

ITEM 1: THE RELATIONSHIP BETWEEN THE PROVISIONS OF THE MULTILATERAL TRADING SYSTEM AND TRADE MEASURES FOR ENVIRONMENTAL PURPOSES, INCLUDING THOSE PURSUANT TO MULTILATERAL ENVIRONMENTAL AGREEMENTS

Communication from New Zealand

I. INTRODUCTION

1. In its submission WT/CTE/W/162 of 10 October 2000, New Zealand emphasized that the negotiation of MEAs remained an essential mechanism through which countries can address environment objectives. The submission also recognized that trade measures will continue to be a feature of some MEAs and that therefore it was important to further develop our understanding of the relationship between such Agreements and WTO rules. While WT/CTE/W/162 acknowledged that the range of potential conflicts between MEAs and the WTO Agreements was tightly circumscribed, it noted that questions may arise, when provisions of an MEA are unclear as to the action they mandate, even among the Parties to it, or in situations where the Parties to an MEA are applying trade measures against a non-party.

2. In the context of these observations, New Zealand suggested that the Committee on Trade and Environment consider, *inter alia*, the contribution that a consultative mechanism guided by first-best principles could make to clarifying the WTO/MEA relationship. At its meeting of 24-25 October 2000, the CTE expressed interest in this proposal and requested an elaboration of the way in which a consultative mechanism might work. This submission responds to that request.

II. THE CONSULTATIVE MECHANISM

3. In WT/CTE/W/162, New Zealand acknowledged that trade measures are seldom the first-best policy tools to achieve environmental objectives. In this context, New Zealand believes that, before a decision to apply a trade measure as part of an MEA is taken, a voluntary consultative mechanism could be utilized to assess whether the trade measure is the most effective instrument available to address the environmental problem at issue.¹ The principle underpinning this voluntary consultative mechanism should be to assist in the identification of a first-best instrument from a range of options to resolve the environmental issue identified as problematic.²

4. The concept of first-best enables the policy maker to evaluate resource allocations and decide whether they are "good" or "bad" from the point of view of society.³ The general rule by which to

¹A minority of MEAs (e.g. CITES) already possess such a mechanism but the majority of MEAs with trade measures do not have any such built-in instrument.

²It is worth noting that the use of such a methodology to guide policy decisions in the WTO context at least is not new. The most important exceptions in GATT Article XX, for instance, address situations where negative externalities need to be remedied.

³In a simplified situation in which there are just two goods and an initial allocation of these goods between two individuals, if it is possible for a reallocation of these goods to take place, whereby one individual gains in satisfaction whilst the other is no worse off, then this change in distribution meets the first-best criterion and is Pareto efficient.

identify a first-best solution in any specific circumstance is that it should be the one which most directly addresses the market imperfection or distortion. First-best therefore provides for: a hierarchy of policy choices; contains a presumption in favour of the most efficient and least distortive choice; and, in this way, allows national policies to be balanced by global welfare issues.⁴ In the context of the issues being addressed by the consultative mechanism proposed by New Zealand, the first-best solution should therefore most directly address the environmental problem which has triggered the potential for the application of a trade measure in the least distortive and most efficient manner possible.

5. New Zealand recognizes that, in any utilization of the voluntary consultative process, there will always be a wide range of possible policy options for consideration. A solution which may work for one environmental problem may not work for others. Experience shows that in many cases, environmental problems are not the result of a deliberate policy of environmental destruction, but may be a by-product of economic activity or may be triggered by a lack of technology and/or technical know-how. In such circumstances, the application of a trade measure may be inefficient because it may fail to address the negative behaviour at the source and may not necessarily alter the action which has led to the environmental degradation originally targeted for action by the trade measures. In response to trade measures by MEA Parties, countries may also move to sell the environmentally damaging products to countries which are not Parties to the MEA. Alternatively, trade in the prohibited substance may be driven underground. In certain cases, therefore, an instrument other than a trade measure may deliver a more efficient and less distortive outcome. The provision of technical assistance, for instance, may in certain circumstances achieve the primary objective, i.e. protect the environment more efficiently and effectively than a trade measure.

6. It should be noted, however, that the use of the voluntary consultative mechanism does not rule out the prospect of trade measures in MEAs. New Zealand recognizes that in certain circumstances trade measures can play an important role in MEAs and that, in some cases, they may indeed deliver an effective and efficient solution to address the environmental problem directly (e.g. CITES).

III. AN EXAMPLE

7. The practical application of the consultative mechanism outlined above may be described with reference to the following hypothetical example.

8. Let us assume that countries A and B are both Members of the WTO, but only country A is a member of an MEA.⁵ This hypothetical MEA is an international convention open to all countries. Its membership comprises Parties in all stages of economic development and includes members of each of the UN regional groupings. Under the terms of the MEA, the Parties have explicitly sought to prohibit the trade in product CS1 which damages the environment. Country B produces CS1 and trades a limited amount of this product annually to clients based in country A.

9. Country A learns of the desire of country B and, in compliance with the terms of the MEA, has the right to refuse the import of CS1 from country B. Before the trade measure is applied,

⁴First-best may be contrasted with second-best, which states that if two or more of the conditions for efficiency are not satisfied, changes which cause some more, but not all, of the efficiency conditions to be satisfied may not be beneficial.

⁵While this example focuses on the use which can be made of the consultative mechanism by WTO Members, it could be utilized more widely. It may, for instance, be possible for members of an MEA to consult with a significant non-party. While outside the scope of this paper, there may also be circumstances where such a voluntary mechanism could be helpful to address global environmental problems which are not covered by the terms of an MEA.

however, countries A and B mutually agree to initiate the voluntary consultative mechanism outlined above to identify a first-best solution to the problem.

10. During the consultations, country A outlines the evidence it has regarding the environmental degradation (either generally and/or specifically) caused by the ongoing production and trade in CS1 by country B. In response, country B notes that the production of and trade in CS1 provides economic benefits for a section of its population. Having outlined the problem as both sides see it, country A and country B decide to consider a hierarchy of policy instruments to address the environmental problem generated through the production of CS1. The instruments considered may include: the imposition of a trade measure; the supply of limited financial assistance for the development of new skills for the factory workers producing CS1; development assistance for the wider community affected by the prohibition of CS1 production; and the transfer of technology and/or technical know-how. Countries A and B consider all of these options and should select the instrument which meets the criteria of first-best.

11. It should be emphasized that New Zealand does not believe that a voluntary consultative mechanism in and of itself would guarantee the delivery of an acceptable solution to all parties at all times. The use of the voluntary mechanism does not, as noted earlier, rule out the use of trade measures. Indeed, trade measures need not await the outcome of the voluntary consultation, if one of the Parties considers this is proceeding unsatisfactorily. It should be further noted that the voluntary utilization of the mechanism does not preclude other action, nor is it designed to undermine the application of control measures. Rather, New Zealand considers that such a voluntary instrument may: facilitate an improved understanding of different points of view; allow for the identification of a range of different policy options; maximize the potential for an agreed solution; minimize conflicts between parties on trade and environment related policies while at the same time avoiding inefficient environmental and economic outcomes. In particular, a substantive and meaningful engagement by countries in a consultative process designed to identify first-best policy options is likely to reduce the potential for discriminatory or arbitrary measures.

IV. CONCLUSION

12. Over the longer term, it is proposed that MEA negotiators who represent countries which are Members of the WTO should consider including a voluntary consultative mechanism guided by first-best principles in new MEAs. In the meantime, New Zealand recommends that Members of the WTO who participate in existing MEAs may wish to favourably consider utilizing such a consultative mechanism before trade measures are applied. The Committee for Trade and Environment may wish to note these recommendations in its record of proceedings.
