

Defining the boundaries of WTO action on sustainable development

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SUSTRA

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ARCHITECTURE OF THE GLOBAL SYSTEM OF GOVERNANCE POSSIBLE RESEARCH AREAS:

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The following briefly describes possible research involving the relationship between the World Trade Organization (WTO) and sustainable development.

I. TRANSATLANTIC RELATIONS, THE WTO AND PUBLIC PREFERENCES

In recent months, relations between the European Union and the United States have deteriorated. While disagreement over how to proceed with Iraq remains at the time of writing by far the most turbulent of issues, sharp differences involving international environmental, human health and food safety policies run just as deep. The decision by the United States in early 2001 to reject the Kyoto Protocol contrasts sharply with the route taken not only by the EU, but also Canada, Russia and others in tackling climate change. Probably more disturbing for US-EU relations is the risk that differences over the use of food labels for genetically modified organisms (GMOs) foods will end up as a formal dispute in the World Trade Organization (WTO). In late 2002, the US cabinet agreed that just such a case should proceed.

It is unclear how such a case would be decided: WTO disputes are heard on a case-by-case basis. However, the prevailing wisdom is that the US would win the case, and loose public opinion not only in the EU, but also in the US itself. After all, isn't giving customers the freedom to choose what the US stands for, especially when organic foods are the largest segment of demand growth in the US – at 30 percent per year? At the same time, others argue that the EU might well win a GMO labeling dispute. (Howse and Marvradois)

In thinking about this case, one can look to the *EU Beef Hormones* Case for clues. That Panel and the Appellate Body of that case, in examining whether the EU ban conformed with provisions set out in the Agreement on Sanitary and Phytosanitary Measures (SPS), examined among other things the underlying scientific justification of the EU measures. In so doing, the WTO panel called upon six scientific experts to direct questions regarding scientific issues raised by the parties. From that evidence, the panel examined the scientific evidence presented by the EU in supporting its use of an import ban. The panel examined the EU interpretation of evidence, and concluded that that interpretation was neither justified nor did it reflect the majority view of scientific opinion, and that therefore, provided insufficient evidence to support the use trade measures. (Wirth)

Several troubling questions arise from the Beef Hormones case that might be of relevance to a GMO dispute. These include: Does the WTO have the competence to arbitrate disputes over differing risk assessment procedures? Some argue that for the WTO to arbitrate scientific disputes at all is a “disserve” to objectives of that institution. (Ward). The panel further raises questions about the role of minority scientific opinion in risk assessment procedures and policy outcomes, (Wirth) and reminds us of the discomfort trade policy has with the precautionary principle (by definition, based on incomplete scientific evidence or minority scientific opinion).

If these questions weren't enough, the case also raises more basic issues regarding the reach of WTO rules that now touch upon virtually every area of economic policy, and public preferences based on democratic will. (Woods, Howse)

For instance, are all public policies involving environmental protection, food safety or other priorities to be based on sound and complete science? What does that say about essentially non-rational public preferences expressed through democratic will? For example, if Europeans are skittish about consuming GMOs, for whatever reason – irrational perceptions about health

risks, or legitimate but incomplete doubts around the environmental effects of gene drift and pollution – then can the WTO overturn popular will?

From a governance perspective, one of the intriguing questions is the mandate of the WTO as perceived by the US and the EU in sorting out these thorny questions. In Beef Hormones, the US displayed a very high degree of comfort in the WTO's arbitrating a dispute around dueling science. That suggests a high degree of confidence by the US in assigning authority to the WTO to arbitrate a wide range of public policies. At least, this would be a reasonable conclusion. However, the US *perception* of the role of the WTO, as well as its stated understanding of the EU's understanding of that role, suggest an opposite conclusion. Robert Zoellick, the US Trade Representative, articulates the difference between the US and EU approach to WTO governance issues thus:

“The United States and the EU share a common aim of trade liberalization , but have pursued different approaches. In the lexicon of the EU, the United States is pressing to “deepen” the WTO by freeing trade across the core agenda of market access. The EU’s distinguishing agenda is to “widen” the WTO mandate by developing new rules to cover more topics...the EU sees the world through the lens of recent European experience: *it wants gradually to achieve a supranational system of governance for globalization.*” (emphasis added) (Economist)

Clearly, it is unclear how to square the above comment, with the deference the US played to the WTO in arbitrating probably the most thorny question for a trade panel: the scientific legitimacy of domestic policies. It is also unclear what Ambassador Zoellick, means in supporting a “deepening” as opposed to “broadening” of trade agendas. In the former area, the 2002 zero tariff proposal is obviously a move to deepen market access commitments. However, both the US and EU have been in step in also pushing for an expanding WTO agenda: the mandate now includes intellectual property rights and patent protection under the TRIPS agreement; investment, services – including linking proposals by the US and the EU in the GATS special sessions to domestic regulatory reform and the adoption of “pro-competitive” privatization policies in the telecommunications and other sectors -- as well as environment, labor, competition policy, the development agenda – the list goes on.

Obviously, this difference is partly a matter of political rhetoric: the US likes to think of itself as being an outsider of the multilateral system: remember the League of Nations? However, this time it looks like much more than rhetoric: the US has stated that if it does not get what it wants out of the WTO, then it will continue to negotiate bilateral and regional agreements. What this does to EU-US relations, public opinion about the WTO, as well as the future of the WTO itself, remains very much in question. It is likely that a GMO WTO dispute will push many of these questions, and underlying notions of governance, even more to the fore.

II. EXPANDING MANDATE AND GOVERNANCE QUESTIONS

In the past decade, there has been mounting criticism of the WTO. Generally, that criticism reflects two positions. First, there are those who contend that the WTO is not doing enough to support welfare enhancing objectives, including the goals of sustainable development. Civil society groups in particular have argued that the WTO has consistently missed welfare-enhancing and social policy objectives, in part because its governance structures are both opaque, and reflect narrow interests of trade liberalization. This criticism has led to charges that the WTO lacks legitimacy, and that reforms in governance would ensure a broader set of policy goals would be included in its mandate. (Esty, 2002)

Second, there are those who argue that the WTO risks diluting its core mandate by taking on social and welfare-related goals. By extending its mandate from lowering trade barriers applied at the border, to introducing rules governing economic policies – broadly defined – behind the

border, the WTO differs from its predecessor the GATT in pursuing deeper economic integration. The mandate of the WTO now comprises a long list of “trade and” issues, including development and capacity building from the Doha ministerial meeting of 2001, as well as the Singapore list of issues like investment, competition policy, core labor standards and others.

In some ways, the extension of the WTO mandate mirrors the broadening of agendas followed by both the World Bank and the International Monetary Fund in the 1980s. Then, both institutions prescribed a proliferation of policy objectives that developing countries had to follow as part of structural conditionality. This proliferation resulted in a clouding of the respective mandates between the Bank and the Fund, probably most sharply articulated by Stiglitz (2002).

The lack of clarity in the core mandate (Pauly, 2002) of the Fund and Bank is being repeated by the WTO. The issue becomes more complicated, because the proliferation of issues is taking place – not by accident – at the same time that the WTO has assumed near universal membership. Today, more than 170 countries are members of the WTO. With Russia’s expected accession in 2005, approximately 90 percent of the world’s population will be living under WTO rules.

This expansion of issues and membership has led to a kind of governance crisis within the WTO. As new issues are brought on, decision-making appears to be becoming paralyzed. Some have argued that current governance structures are increasingly inefficient, because they are too inclusive. (Ostry, 2002) Accordingly, proposals have been forwarded to narrow the governance structures in a way that allows more efficient decision-making. Various proposals have been forwarded in this regard, from reviving or reordering the “Green Room,” to having a smaller number of trade ministers from capitals participate in regular meeting. One practical problem with this arrangement is that developing country members are already hampered in Geneva by their inability to participate in all WTO committees and negotiations. (Blackhurst, 1999)

There are thus two sharply opposing views of the governance crisis facing the WTO: the critique from civil society that the WTO is *illegitimate*, because it is not embracing social welfare issues sufficiently. And the critique that, by widening its mandate and membership simultaneously, the WTO risks becoming *inefficient* as a decision-making body. (This observation does not include WTO dispute settlement.)

There are important differences between the WTO and the other Bretton Woods institutions. At the same time, the governance debate involving the World Bank and IMF is arguably more advanced, partly because it has been underway for so long. (Woods, Helleiner) A rich area of policy-relevant research is to draw lessons from the governance debate of the Fund and the Bank, particularly with regards the shift in the Fund’s view of policy sequencing, to examine possible lessons of relevance to the WTO.

III. THE WTO DOHA MANDATE

The Doha Ministerial Declaration of November 2001 has been widely viewed as a step forward, in two areas. First, it is regarded as formalizing or elevating the relationship between trade and environment, through the obligations set out in paragraph 31. Second, it embraces the notion more generally of sustainable development, through paragraph XX.

Discussions in the WTO around paragraph 31 need to be examined closely. Although early, they appear to be headed in the wrong direction, in terms of identifying practical measures by which the trading system can support environmental policy. In two of the three core areas – the relationship between Multilateral Environmental Agreements (MEAs) and environmental

labeling – the undercurrent of discussions has always been whether international environmental legal agreements and environmental labels run afoul of WTO rules. Current activities in the WTO Committee on Trade and Environment appear centered on devising “modalities for the exchange of information” between that institution and MEA Secretariats, and the use of trade measures between MEA parties. On the first area, the WTO and UNEP are facilitating an exchange of information between government officials regarding decisions taken *by them* in different international negotiations. One might imagine that information coordination would be better achieved at national capitals.

However, the real question is where information exchange is actually leading? The decade-long discussions in the WTO about the ability of MEAs to use trade measures has never been neutral. Instead, most WTO members have voiced concern about the ability of MEAs to apply trade and trade-related measures – particularly trade measures applied against non-parties -- as part of their menu of instruments to achieve environmental objectives.

It is unlikely that the WTO will constrain the use of trade measures in the Montreal Protocol, CITES or the Basel Convention. It is also likely that the consensus reached in 1996, in the Report of the Committee on Trade and Environment to the Singapore Ministerial Meeting, on the use of trade measures between MEAs, will be repeated. Then, WTO members acknowledged that disputes over the use of trade measures applied between parties ought to be heard within the dispute settlement apparatus of the MEA itself. Informally called the “consenting adults” clause, it basically stated the obvious.

However, the real question is whether the second part of that 1996 report – which addressed the question of trade measures applied against non-parties – has had any chilling effect on subsequent MEA negotiations? It does seem very clear that the Biosafety Protocol, the Conventions on Prior Informed Consent and Persistent Organic Pollutants, all included a WTO “trumping clause” (although the Biosafety Protocol also included the opposite language in its preamble stating that nothing in that accord would be “subordinate” to other international agreements.)

A quite different approach to the relationship between MEAs and the WTO involves identifying practical areas in which the trading system can assist in the implementation of MEAs. An opportunity is to increase coordination around notification procedures between the two regimes. The backbone of the daily operations of MEAs entails notification between parties. This includes prior informed notification and consent procedures in the Basel and PIC conventions, advanced information exchange in the Biosafety Protocol, export and import permits in CITES, Montreal, etc. Similarly, the daily functioning of the WTO is based on notifications, submitted by Members to assist exporters and customs officials keep track of domestic standards and regulations between trading partners. A practical approach is to find ways to reduce the overlap between notification systems of the WTO and MEAs, especially to assist developing countries. Already, parties to CITES and Basel and Montreal have submitted notifications to the WTO, under different Uruguay Round Agreements.

In January 2002, the revised Harmonized System (HS) of custom codes included new categories of 6-digit customs codes for some goods and services that are traded under conditions set out in MEAs. Hence, there is a basis for cooperation between the two regimes, to reduce administrative overlap, provide practical assistance to customs officials in developing countries, and shift the WTO-MEA discussions away from a fruitless discussion of “regime compatibility.”

The second Doha decision that warrants research involves accelerated liberalization of tariffs and non-tariff barriers for “environmental goods and services.” This decision has the potential to increase the availability of green goods in global markets. However, WTO Members appear to be narrowing the definition of environmental goods and services exclusively to

environmental technologies. This is a mistake in several ways. First, capital technologies for end-of-pipe pollution abatement strategies represents only one part of the environmental agenda. Increasingly, environmental actions involve integrated, upstream management systems designed to avoid pollution before it is generated. By isolating only capital technologies, the WTO not only risks ignoring 20 years of advancement in environmental policy. It could lead to a marginal price distortion between tariff-free environmental technologies, and relatively more expensive environmental services.

Second, focusing on environmental technologies ignores the remarkable progress that has been made in environmental goods, broadly defined. Today, consumers can find substitute environmental goods in household and commercial markets, from fax machines and computers to recycled paper and hybrid-zero or low-emission automobiles. The most logical way to differentiate environmental goods from their mainstream counterparts is through environmental labeling and certification schemes, the other agenda item in the Doha ministerial declaration. Labeling and certification represents among the most innovative experiments in governance, involving non-state actors in developing and developed countries. The WTO mandate involving tariff reductions *could* lead to marginally lower prices for green goods, compared to their mainstream counterparts. For progress to proceed here, the WTO should shift its approach to environmental labeling, from measures that are allegedly outside of WTO rules, to using labels as the basis for liberalization to proceed.

Third, and most important, the environmental goods and services decision has the potential to break the impasse between developing and developed countries on trade-environment discussions generally. However, to do this, WTO members need to broaden the definition of environmental goods and services beyond areas in which the US and EU have a comparative advantage in capital goods, to cover exports of interest to developing countries.

The Doha decision involving environmental goods and services finds its strongest link to the overarching intent of the Doha Development Round, involving increasing market access for developing countries. Among the areas in which developing countries face the highest market access impediments are agriculture, textiles and apparel. These are also areas in which developing countries have a comparative advantage in producing and exporting environmental goods, broadly defined. Take the case of coffee. Estimates suggest that 90 percent all coffee grown in Ethiopia, and 75 percent in Mexico, fall under the rubric of “sustainable coffee.” The reason is simple: almost all traditional, community farming in developing countries lacks capital inputs like pesticides, fertilizers, biotechnology, and intensive irrigation.

There is an opportunity for the WTO to shift the north-south divide on trade-environment, by examining in a comprehensive manner the coverage of environmental goods and services in a way that accurately reflects the environmental sector, and that benefits developing countries.

IV. UNDERSTANDING THE ECONOMIC, INCOME AND ENVIRONMENTAL EFFECTS OF TRADE

Briefly, despite ten years of work in understanding the environmental impacts of trade liberalization, the picture of how trade affects the environment remains unclear. This should not be surprising, since the question of how trade brings about *economic* effects remains surprisingly imprecise.

One of the most important assumptions of trade theory is that of conditional convergence. As countries trade, it is assumed that a convergence takes place in per capita GDP, as well as convergence in other areas, like technologies, information, institutional structures, etc. A particularly important area that merits more research involves how the WTO is affecting income.

There are very different perspectives on the relationship between trade and economic growth. For example, Sachs and Warner, 1995; Dollar, 2001 argue that a strong relationship exists between trade, economic openness and income growth. However, other views (Revenga, Edwards) dispute this view. While studies are inconclusive, the WTO (2000) noted that income inequality gaps *between* rich and poor countries has increased in absolute terms in the past decade. Perhaps more importantly, income gaps and inequality *within* countries, in many cases, has widened to a greater extent than the gap between countries. The link between wage inequality and trade needs to be examined more closely, from an economic and equity perspective. Questions include the effect of trade liberalization on skilled versus unskilled labor; the link between trade, production specialization and vertical integration; and the link between vertical integration and foreign direct investment. Analysis by the International Labor Organization (ILO) suggest that, at least during the early stages of liberalization, wage inequality follows a diverging, rather than converging, trajectory.

Understanding the relationship between trade and income is also important from an environmental quality, and environmental policy, perspective. Clearly, the assumptions of the Environmental Kuznets Curve, when introduced by Grossman and Krueger, have been shown to be flawed. However, analysis arising from that debate could usefully return to the wage-income-environmental quality debate.

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