

**Sustainable Development and Energy Security:**  
**The WTO and the Energy Charter Treaty**

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## **Introduction**

The trade-environment linkage – or sustainable development as it is now called – has been uneasy and unclear. “Sustainable development” is now firmly lodged in the WTO – at least in words, and in a rule-based system words matter. But the present arrangements in the WTO are ill-suited to cope with the formidable challenges of environmental deterioration, growing inequality and today’s big headline issue – energy security (see below).

This paper will first trace the trade and environment issue as it evolved into sustainable development in the global trading system. Then, we will provide a brief review of the Energy Charter Treaty. We will then explore some options for policy cooperation between the two institutions. After all, policy coherence is part of the historical legacy of another institution – the Summit.

## **Trade and the Environment**

There was no explicit reference to the environment in the GATT (the General Agreement on Tariffs and Trade) when it was established in 1948. But as the issue became prominent in international circles the GATT was pressured to pay attention. In 1971, after the Stockholm Conference on the Human Environment, a GATT Group on Environmental Measures and International Trade (EMIT) was formed. It did not meet until November 1991, in advance of the 1992 Rio Summit on Environment and Development. By and large the mainstream view in the trade community was that environmental policies could spur protectionism – a kind of Baptist-Bootlegger approach. And environmentalist NGO’s (ENGO’s) were far more interested in lobbying the World Bank than the GATT.

But everything changed in the early 1990s after a GATT dispute panel ruled in favour of Mexico's challenge to the American embargo on tuna caught in a fashion harming dolphins. This mobilized a massive attack on the GATT and the ongoing Uruguay Round. Posters of "Gatzilla" were plastered on streets in Geneva and Washington. The new slogan was GATT – "Guaranteeing a Toxic Tomorrow."

And the ENGO's were very effective at the end of the Uruguay Round in pressuring the US government to ensure a reference to sustainable development was included in the preamble of the document establishing the WTO.<sup>1</sup> This was an enormous victory for the Greens. Unlike the tuna and dolphin failure, in a challenge to the US concerning shrimps, the Appellate Body in 1998 cited the WTO's preamble. So, sea turtles were viewed as a non-renewable resource and the substance of WTO rules in effect amended. And the role of the Dispute Settlement Mechanism (especially the Appellate Body) was launched – rule of law and rule of lawyers.<sup>2</sup> I wonder if developing countries in Marrakesh understood the implications of the WTO preamble. How much expertise did they possess about constructive ambiguity? Let me explain.

There was a favourite joke in the 1990's about drafting communiqués. After gruelling all-night sessions, the final draft was produced and the question was put: is there anyone here who believes that this communiqué can be fully understood in his (or her) nation's capital? If no hands went up, it was time to go. The outcome was a masterpiece of creative ambiguity. I certainly do not know but I have always imagined that the definition of sustainable development was achieved in the same way. In 1987, the UN Brundtland Commission report, Our Common Culture, defined the term "sustainable development" as follows: "development that meets the needs of the present

without compromising the ability of future generations to meet their own needs.” Since then, there have been hundreds of definitions but this is the most famous. However, I am not sure it might not be termed “destructive ambiguity.” Let me explain.

There were, and to some extent still are, wide differences between the economists and the environmentalists that were not created but were catalyzed by events in the 1990’s. The differences are complex but often expressed in a right-left debate. Further, there was a serious North-South cleavage reflecting fundamentally different priorities. The South favoured growth, not the post-materialism of many ENGO’s from rich countries. American ENGOs in particular have been mainly concerned with wildlife protection and landscape protection. As one Southern ambassador at the WTO remarked, “If only we were elephants, developed countries might be more concerned about us.”<sup>3</sup>

So it seems fair to say that the ambiguity was an attempt to gloss over these deep divides. The conventional wisdom cited the Three E’s – efficiency, equity and ecology – enshrined in sustainable development. This was win-win-win. But how? What are the policies and how are they connected? How do we measure sustainable development? What are the costs and benefits? Who pays for what? How is this related to trade? And so on – and on.

These and other issues remain to be analysed and debated. But it is important to recognize that while left-right and North-South conflict remains, there is a far greater willingness today than in the 1990’s to discuss the linkages between trade and development and environmental concerns. A WTO Committee on Trade and the Environment (CTE) and on Trade and Development (CTD) were established. This change was reflected in the Doha agenda.

### **The Doha Agenda and Sustainable Development**

The Doha Round (or DDA, the Doha Development Agenda as it is often termed) was the first in the trading system to include issues related to trade and environment. These included: the relationship between WTO rules and specific trade obligations in MEA (to be limited in scope to parties to the MEA in question); procedures for information exchange between MEA's and relevant WTO committees and on the criteria for the granting of observer status; negotiations on the reduction or elimination of tariff and non-tariff barriers to environmental goods and services. A cautionary note was added that the outcome of these negotiations must not alter the balance of WTO members' rights and obligations under existing agreements.

In addition to these negotiations, the CTE was mandated to review a number of other trade-related environment issues including the effect of environmental measures on market access for developing countries and the effects of trade liberalization on the environment. These issues were actually included at the founding of the CTE in Marrakesh. And nothing much emerged.

Another, potentially very important issue on the DDA was "to clarify and improve WTO disciplines on fisheries subsidies, taking into account the importance of this sector to developing countries." This is the first proposal that deals directly with an environmental issue *per se* and was included because of effective lobbying by ENGO's. It is not being negotiated in the CTE but is included in the Group on Rules.

It is not difficult to summarize the outcome at Hong Kong. One word will do: nothing. Given the fear that the whole Round would collapse – as in Cancun – this may

not be surprising. Sustainable development is not at present a hot ticket item for the WTO. At least not right now.

Yet we should recognize that, more by accident than design, the WTO houses a wide range of agreements and handles numerous disputes that are related to sustainable development. This transformation was the result of the Uruguay Round which shifted the focus of the trading system from border barriers to major areas of domestic policy and institutional infrastructure. A recent book by Gary Sampson<sup>4</sup> provides a comprehensive review of the substantive links between WTO provisions and sustainable development including, for example, the complex and sophisticated regulations and the technical mandatory standards to protect public health, safety and the environment (TBT's and SPS) and the intellectual property issues in TRIPS, for example, concerning biotechnology that arouse enormous anger and friction both across the Atlantic (GMO's and Frankenfood, etc.) as well as North and South (access to essential medicines) and, within the environment community, biodiversity. And surely the issue of reducing trade distorting agricultural and other subsidies should take into account the environmental and distributional impacts for win-win-win policies. So even if the Doha agenda on sustainable development were completed by the end of the Round, this would hardly scratch the surface of the WTO and Sustainable Development.

Moreover, let us not forget the Development part of S.D. Another unintended consequence of the Uruguay Round was systemic asymmetry, a profound manifestation of inequity. While there is not the time now to describe these features of the global trading system, one crucial aspect is complexity. The need for knowledge, advanced and sophisticated, is essential. Complexity requires knowledge and knowledge enhances

power. The strong are stronger because of their store of knowledge and the weak are weaker because of their poverty of knowledge. So the system has endogenized asymmetry. The knowledge trap feeds the poverty trap. And this is well documented by a growing number of case studies by the World Bank that demonstrate the capacity deficit. Many concern the TBT's and SPS. Further, the asymmetry is not offset but rather reinforced by the legalization of the system as a number of recent studies show.<sup>5</sup>

What is at stake in the Doha Round is not a negotiation on trade but on the survival of the rules-based multilateral trading system. The alternative is very apparent – fragmentation by an increasing proliferation of preferential agreements led by American “competitive liberalization” based on power and *episodic ad hocery*. This fragmentation is exacerbated by the recent mushrooming of regional trade and other agreements involving developing countries. These reflect the New Geography already apparent at Cancun and the decline in attraction of the WTO.<sup>6</sup> They also reflect the ongoing shift in the Balance of Power from the West to the East and Russia. But that's another story.

Whatever the final outcome of Doha, it would be both possible and very desirable (not to say urgent) for the WTO member countries to launch some serious reform.

First, on environmental issues, the DDA, para 51, explicitly calls on the CTE and the CTD to “act as a forum within which the environmental and developmental aspects of the negotiations can be debated in order to achieve the objective of sustainable development.” There is little likelihood that there could be a serious and informed debate on this subject if it is tied to negotiations. That would completely constrain the participants. What is required is a WTO policy forum – recommended by the Sutherland Consultation Board among others – to be accompanied by an increase in research

resources. There was one in the GATT – the Consultative Group of 18 – involving senior officials from capitals. It was immensely important in the launch of the Uruguay Round. The forum should include knowledge networking with NGO's, IGO's, MEA's, etc. It should begin to explore the main dimensions of SD.

That this is a formidable challenge must be acknowledged. The trading system thrived on reciprocity often derided as mercantilism by policy purists. The environmental issues are *au fond* intrinsic to public goods. The trade-offs are complex: costs now and uncertain benefits over an uncertain time frame. Reciprocity is not on the table. The system of national accounts (SNA) was created as an offspring of Lord Keynes' General Theory. Measurement is key to the policy process. But despite myriad efforts, there is no generally accepted definition or data on sustainability. These are but a few of the agenda items to be tackled. But the most stupendous item is global warming. And there is a widening chasm between the US government and the EU. American states and even cities are adopting SD policies. There has been a proliferation of codes of corporate social responsibility by American multinationals (although a recent review of these measures by David Vogel suggests that the impact on environmental degradation will be modest in the absence of government policy<sup>7</sup>). So a policy forum is essential to engage a wide range of actors and not just countries. It would not likely be approved by many WTO members but what about a coalition of the willing?

And in addition to the policy forum, the Aid For Trade project announced in Hong Kong will require cooperation between the WTO and development institutions such as the World Bank and others as in the Integrated Framework launched in 1997 as a demonstration of the improved "international coherence" promised in the Uruguay



Round. This was designed to include only the WTO and the Bretton Woods Twins. The idea of cooperation with institutions covering issues such as the environment or energy security would not have occurred to anyone. But as noted above, only a decade after the completion of the Uruguay Round these are headline issues. So let me conclude with a brief discussion of the Energy Charter Treaty.

### **Energy Security**

The issue of energy security has been of high priority to the EU for many years as the brief history of the Energy Charter will amply demonstrate shortly. That was hardly the case in the US – except during the 1970’s and the OPEC crises. But today, energy security is headline news. A recent survey of foreign policy (the second in an ongoing series) shows a striking change: nearly 90% of Americans put energy security at the top of their list of worries, a dramatic change since the 2005 results.<sup>8</sup> There are a number of complex and interrelated reasons for this new “tipping point” which will change public policy pressure but seems unlikely to recede.

Coincidentally or not, the 2006 G8 Summit hosted by Russia will plan energy security at the top of the agenda. This is likely to be a complex and contentious issue. A brief explanation would be useful.

The roots of the Energy Charter date back to the early 1990’s when it was launched by the EU as a project to enhance cooperation between East and West and facilitate the transition to market economies of the former Socialist countries. A kind of “grand bargain” investment for Eastern energy supplies. The scope has broadened considerably since 1991 when the European Energy Charter was established and in 1998,

the Energy Charter Treaty entered into legal force. As well as European countries, a number of Asian countries have joined. But the US and Canada have not and Russia has refused to ratify.

The treaty is an enormously complex and ambitious institution. First of all, it incorporates the rules of the WTO, even for non-members. But the most essential feature of the Charter concerns investment. The rules for investment are divided into two sections: one covers pre-establishment and the other post-establishment. The latter are based on NAFTA and include investor-state dispute settlement by arbitration (à la NAFTA Chapter 11). The pre-establishment rules remain “soft law” and do not cover vital issues such as MFN and national treatment. The same is true of other issues such as environmental regulation and competition policy.

The Energy Charter Treaty is, however, the first multilateral agreement that covers investment, albeit in one sector. This is pathbreaking and a first step in establishing clear and transparent rules to reduce risk and encourage financial support for energy supply. However, the efforts to extend the provisions concerning investment access (pre-establishment) has so far failed. Similarly, another key factor on the supply side – transit infra-structure – is still not agreed and despite lengthy negotiations for a Protocol remains subject to serious disputes, especially with Russia. Indeed, the most serious deficiency in the Charter is the refusal of Russia to ratify the Treaty. Energy security without Russia is akin to Hamlet without the Prince.

Clearly, the most significant achievement for the G8 Summit in the issue of energy security would be for the United States and Canada to ratify the Energy Charter so that the G7 could persuade Russia to do likewise. But that, unfortunately, seems

unlikely. Press reports suggest that even the definition of “energy security” cannot be agreed upon.<sup>9</sup>

Maybe it would be wiser to recognize that the Energy Treaty Charter is far too ambitious in today’s geo-political ambience and instead of reaching to build a bridge too far, the G8 should initiate a step-by-step passage for a long journey. Even though the destination is not fully agreed.

As stressed above, the heart of the Treaty concerns foreign investment. After the failure of the OECD’s MAI (Multilateral Agreement on Investment) and rejection of the European proposal include investment in the WTO at Cancun, the main route to investment rules remains bilateral agreements “designed” for the most part by the powerful, especially the US and EU. The only exception has been NAFTA. And, indeed, NAFTA established the template for the Energy Treaty investment regime.

The NGO attacks on the MAI and NAFTA were build on a fundamental concern over “state sovereignty” and centered mainly on the investor-state dispute mechanism. But there were also disputes concerning differences among legal systems. For example, although US and Canada are both common-law countries, Canada does not include property rights in the Constitution and have different jurisprudence in the area of “regulatory takings.” This has raised a political firestorm in several challenges by American companies. But in the case of Mexico the differences in legal systems were so great that NAFTA required fundamental change in laws, regulations and administrative law procedures. How this has provided credible implementation has not been examined so far.

The point of this digression is to assert that significant differences among countries in legal and regulatory system are of fundamental importance to the effectiveness of the Treaty. The G-8 should launch a project on analysis of the legal and regulatory systems with respect to foreign investment in energy both pre and post-establishment. It would be very important, in addition to legal experts and multinational corporations, to include WTO Secretariat to discuss TRIMS (trade-related investment measures) and TRIPS (trade-related intellectual property measures). A review of the MAI experience provided by the OECD Secretariat would also be immensely useful.

The legal and regulatory differences will be significant and will provide information essential to the understanding of how effectively they could be monitored in regards to implementation. This would be useful both to members and to those considering membership. Clearly, there is no single benchmark but surely this would facilitate a reasoned discussion on the key issue: what is energy security and how can it be established via an investment regime?

This would be a useful project to launch as a continuing process. A special forum should be established by the Charter and open to members and non-members. There should be an agreed list of issues presented to members for discussion and debate. There should be a recognition that the situation is urgent. And that “energy security” is not just about the market but part of an ongoing (and dangerous) geo-political game. Thinking about that (like being hanged in the morning) could clear the mind. Put it this way: we need energy security to foster sustainable development. This is international coherence writ large.

## **Footnotes**

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<sup>1</sup> This was told to me by Mark Halle, IISD, Geneva.

<sup>2</sup> J.H.H. Weiler, “The Rule of Lawyers and the Ethos of Diplomatic Reflections on WTO Dispute Settlement,” Roger Porter, et al (eds.) Efficiency, Equity, Legitimacy, Brookings Institution Press, Washington, DC, 2001, p 339.

<sup>3</sup> Gregory C. Shaffer, “The World Trade Organization Under Challenge: Democracy and the Law and Politics of the WTO’s Treatment of Trade and Environment Matters,” Harvard Environmental Law Review, 2, 2001, p 88.

<sup>4</sup> Gary Sampson, The WTO and Sustainable Development, UNU Press, Tokyo, 2005.

<sup>5</sup> Sylvia Ostry, *The Post Doha Trading System*, Pre-G8 Academic Conference, University of Glasgow, June 29-30, 2005, publication pending.

<sup>6</sup> See Agata Antkiewicz and John Whalley, “BRICSAM and the Non-WTO”, presented at a Conference on June 1, 2006, Toronto.

<sup>7</sup> David Vogel, The Market for Virtue, Bookings Institution Press, Washington, DC, 2005.

<sup>8</sup> Daniel Yankelovich, “The Tripping Points,” Foreign Affairs, May/June 2006, New York, pp 115-126.

<sup>9</sup> This has become amply apparent in the flood of articles in advance of the G-8 Summit. A neat way of summing this was recently presented by President Putin: you want security of supply and we want security of demand. But that is just one way of covering up a vast and complex set of disagreements.