

**METHODOLOGIES FOR ENVIRONMENTAL ASSESSMENT
OF TRADE LIBERALISATION AGREEMENTS**

Communication from the Organization for Economic Cooperation and Development (OECD)

Item 2

Attached is the report on the OECD Workshop on "Methodologies for Environmental Assessment of Trade Liberalisation Agreements" held in Paris on 26-27 October 1999. It was prepared by the workshop rapporteur¹ and has been de-classified, following review in the OECD Joint Working Party on Trade and Environment, on the responsibility of the OECD Secretary General.

I. INTRODUCTION

1. A workshop, "Methodologies for Environmental Assessment of Trade Liberalisation Agreements", was held at the OECD Headquarters in Paris on 26-27 October 1999.² The four half-day sessions were chaired by the co-chairs of the OECD Joint Working Party on Trade and Environment, Oddmund Graham and Skip Jones; by René Vossenaar, Chief of UNCTAD's Trade and Environment Unit; and by Hussein Abaza, head of UNEP's Economics and Trade Unit. Some 90 people attended, including Member country delegations and representatives from intergovernmental organisations, non-governmental organisations and academia, all in a personal capacity. No formal conclusions were adopted by the participants. This report outlines the main messages that emerged from the presentations and the discussions.

2. A recurring theme throughout was that the art and science of environmental assessment of trade agreements are still in their early stages. Many participants paid tribute to the OECD's 1994 "Methodologies for Environmental and Trade Reviews" as a useful point of departure and valuable for its practical guidance. However, all acknowledged that more work on developing and improving data and methodologies is needed. As a result, and owing to the diversity of available approaches and methodologies, it was considered premature to attempt to develop detailed, multilateral guidelines on environmental assessment of trade agreements. It was felt, however, that setting out best practices and common views on approaches and assumptions would be useful. In addition, the OECD was unanimously praised for convening the workshop in order to allow for valuable exchanges and collective learning.

¹Richard Tarasofsky, Workshop Rapporteur and international environmental lawyer.

²The workshop was made possible by voluntary contributions from the Governments of Canada, Finland, Japan, the Netherlands, Norway and Sweden. The volume of the Workshop Proceedings is now available as an OECD publication.

II. GENERAL CONSIDERATIONS

3. A variety of general points regarding environmental assessment of trade liberalization agreements were made. In particular, there was an exchange of lessons learned from past and ongoing environmental reviews of trade agreements, each of which was recognized to have some limitations. These experiences include:

- Reviews by the Governments of Canada and the United States of NAFTA and the Uruguay Round.
- A review by the European Commission of the EU single market.
- A Sustainability Impact Assessment based on EU negotiating proposals for the Millennium Round, commissioned by the European Commission and carried out by a consortium led by the University of Manchester.
- A framework for carrying out environmental assessments of trade liberalization agreements developed by the North American Commission for Environmental Cooperation.
- A methodology for environmental assessments of trade liberalization agreements developed by WWF International.

4. A necessary condition for a successful assessment is sufficient political commitment to make it happen and to carry it out effectively. In particular, it was argued that if an assessment process was to occur during the negotiation of a trade agreement, it would need considerable political backing. At the same time, however, participants were of the view that the independence of the assessment had to be ensured in order to maintain its credibility. In addition, it was emphasized at several points that the precise purpose of the assessment must be clearly borne in mind when designing and carrying it out. With hindsight, it was apparent that past assessments had two major substantive gaps, in that they had not covered trade in services, especially as regards sub-sectors which have effects on the environment, and investment aspects of trade agreements.

5. At the same time, the need for assessments to examine issues relating to scale, technology, composition and regulatory effects, as noted by the OECD in 1994, was reaffirmed.

6. It was generally recognized that no assessment is a purely technical exercise; there will always be an element of policy assumptions and value judgements. This was considered legitimate, as long as these are transparent. In particular, it was suggested that a set of clear hypotheses should be developed for testing by the assessment, in order to provide a focus for the exercise. At the same time, it was noted that the assessment would reveal the necessity of trade-offs. It was not considered the task of the assessor to deal with these trade-offs; rather, the results of the assessment should be an input into a transparent political process.

7. It was noted that assessments in developing countries pose special challenges. First, there is the question of the priority accorded to devoting resources to this task. It was pointed out, for example, that as countries move along the Kuznets curve (whereby environmental conditions get worse before they get better) some may actually "choose to be dirtier". Second, even if assessment is a priority, there is a very real possibility that the necessary resources and information would be lacking. Several participants therefore emphasized the need for capacity building in this regard. Third, methodologies that take into account the realities and perspectives of developing countries need to be improved. Fourth, it was argued that the willingness of developing countries to undertake such assessments would increase, to the extent that the general North-South divide on trade and environment issues lessens.

III. METHODOLOGY

8. Much of the workshop was spent addressing technical and procedural issues of assessment methodologies.

(i) *Technical issues*

9. A series of technical issues arose in relation to the economic, environmental/sustainable development and regulatory/institutional aspects of the assessment process.

(a) Economic aspects

10. In contrast to past assessments, which were largely qualitative, recent initiatives provide more quantitative tools. A central point made, however, was that despite considerable advances, it is still difficult to draw precise economic causal links resulting from trade liberalization and to determine the correlation between the economic data and the environmental consequences. In particular, it was considered important, but also difficult, to distinguish between the effects of trade liberalization and of economic growth. A key challenge is to determine a baseline for the analysis that would reflect what would happen had the trade agreement not been concluded. This challenge is complicated by the possibility that the future without the trade agreement will not be the same as a continuation of the status quo. Given these difficulties, several speakers pointed to the need to develop practical approaches to deal with these uncertainties.

11. Several specific points were made for improving the economic analysis of environmental assessments, in particular the need to:

- Improve the analysis of the economic consequences of policy and technology effects, especially given the changing/diminishing role of government in many economies.
- Make economic analyses more dynamic, especially to take account of the propensity of affected populations to learn and cope with economic changes.
- Make more realistic estimates of global and regional production shifts.
- Account for variation not only between, but also within, countries.
- Focus the analysis on households in certain assessments. In doing so, it is useful to integrate the economic and environmental and social aspects at an early stage. It is also useful to recognize that there are cases where the household is both a firm and a consumer.

12. Various approaches to undertaking such analyses are possible, but several speakers were of the view that sectoral approaches may be the most feasible. In such a case, it becomes necessary to develop clear criteria for selecting the sectors and for identifying the categories of environmental effects. In addition, it must be recognized that a single sector may have a myriad of environmental impacts. One disadvantage of the sectoral approach is that intersectoral effects will not be taken into account.

13. A variety of economic modelling approaches were presented, both generally and in relation to sectoral experience, in agriculture, forestry and manufacturing, including:

- Computable general equilibrium (CGE) models, including the Global Trade Analysis Project (GTAP) database and model, with an environment sub-model.
- Partial equilibrium models.

- The extended domestic resource cost (EDRC) approach.
- The comprehensive model for policy assessment.

14. Models were considered useful because they aim to take account of the impact on several countries of different sources of environmental damage. To date, however, each approach has limitations. For example, while CGE models are attractive in principle for their ability to account for many factors and effects, there are inevitably data and cost limitations. At the same time, partial equilibrium approaches may be more feasible but focus on changes in one sector and do not assess economy-wide effects.

15. Several key points emerged during the discussion on modelling. One is that the science of modelling is still evolving, so that one cannot definitively state that one approach is preferable to any other. Indeed, in some cases, the approaches can be complementary and build on each other; in particular, partial equilibrium models can feed into general equilibrium models. Thus, the participants welcomed the diversity of approaches.

16. Another consideration is that in all cases there are data limitations. This can force the modeller to use dummy or proxy variables, although this creates its own problems. The need to extend current databases was pointed out, as was the need for more data from developing countries. Valuation methods also need to be improved.

17. Some speakers urged greater consideration of certain variables, such as: costs of abatement, technology transfer, feedback, transition costs, regulatory policy impacts (technology and pricing), and the public sector's revenue-raising potential. However, it was also acknowledged that there may be feasibility limitations to examining these variables.

18. The importance and difficulty of calibration of data was emphasized.

19. Finally, models allowing for a bottom-up approach, e.g. focusing on domestic circumstances and firm-level data, were seen as particularly valuable.

(b) Environmental/sustainable development issues

20. Several challenges relating to environment and sustainable development emerged from the discussion.

21. A key problem raised at several points is the lack of definition and precision of the concept of sustainable development. Without this, the appropriate balance between environmental, economic and social impacts remains elusive and may affect the carrying out and interpretation of assessments.

22. Another challenge arises from the fact that environmental data are most credible when they relate to the local, or micro, level. By contrast, some of the economic analysis needed in carrying out assessments is at the macro level, and political decisions are also made at the macro level. Therefore, it is important to find ways to link the micro and macro levels of analysis.

23. A third issue relates to the general lack of environmental methodologies available for measuring certain kinds of impacts. In particular, there is a dearth of data and indicators on biodiversity and land use which hampers assessments in those areas.

24. In addition, it was argued that the precautionary and preventive approaches needed to be made operational, so as to make them applicable to the purposes of assessments.

25. A final issue relates to whether a distinction exists between undertaking environmental assessments and sustainable development assessments, and if so which is preferable.

(c) Regulatory effects

26. The need to address the regulatory effects of trade liberalization agreements arises from the legal nature of such agreements, and the fact that as barriers to trade are lowered, trade liberalization increasingly affects domestic regulation. Although this may be self-evident, there are no agreed methodologies for assessing regulatory effects from the legal point of view. This is in part because the process of legal interpretation is not always predictable, but also because the agreements themselves may contain a degree of ambiguity.

27. Two speakers made some methodological proposals to help assess regulatory effects which included suggestions in relation to frameworks, checklists and baselines. They presented two approaches: sectoral and rule-by-rule. The first is based on the methods used to carry out strategic environmental assessments and includes a pre-negotiation phase, the assessment itself and a follow-up phase. The pre-negotiation phase identifies concerns and objectives and carries out screening and scoping of issues. The assessment itself includes assembling baseline data on the existing body of instruments, scenario building based on an integrated examination of all measures affecting a sector, linking scenarios with relevant instruments and objectives and aggregation of information. The follow-up phase involves examining the effectiveness of the new instruments and assessing the constraints placed on countries when introducing new measures.

28. The rule-by-rule approach involves examining the constraints on environmental policy making posed by international trade agreements. Although a taxonomy of constraints can be identified, these are fraught with legal uncertainties, such as the definition of "like product" in the WTO Agreements.

29. Challenges in developing methodologies for assessing regulatory effects include:

- Developing a more detailed taxonomy of possible constraints from trade agreements on environmental regulation.
- Assessing the impacts of trade liberalization on international environmental standards and multilateral environmental agreements.

30. It was also suggested that it would be useful for litigation specialists to anticipate possible interpretations of textual proposals to discover possible unintended applications.

(ii) *Procedural issues*

31. Procedural issues relating to how and when assessments should be carried out were discussed extensively during the workshop. Key points that emerged were the importance of:

- Taking an interdisciplinary approach to carrying out the assessments.
- Consulting a broad group of stakeholders, including environmental NGOs, consumer groups, trade unions, farmers, etc.
- Building on and sharing information on past experience with assessments.

32. It was emphasized that different types of assessment call for different levels of public participation. Public participation was seen as adding legitimacy to the process of making trade-policy choices and as ensuring that as many actors as possible feel some ownership of the process. Decisions on precisely what level of public participation is appropriate should be made in accordance

with the objectives of the assessment. The potential for the Internet as an effective vehicle for obtaining public views was also emphasized.

33. An environmental assessment can be undertaken prior to negotiation of the trade agreement, during the negotiation of the trade agreement, after the agreement is signed, but not yet ratified, and after the agreement is implemented. It was argued that assessments carried out during the first two phases would be the most effective. During the first phase, public participation acts to ensure that all environmental issues are brought into the process, thereby allowing policy makers to assess their relative importance. It was argued that this type of assessment calls for broad public participation.

34. Assessments carried out during negotiations can be significant, particularly when the negotiations are protracted. In this case, the objective of such assessments is to address issues not foreseen during the pre-negotiation phase. It was argued that at this point, limited public participation would be sufficient, e.g. through an advisory group reporting to the responsible minister or trade negotiators.

35. The purpose of assessments carried out after signing, but prior to ratification, is to determine the necessity of flanking measures. It was argued that a wide level of public participation should take place to ensure that the most effective flanking measures are adopted.

36. Assessments carried out after implementation are designed to measure physical impacts. It was argued that such assessments can involve more limited public participation, perhaps through a continuous channel.

37. The discussion revealed that key threshold issues relate to how decisions are made as to when public participation is appropriate and in relation to what issues and hypotheses. It was noted that public participation issues become more complex once one moves from national to international level, since the international debate on public participation is clouded by other political considerations.

IV. USES OF THE ASSESSMENTS

38. Participants stated at several points that environmental assessments of trade agreements should not be purely theoretical exercises, but should lead to practical and policy-relevant results. In the stages prior to the implementation of a new international trade agreement, environmental assessments should be aimed at influencing the policy-making process by contributing to the:

- Determination of a country's priorities.
- Determination of a country's negotiating position.
- Determination of necessary environmental and possible flanking measures, particularly when transposing the international trade agreement into domestic law. The point was made that when assessments point to possible negative environmental effects arising from trade agreements, the appropriate response is not to halt the process of liberalization but rather to develop appropriate environmental policy responses.

39. Once a trade agreement has been implemented, assessments should be used to assess the actual environmental impacts, including from the social, economic and regulatory perspectives. Because liberalization may present "win-win" opportunities, this does not mean that there will be no losers. And because no assessment process will be perfect, an iterative cycle should be aimed for, so that *ex post* assessments can be the basis for future *ex ante* assessments.

V. SUMMARY OF PROPOSALS FOR FUTURE RESEARCH AND ACTION

40. This section highlights the main action points emerging from the workshop, which followed from the identification of gaps in current methodologies.

(i) *General matters*

- Keep the 1994 OECD *Methodologies* under consideration for possible review and for their potential application to areas not yet assessed, such as services.
- Develop methodologies to assess the environmental impacts of the GATS and investment provisions in trade agreements.
- Develop assessment methodologies for the effect of trade liberalization agreements on international environmental standards and multilateral environmental agreements.
- Develop frameworks for identifying the necessary trade-offs when considering the economic, environmental and social impacts of trade agreements.
- Provide a forum, such as the Joint Working Party, to enable Member countries to share experience with methodologies and economic/trade/environment models, particularly as regards practical aspects, and to explore the possibility of common approaches (e.g. between North and South).
- Increase capacity building in developing countries so as to facilitate the carrying out of more reviews and sharing assessment experience with observers working in developing countries, such as UNEP.

(ii) *Specific matters*

(a) Economic issues

41. In addition to consistent calls to improve the quantity and quality of data, several proposals were made in respect of CGE models, particularly in relation to forests and agriculture.

For forests:

- Incorporate insights from the household agricultural literature into CGE models, e.g. joint production of agricultural goods and fuelwood by the household, the wide variety of prices affected by trade liberalization which impact on land clearing and the effect of land tenure on land clearing.
- Further evaluate the effect of off-farm wages on deforestation.

For agriculture:

- Update estimates of the global shifts in agricultural production, given the slow progress in policy reform and liberalization and factoring in new price, cost and technology conditions.
- Provide more inclusive coverage of environmental effects, including biodiversity, genetically modified organisms, transport, concentrated animal operations and landscape values.
- Include cross-country and temporal analyses of agriculture-environmental policy change.

- Analyse business-led environmental management strategies, including the pattern of diffusion of "green" technologies.
- Analyse factors shaping technology innovation and adoption for agriculture-environmental management.

(iii) *Regulatory effects*

- Develop comprehensive and detailed checklists of issues to be considered when reviewing actual and potential effects of trade liberalization agreements on domestic environmental law, in consultation with NGOs and academics.
- Develop a full catalogue of possible uses, including potential unintended effects, to which a trade liberalization agreement might be put, by involving litigation lawyers in the review.
- Develop commentaries on proposed trade agreements to explain regulatory effects.

(iv) *Environmental/sustainable development issues*

- Improve the development of indicators for environmental impacts, especially damage to biological diversity.
 - Intensify research so as to consider a wider range of environmental impacts of trade agreements than has been examined to date.
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