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Volume 3 Number 2, 2002/p.163-175 esteyjournal.com

The Estey Centre Journal of
International Law and Trade Policy

Who Should Make the Rules of Trade? – The Complex Issue of Multilateral Environmental Agreements

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In recent years, governments have negotiated a number of Multilateral Environmental Agreements (MEAs) that include clauses regarding trade measures that conflict with their WTO obligations. As yet, there has been no formal dispute regarding which obligations should prevail, but the threat of conflict is perceived to be sufficiently grave for the parties to the Doha Ministerial to agree to examine the issue. Those who have strong preferences for environmental amenities have put considerable effort into fostering MEAs and are lobbying hard for them to prevail over the WTO in their areas of competence. The current lack of transparency caused by conflicting rules increases the degree of risk perceived in the international commercial environment. As MEAs allow trading partners to impose trade barriers on ratifying partners when the WTO rules would not, a perverse set of incentives is created that may lead to sub-optimal levels of environmental protection as well as sub-optimal amounts of investment in trade-related activities. The use of trade measures in MEAs is examined and suggestions are provided for removing the conflicting rules of trade.

Keywords: Doha, MEA, negotiations, ratification, trade measures, WTO

> …trade rules must: ensure deference to multilateral environmental agreements (MEAs) when there are conflicts between trade rules and trade-related provisions of MEAs.
>
> Center for International Environmental Law, Consumer's Choice Council, Defenders of Wildlife, Earthjustice Legal Defense Fund, Friends of the Earth, Institute for Agriculture & Trade Policy, National Wildlife Federation Natural Resources Defense Council, Sierra Club, World Wildlife Fund[1]
>
> With a view to enhancing the mutual supportiveness of trade and environment, we agree to negotiations, without prejudging the outcome, on: (i) the relationship between existing WTO rules and specific trade obligations set out in multilateral environmental agreements (MEAs).
>
> The Doha Ministerial Declaration[2]

One is sometimes led to wonder whether there is anyone "minding the store" when it comes to international negotiations. While it is understandable that in large government bureaucracies the left hand may not know what the right hand is doing, it is hard to imagine that this can be the case over a large number of countries that are collectively engaged in long-term, complex negotiations. In this light, it seems surprising that a large number of governments of countries that are members of the WTO have also signed a variety of Multilateral Environmental Agreement (MEAs) that have trade provisions that contradict in fundamental ways their WTO commitments. For example, did it not occur to at least one of the 140-odd countries that negotiated The Cartegena Protocol on Biosafety to the Convention on Biological Diversity – hereafter the Biosafety Protocol (BSP) – to raise the point that the process-based labelling regime for transboundary movements of the products of biotechnology they were agreeing to was in direct conflict with WTO rules that only allow labelling based on product characteristics?[3]

Of course, the reality is that they did realize what they were doing but, given the political pressure to come up with an agreement, signed the protocol anyway; leaving the inconsistencies to be sorted out later (Falkner, 2001). If this were an isolated incident, it could simply be written off as an anomaly. The practice of governments signing separate international agreements that have inconsistent and conflicting clauses is, however, sufficiently common for there to be a well established principle of international law to deal with the problem (Isaac et al., 2002). As a general principle,

in international law, when there is a dispute between two states that have both signed two treaties with conflicting clauses in the same subject area, it is the newer of the treaties that prevails. According to the Vienna Convention on the Law of Treaties:

Article 30:

1. Subject to Article 103 of the Charter of the United Nations, the rights and obligations of States parties to successive treaties relating to the same subject matter shall be determined in accordance with the following paragraphs.

…

3. When all the parties to the earlier treaty are parties also to the latter treaty but the earlier treaty is not terminated or suspended in operation under article 59, the earlier treaty apples only to the extent that its provisions are compatible with those of the latter treaty.

While the law looks relatively straightforward, the reality is much more complex and serves to make the relationship between the WTO and MEAs opaque. For example, the Convention on Biological Diversity (CBD), an MEA, was signed in 1992 and clearly post-dates the 1947 General Agreement on Tariffs and Trade. However, the GATT has built-in renegotiation provisions so that, in its latest iteration, the Uruguay Round provisions of 1994 prevail and post-date many of the MEAs. Of course, there is a new set of negotiations at the WTO which, when completed, will post-date all MEAs that exist at the current time. From the point of view of the environmental movements that have been putting considerable effort into fostering MEAs, the results of these negotiations could negate all their work. According to Caldwell (1998),

> The major difficulty associated with relying on the hierarchical treaty argument is that the later-in-time provision of the Vienna Convention will not adequately serve the GATT/WTO regime or future MEAs. For example, the GATT/WTO regime has a tradition of negotiating additional agreements in new areas of trade liberalization over the course of several years. The latest adoption of the Uruguay Round Final Act clearly places the GATT/WTO regime as the later-in-time treaty in relation to many of the current MEAs. Similarly the negotiation of future MEAs may result in their achieving priority over the GATT/WTO regime. The final result would be a patchwork of differing treaty priorities and minimal clarification of the relationship between the GATT/WTO regimes and the MEAs.

The Vienna Convention on the Law of Treaties also states in Article 30 (2):

> When a treaty specifies that it is subject to, or that it is not to be considered incompatible with, an earlier or later treaty, the provisions of that other treaty prevail.

This provision was clearly put in place to allow countries to specify which treaty would prevail if the later-in-time rule did not represent the intent of the contracting parties. In the case of some MEAs, the signatories were careful to ensure that the provision was thwarted. In the case of the BSP, the wording purposely obfuscates the relationship between the BSP and the WTO (Phillips and Kerr, 2000). The preamble to the BSP states:

> *Recognizing* that trade and environmental agreements should be mutually supportive with a view to achieving sustainable development,
>
> *Emphasizing* that this Protocol shall not be interpreted as implying a change in the rights and obligations of a Party under any existing international agreement,
>
> *Understanding* that the above recital is not intended to subordinate the Protocol to other international agreements.

The first paragraph provides no guidance if environmental agreements and trade agreements are not mutually supportive – as is clearly the case with the BSP and the WTO (Isaac et al., 2002). The second and third paragraphs of the preamble are in direct contradiction. The *Understanding* (third) paragraph suggests that any rules the BSP makes regarding trade in the products of biotechnology would not have to defer to WTO rules. On the other hand, the *Emphasizing* (second) paragraph implies that a signatory can refer to existing WTO obligations regarding rules for trade in the products of biotechnology (Phillips and Kerr, 2000). Such obfuscation was not accidental – it allowed contending parties to the BSP to claim that the protocol reflected their point of view and that they had not given anything unacceptable away in the negotiations.

Thus far we have been assuming that the contending parties have both signed each conflicting agreement. The problem is further complicated, however, when memberships do not overlap. The Vienna Convention on the Law of Treaties is, however, clear on this point. Article 30 (4) states:

> When the parties to the latter treaty do not include all the parties to the earlier one
>
> (b) as between a State party to both treaties and a State party to only one of the treaties, the treaty to which both States are parties governs their mutual rights and obligations.

This calls up the spectre of different sets of rules for different trading partners. In the case of the BSP, to which the United States cannot belong,[4] this problem has considerably vexed the EU, which would prefer to have its trade regime for biotechnology governed by the BSP rather than the WTO. In spite of the clear statement of the Vienna Convention's Article 30 (4), the EU has been attempting to have the trade provisions of MEAs apply to non-signatories as well as those countries that have signed (*Inside US Trade*, March 29, 2002).

The possibility of multiple rules for trade in the same commodity creates a perverse set of economic incentives. The reason MEAs' trade rules are contentious is that they typically allow countries to impose trade barriers in a more restrictive manner than is the case if WTO commitments are complied with. This means that an exporting country that signs the same MEA as an importer faces stricter import rules than an exporting country that does not sign the MEA. In effect, the latter country receives preferred access. This has interesting ramifications for future MEAs and any existing MEAs that have not come into force. Typically, MEAs are negotiated and then must be ratified by a number of countries prior to coming into force. For example, the BSP has been negotiated but it must be ratified by 50 countries before it comes into effect. Hence, there may be considerable strategic trade value for a country in championing the completion of negotiations and then encouraging other countries to ratify the agreement, but not to ratify the MEA at home. Once it comes into force, non-ratifying countries enjoy preferred access to markets relative to those countries that have ratified.

Given that MEAs are put in place to enhance environmental amenities, the hope of those who promote them is that the agreements will encourage countries that give a lower priority to their environment to "step up to a higher bar". Typically then, the

countries that will be early ratifiers of an MEA will be those that give a higher weight to their environment, and likely can more easily conform to the higher standard. Countries that value their environment less (and trade more) will be less likely to ratify. As a result, the goal of raising environmental standards in countries that most need to will be thwarted.

Of course, if countries that might be inclined to ratify feel that their competitiveness in export markets is threatened by those that will not comply, then they may be less inclined to ratify the MEA. The result is an increased probability that the MEA will not come into force. Hence, inconsistencies between the WTO rules of trade and those of MEAs may be a prescription for failure of the latter. They increase both the probability that an agreement will be reached in the negotiation stage and that all the efforts of the proponents of stricter environmental regimes will be for naught.

Even if an MEA is signed by two participants, the MEA may still be sufficiently flawed that disputes between signatories end up at the WTO. Interpretations of the rules of trade are often the subject of disputes. One only has to look at the docket of the WTO dispute panels. Governments have not, however, given MEAs dispute settlement mechanisms. Hence, if there are disputes over the trade provisions of MEAs, governments will have no mechanism to have them adjudicated. This would appear to give importers a virtual *carte blanche* to put import restrictions in place. Of course, much of the history of the GATT/WTO revolves around putting limits on the ability of governments to act arbitrarily. The absence of dispute mechanisms reduces the credibility of the MEAs as viable international mechanisms and will lead countries to revert to the WTO dispute system for the resolution of trade issues. WTO panels, however, must decide disputes according to WTO rules (Isaac et al., 2002).[5]

The current state of affairs regarding the relationship between MEAs and the WTO is clearly sub-optimal from the point of view of those most directly affected. The incentive structure is biased against the successful acceptance of MEAs with trade provisions, meaning that those who wish stronger protection for the environment will not be satisfied. Those with an interest in investing in international commercial activities find the international trading environment more risky due to competing sets of rules and a general lack of transparency. This reduces the incentive to invest in these activities. The blame lies directly on the shoulders of governments. Their unwillingness to ensure consistency between the trade commitments in different agreements has led to the current institutional failure. The issue came to a head at the WTO Ministerial in Seattle. As a result, at the Doha Ministerial it was agreed that the

WTO's Committee on Trade and the Environment (CTE) would attempt to find a solution to the problem.

Currently, there are approximately 20 MEAs that have clauses dealing with the regulation of international trade, many of which do not conform to WTO norms (Belcher, et al., 2001). In some cases there are both sufficient consensus among the parties and sufficient overlapping memberships that there have been no difficulties, even if the rules of the WTO conflict with the trade provisions of the MEA. Three such examples include the Convention on International Trade in Endangered Species (CITES), The Basel Convention on the Transboundary Movement of Hazardous Wastes and Their Disposal, and the Montreal Protocol on Substances that Deplete the Ozone Layer (Isaac et al., 2002). As yet, none of these have been challenged at the WTO. This is not surprising given the large number of ratifications and the small amounts of trade affected. In the case of the BSP and Convention on Biodiversity, the quantity of trade affected will be substantial and there is little consensus on the issues. Thus, it can not be assumed that the inconsistencies can be safely ignored.

The CTE does not have an easy task ahead of it. The WTO has consistently said that it believes that MEAs are the correct venues for devising environmental regulation – a stance that is considerably at variance with the power-hungry, grasping image with which environmental NGOs like to portray it. The mandate given the CTE at Doha is also weak because it is prefaced with the phrase "without prejudging the outcome" which is code for agreeing to enter into negotiations without committing to finding an acceptable compromise. Can an acceptable compromise be found? To answer that question requires a close examination of the rationale for having trade provisions in MEAs.

Four distinct reasons for using trade measures to achieve environmental goals can be identified. They are: (1) coercion – using trade measures pro-actively as a means of coercing governments or private firms into altering their environmental policies or practices; (2) market failure – using trade measures to correct market failures surrounding the environment; (3) protectionism – using trade measures to provide relief from international competition based on lower environmental standards; and (4) preferences of civil society – using trade measures to limit market access for goods or services associated with environmental practices considered unacceptable. Each of these will be dealt with in turn.

Trade sanctions are a time-honoured method of international coercion. They are used in attempts to induce governments to change behaviours which are deemed to be unacceptable. Trade sanctions lie in the middle ground of coercion between military

action and diplomacy (in economists' terms, moral suasion). Environmental activists in developed countries have strongly held preferences. Through their NGO organisations they are formidable lobbyists in their own countries. They are often frustrated, however, by their inability to influence the behaviour of foreign governments on environmental issues. Some environmental NGOs are advocates of using trade sanctions to achieve environmental ends. While developing countries often characterise this coercion as thinly disguised neo-colonialism and a direct violation of their sovereignty, many environmental NGOs remain convinced of the morality of using sanctions as coercive measures (Kerr, 2001). The evidence on sanctions suggests, however, that they are not particularly effective and may actually provide a perverse set of incentives that encourage the continuation of the activities at which sanctions are aimed (Kerr and Gaisford, 1994). Hence, it seems that trade measures should not be allowed in MEAs for coercive reasons. They simply impose a distortion on markets without any assurance that they will achieve their goal. Direct negotiations to solve the problem, however difficult, are a preferred policy option.

Trade measures are almost always a sub-optimal method of correcting market failures (Leger et al., 1999). Trade policy measures such as tariffs, however, may have a role to play in correcting environmental-based market failures such as transboundary externalities. This is particularly the case when the negatively affected country is unable to reach an agreement with the other country to correct the market failure using more direct means such as the other country's regulations, subsidies or tax regime. The use of trade measures for this reason is unlikely to be extensive because of their inherent inefficiency. Alternatives to trade measures include financial transfers from those who benefit from pollution abatement to those who pollute, internationally traded pollution permits, and incentive schemes to protect natural resources (Kerr, 2001). Well-designed environmental policy alternatives to trade measures will mean that the global economy can achieve its environmental goals with less welfare loss.

Domestic firms seeking protection from foreign competition, while they may lose some battles, are never vanquished. Over the last half of the 20th century traditional protectionists' arguments were systematically discredited intellectually, and protection, when it is still granted, is most often directly identified with the special interest which requests it (Kerr and Perdikis, 1995). This makes protectionist policies more difficult to defend. Protectionists greatly covet the mantle of intellectual legitimacy. Recently, protectionist vested interests have begun to argue that unfair foreign competition arises due to less stringent (and, hence less costly for their foreign competitors to comply with) environmental regulations and/or enforcement of those

regulations (Clement et al., 1999). Similar arguments are being made regarding lower labour standards in developing countries. These arguments were endowed with a measure of legitimacy by the inclusion of side agreements on environment and labour standards in the NAFTA.

While these traditional, but newly dressed up, protectionist arguments have been able to gain some credence on the political front, they have yet to gain intellectual credibility. Economists argue that environmental regulations and the quantity of resources dedicated to their enforcement tend to reflect the underlying social preferences of a society. Developing countries simply weight protection of the environment less heavily than rich countries. As with lower wages, in part this simply reflects their lower level of economic development. As a result, the lower costs associated with complying with environmental regulations are simply part of what is called a country's comparative advantage. As Krissoff et al. (1996) state:

> Economists see little justification for trade measures designed to correct for these cost differences, especially if these differences reflect underlying contrasts in social preferences, resource endowments, and environmental conditions (p. 30).

Finally, the inclusion of trade measures in MEAs arises from individuals who hold strong preferences for environmental goods and services even if they don't directly consume them. Their strongly held preferences manifest themselves in the desire to make personal consumption or social choices that they consider environmentally friendly. They may ask that imports be labelled so that they can make informed choices on the basis of either product characteristics (tropical timber) or production methods (dolphin friendly tuna). They may want exporters to take responsibility for packaging materials.

They may also not be content to restrict the expression of their preferences to being enabled to make an intelligent personal consumption decision but rather may wish to impose their preferences on others. They may lobby their politicians to ban imports of furs caught using leg-hold traps or to keep imported genetically modified organisms out of their environment. It is naïve to think that the granting of protection in these areas can be confined to creating conditions where consumers can make an informed choice and then letting the market decide. This is the intellectual equivalent of suggesting that if consumers wish U.S. automobile manufacturers to survive they simply will not buy Japanese cars. These arguments did not prevent politicians from providing protection to U.S. automobile manufacturers and they will not prevent the extension of protection in response to environmental lobbying.

When the GATT was established, no one but domestic producers was expected to ask for protection. The GATT, and subsequently the WTO, was established exclusively to limit the ability of governments to extend protection to domestic producers. One of the central pillars of this restraint was that trade barriers could not be put in place on the basis of the processes used in production. There was a very good reason for this. If trade barriers could be put in place on the basis of the technology used in production, it would be relatively simple to devise ways of discriminating against foreign products not produced in the same way as competing domestic products (e.g., trade barriers against cloth produced on hand looms in developing countries that was successful in competing with mechanized production in developed countries). The process rule is a good rule when domestic producers are the only group asking for protection (Gaisford et al., 2001).

Environmentalists (and consumers), on the other hand, are often asking for protection because they object to the processes used in production. Their requests are not confined to environmental protection, but extend to the issues of child labour, animal welfare standards, biotechnology, organic production, dolphin friendly fishing methods, and so forth. The WTO has not been able to deal adequately with the production process issue (Perdikis and Kerr, 1999). As a result, those seeking protection have had to find other venues, including MEAs, to obtain the protection they desire. Those negotiating MEAs have been willing to accommodate trade barriers based on production processes.

It seems unlikely that the CTE will be able to accomplish its task. First, the member states need to deal directly with the question of accommodating non-producer demands for protection based on production processes. This will not be easy because it will require a method of determining the legitimacy of the request for protection and ensuring that the process cannot be captured by traditional producer-based protectionist interests (Perdikis and Kerr, 2001).

To return to the question of who should make the rules for trade, the simple answer is that it does not matter as long as there is a consistent set of principles. The rules of trade, however, need to be concerned with trade facilitation and not enlisted to assist in the accomplishment of other goals. Hence, it would seem unwise to adopt the 1996 proposal to amend Article 20 of the GATT; the amendment would create a presumption that measures undertaken pursuant to an MEA would be viewed as "necessary to protect the environment" and thus compliant with the WTO rules as long as they were non-discriminatory and non-arbitrary *(Inside US Trade*, June 7,

2002). Given the range of reasons that trade barriers are sought, this proposal would give the framers of MEAs a virtual *carte blanche* to put trade barriers in place for coercive or protectionist purposes. It would seem far wiser to insist that any trade measures included in an MEA be consistent with WTO rules. This would centralize the development of trade rules and force WTO member states to deal with the production process issue directly. This centralization would remove the perverse incentives surrounding ratification of MEAs and increase the degree of transparency for those wishing to invest in trade-related activities.

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1. Principles for Environmentally Friendly Trade, on the website of the Center for International Environmental Law, May 2001, http://www.ciel.org/Publications/TAEprinciplesMay1601.pdf.
2. World Trade Organization, Doha WTO Ministerial 2001: Ministerial Declaration, 20 November 2001, www.wto.org/english/thewto_e/minist_e/min01_e/mindecl_e.htm.
3. This distinction is very important in the case of biotechnology because the final good produced using biotechnology may not have any product characteristics that differ from those of a good produced using conventional means. The two goods differ only in the process used to produce them. As labelling is likely to impose considerable costs related to monitoring, testing and supply chain segregation, these subtle differences in the rules of international trade can have significant impacts on the costs of engaging in international trade (Gaisford et al., 2001).
4. The United States is not in a position to join the BSP because it has not ratified the Convention of Biological Diversity (Isaac et al., 2002). Under Article 32.1 of the CBD "a State or a regional economic integration organisation may not become a Party to a protocol unless it is, or becomes at the same time, a Contracting Party to this convention."
5. In this vein, the EU has suggested that MEA provisions should be taken into account by WTO panels in the current WTO negotiations. There have been strong initial reactions by some countries against this suggestion (*Inside US Trade*, March 29, 2002).

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