C/W/97, *International Regulatory Initiatives in Services* (1 March 1999), which surveys the predominant regulatory issues, as well as the current international regulatory initiatives, at the sectoral level.

<sup>11</sup>W/9 also notes that, although there is no definition of technical standards in the GATS, the work of the WPPS in the accountancy sector suggests that standards in the area of trade in services apply not only to the

determining whether a Member is in conformity with the obligation under paragraph 5(a), account shall be taken of international standards of relevant international organizations<sup>12</sup> applied by that Member". Considering that Article VI:5 is a temporary provision, i.e. pending the entry into force of disciplines developed under Article VI:4, Members may wish to consider making a reference to international standards a permanent part of the necessity test of any generally applicable disciplines.

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technical characteristics of the service, but also the rules according to which the service must be performed (i.e. product and performance standards).

<sup>12</sup>"The term "relevant international organizations" refers to international bodies whose membership is open to the relevant bodies of at least all Members of the WTO."