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## IX. INTERNATIONAL ECONOMY AND THE ENVIRONMENT

### 1. INTERNATIONAL TRADE RULES, WORLD MARKET CONDITIONS, AND ENVIRONMENTAL EFFECTS

There was considerable activity in 1994 relating to international trade institutions and the impact of trade rules on the environment. The most notable activity took place in respect to the World Trade Organization (WTO), which on January 1, 1995, succeeded the General Agreement on Tariffs and Trade (GATT) as the international organization principally responsible for governance of the multilateral trading system.

#### *(1) Environment-Related Matters and the GATT-WTO*

On April 15, the Final Act Embodying the Results of the Uruguay Round of Trade Negotiations was signed by Ministers at Marrakesh. The Final Act included the texts of the new WTO-related agreements. The WTO agreements with specific implications for the environment have been described in prior *Yearbook* reports on this subject.

#### *(a) The Marrakesh (→) Decision on Trade and Environment*

The Ministers took a Decision on Trade and Environment in connection with the Marrakesh signing of the WTO. In this Decision, the Ministers directed

the first meeting of the General Council of the WTO to establish a Committee on Trade and Environment open to all members of the WTO to report to the first biennial meeting of the Ministerial Conference after the entry into force of the WTO when the work and terms of reference of the Committee will be reviewed, in light of the recommendations of the Committee. . . .

The Marrakesh Decision stated that the Trade Negotiating Committee Decision of December 15, 1993 (*see* 4 *YbIEL* 283 (1993)), would constitute the terms of reference of the Committee. The Decision said that within such terms of reference, the Committee would address a number of matters, including the relationship between the international trading system, on the one hand, and taxes for environmental purposes, technical standards, and packaging and labelling requirements, on the other. The Committee would also consider transparency, the relationship between dispute settlement mechanisms in the multilateral trading system and multilateral environmental agreements, and the effect of environmental agreements on market access (especially in relation to developing countries). The Committee

would further consider the work program envisaged by the Decision on Trade in Services and the Environment, and the relevant provisions of the TRIPS Agreement, as well as arrangements for relations with inter-governmental and non-governmental organizations.

(b) *GATT Dispute Settlement Panels*

Two GATT dispute settlement panel decisions concerning environment-related measures were rendered in 1994. Neither of these decisions was made under the new WTO dispute settlement procedure and neither was adopted in 1994 by the GATT Executive Council. The United States has objected to adoption of the Tuna II panel report, and the European Union has objected to adoption of the CAFE Standards panel report. The status of these decisions under the WTO may engender controversy, and the Preparatory Committee established to consider GATT-WTO transitional issues may have this status issue as one of its agenda items.

(i) (→) *United States-Restrictions on Imports of Tuna (Tuna II) Panel Report*

This case involved a complaint by the European Economic Community (EEC) and Netherlands, as co-complainants, against the United States. The complaint of the EEC and Netherlands was brought following the decision of the government of Mexico not to seek adoption of the panel report on the same subject matter rendered in its favor in 1991 (*Tuna I*). In *Tuna II*, the complainants again challenged the GATT-legality of the US Marine Mammal Protection Act (MMPA). This legislation, *inter alia*, requires the imposition of restrictions on the import of tuna from nations harvesting in the Eastern Tropical Pacific when their harvesting practices yield an unacceptably high mortality rate for marine mammals (including dolphins). It also requires the imposition of a secondary embargo on nations that import tuna from nations subject to the primary embargo.

As in *Tuna I*, the panel concluded that US MMPA import restrictions should not be considered internal regulations applied at the nation's border pursuant to GATT Art. III and Note ad Art. III since the United States was not attempting to regulate tuna as a product, but rather was attempting to regulate tuna harvesting methods that could not "have any impact on the inherent quality of tuna as a product" (para. 5.9). The panel found that MMPA embargoes are import restrictions prohibited by GATT Art. XI. It then addressed US arguments that its measures are justifiable, even if inconsistent with Art. XI, because they are taken under Art. XX(g) to conserve dolphins (an exhaustible natural resource), or because they are necessary under Art. XX(b) to protect the life and health of dolphins.

Distinguishing *Tuna II* from *Tuna I*, both the United States and the co-complainants sought to use the negotiating history, terms, and practice of

states with respect to treaties other than the GATT to aid in interpretation of Art. XX(b) and (g), and to address whether those provisions permit the imposition of extraterritorial measures. The panel, however, rejected these arguments on the basis of the rules of interpretation of the Vienna Convention on the Law of Treaties. According to the panel, since the parties to the GATT and the parties to the other referenced treaties are not coextensive, the other treaties could not be used as general GATT interpretative sources. The panel noted that a number of the referenced treaties were entered into after the GATT. It also said that practice under the various other treaties could not be used to generally interpret the GATT since practice under other treaties was not practice under the GATT. The panel finally noted that the other referenced treaties and their negotiating history could not be used as a supplementary interpretative source since: (a) the use of supplementary sources is confined to situations that the panel did not consider present in this case; and (b) none of the references cited by the disputing parties appeared to the panel to provide clear support for any particular contention.

The panel found that US embargo measures were not taken with the primary purpose of conserving exhaustible natural resources since the embargo measures would not be effective in controlling dolphin mortality unless harvesting countries changed their policies and practices. The panel said that while parties to the GATT are permitted to take trade measures to implement policies relating to conservation within their own jurisdictions, the balance of rights and obligations among parties to the GATT would be seriously impaired if parties were permitted to take trade measures to force changes to policies within the jurisdiction of other nations. The panel concluded that since the US measures were directed to forcing other countries to change their policies, and not directed primarily to the conservation of resources, they were not justifiable under Art. XX(g).

The United States and EEC agreed that protection of the life of dolphins could come within the scope of necessary measures under Art. XX(b), but differed as to whether measures could be taken to protect the life of living things outside the territory of a party. The panel noted that under certain other provisions of the GATT, parties could accord different treatment to products of different origin. The panel found that "[i]t could not therefore be said that the GATT proscribed in an absolute manner such measures" (para. 5.32). The panel also noted that under general principles of international law, states are not prohibited from regulating the conduct of their own nationals with respect to the treatment of animals outside their own territory. The panel concluded that US policies, insofar as they related to US nationals and vessels, fell within the range of policies covered by Art. XX(b).

The panel went on to examine whether the primary and secondary embargo measures of the United States were "necessary" to protect the life

and health of dolphins. The panel referred to prior GATT panel decisions that took a narrow view of the Art. XX "necessary" standard, requiring parties that rely on the exception to take the least GATT-inconsistent measures reasonably available to them. The panel followed the same reasoning with respect to Art. XX(b) as it had with respect to Art. XX(g), finding that the United States was relying on forced changes to the policies and practices of other nations in order to make its own policies succeed. The panel found that while Art. XX(b) did not expressly prohibit such conduct, trade measures taken by one GATT party to force changes to the policies of other parties within their own jurisdictions would seriously impair the objectives of the GATT. The panel recommended that the United States bring its measures into conformity with its obligations under the GATT.

Although there are subtle differences in the reasoning of the *Tuna I* and *Tuna II* panels, from the perspective of environmental non-governmental organizations (NGOs) there does not appear any significant advance in *Tuna II* toward permitting countries in the GATT-WTO to maintain unilateral extraterritorial measures.

*(ii) US CAFE Standards Panel Report*

The Corporate Average Fuel Economy (CAFE) Standards dispute involved a claim by the European Community (EC) against the United States. The EC alleged that the US luxury tax on automobiles, the US gas-guzzler tax, and US legislation governing automobile fleet fuel economy, discriminate against automobiles imported into the United States from the EC. The luxury tax is imposed on the retail sale of automobiles. The tax rate is 10 percent of the amount by which the sales price of the automobile exceeds \$30,000 (which base, per a 1993 amendment to the legislation, is indexed for inflation). The gas-guzzler tax is imposed on manufacturers whose automobiles within designated model types fail to achieve specified fuel economy standards (*i.e.*, that exceed a base fuel economy threshold). The tax is imposed with respect to each automobile and is disclosed to the consumer. CAFE legislation requires manufacturers and importers of automobiles to achieve certain fuel economy standards across the range of their US production/sales (but not exports), as well as their imports. Corporate fleet fuel economy is determined through a series of complex measures established by the US Environmental Protection Agency (EPA). For companies that are both manufacturers in the United States and importers, average fuel economy is calculated separately for imported and US-produced automobiles.

The EC contended that the luxury tax was inconsistent with US obligations under GATT Art. III:2, which requires equivalent treatment of "like products" of domestic and foreign manufacture. The EC contended that automobiles above and below the indexed \$30,000 threshold are "like prod-

ucts," that the threshold is not based on objective standards, and that it has the effect of discriminating against EC producers that tend to export automobiles exceeding the threshold to the United States.

The panel decided that the principal criterion to be used in determining whether different and less favorable treatment applied to imported products (with similar characteristics to domestic products) is whether the distinction is made "so as to afford protection to domestic production" (referring to GATT Art. III:1) (para. 5.9). This criterion was held to be inconsistent with Art. III:2. The panel observed that the term "so as to afford protection" suggested both "aim and effect." "Aim" indicates a desired outcome as opposed to an incidental consequence, and "effect" refers to according greater competitive opportunities to domestic products. The panel said that the "effect of a measure in terms of trade flows was not relevant for the purposes of Art. III, since a change in the volume or proportion of imports could be due to many factors other than government measures" (para. 5.10). The panel found that, despite statements by some US legislators suggesting a protectionist intent, the establishment of the \$30,000 threshold was consistent with the aim of raising revenues from the sale of "luxury" products, and that there was considerable uncertainty as to the impact of the tax on domestic as opposed to foreign products. The panel also found that there was not conclusive evidence that a change in conditions had occurred favoring US producers, and that EC manufacturers could export less expensive automobiles to the United States if they so chose. The panel concluded that the luxury tax was not adopted so as to afford domestic protection and that automobiles above and below the threshold could not, for the purposes of the luxury tax, be considered "like products." The luxury tax was not inconsistent with Art. III:2.

The EC claimed that the gas-guzzler tax is also inconsistent with GATT Art. III:2 because automobiles with different fuel consumption characteristics are nevertheless "like products," and because the gas-guzzler tax falls disproportionately on EC produced automobiles. The United States argued that the tax was based on objectively justifiable distinctions aimed at a policy other than protection of domestic production. It further said that even if the tax was inconsistent with Art. III:2, it was justified under Art. XX(g) as related to the conservation of fossil fuels.

The panel invoked the criterion it used in respect to the luxury tax, *i.e.*, whether the measure was adopted so as to afford protection to domestic production. The panel noted that even though the tax affected few cars (since it was complementary to the CAFE standards), and that other more efficient measures might have been used for conservation purposes, that the measure did not target foreign automobiles. The panel noted that at the time the tax was adopted, US manufacturers could not achieve the relevant fuel consumption threshold. The panel also found that the tax did not have

the effect of protecting domestic production because EC manufacturers had the technology to meet the relevant threshold. The panel concluded moreover that the methodology used by the United States in determining fuel economy did not have the aim or effect of protecting domestic production, and that the exclusion of certain types of vehicles (*e.g.*, light trucks) did not have such aim or effect (even though including all vehicles might have advanced fuel conservation policies). In light of its determination regarding Art. III, the panel did not consider the US argument concerning Art. XX(g) with respect to the gas-guzzler tax.

The panel examined the claim of the EC that US CAFE standards are inconsistent with GATT Art. III:2 and :4. The EC contended the CAFE standards are inherently discriminatory since specialized manufacturers of imported cars may not use the fuel economy of cars that meet the requisite CAFE standards to offset the fuel consumption of cars that fail to meet these standards, as may their US counterparts. The EC argued that its manufacturers suffered a disproportionate impact from the regulations. The United States asserted that its regulations did not afford protection to domestic production, and that there was in fact no disproportionate impact.

The panel decided that US CAFE standards are a regulatory requirement affecting the internal sale of a product within the meaning of GATT Art. III:4, and not a tax within the meaning of Art. III:2. The panel found that the part of the CAFE standards that requires separate fleet accounting for foreign and domestic products places imported cars at a competitive disadvantage. It precludes US manufacturers of large cars from including small foreign-produced cars in their fleet calculations (thus discriminating against foreign small-car manufacturers), and likewise precludes foreign manufacturers of large cars from including US-produced small cars in their averaging (thus discriminating against foreign large car manufacturers). The panel said the possible adverse impact of the regulations on US large-car manufacturers (because they may not average with small foreign cars) could not be used to counterbalance the discriminatory impact imposed on foreign manufacturers. The panel decided that separate foreign and domestic fleet accounting was inconsistent with GATT Art. III:4. The panel similarly concluded that CAFE regulations that distinguished between products based on the foreign or US ownership of the manufacturer could not be consistent with GATT Art. III:4 since the distinctions in the regulations are not directly related to cars as "products."

The panel then addressed whether the provisions found contrary to Art. III:4 could be justified by the United States under Art. XX(g). It found that conservation of gasoline was within the range of policies mentioned in that article. The panel observed that the question whether the US measures were primarily related to the conservation of resources was not addressed to



CAFE standards in general, but only to the discriminatory elements the panel had found to be inconsistent with Art. III:4. The panel found that separate foreign and domestic fleet accounting did not serve conservation objectives (moreover, evidence suggested that by reducing imports of small foreign cars, separate accounting was contrary to the conservation objectives). The panel noted that CAFE regulations might apply to the fleets of foreign manufacturers in the absence of separate foreign and domestic fleet accounting, and that a CAFE arrangement that excluded separate fleet accounting and applied to import car manufacturers may, if properly designed, meet the conservation objectives of Art. XX(g). The panel rejected a further EC claim that the combined effect on EC products of the luxury tax, gas-guzzler tax, and CAFE standards constituted an additional inconsistency under Art. III.

In summary, the panel found only the separate domestic and foreign fleet accounting provisions of the CAFE standards to be inconsistent with the General Agreement. It may be hoped that this decision will alleviate some of the concerns that environmental NGOs have expressed with respect to the impact of the GATT on progressive environmental regulation.

*(c) Subcommittee on Trade and Environment*

In addition to the Marrakesh Decision and the panel reports, environment-related activity at the GATT in 1994 included several meetings of the Sub-Committee on Trade and Environment (the Subcommittee will be formally transformed into the Committee on Trade and Environment at the first meeting of the WTO General Council in 1995). The initial meetings of the Sub-Committee were largely devoted to administrative matters and the formulation of a work program. There also were important substantive discussions, however, in particular at the meeting of 15–16 September. Sub-Committee members debated the subject of charges and taxes for environmental purposes, including the application of border tax adjustments. They discussed the trade effects of environment-related product regulations, including recycling and reuse requirements, as well as eco-labelling measures. The role of NGOs in the Committee's activities was also actively debated. The United States took the lead in urging an enhanced role for NGOs, including their participation in meetings. Although most delegations appeared to recognize the need to increase transparency at the WTO, there was clear resistance to a participatory role from a majority of Committee members. The Chair of the Committee was authorized to hold informal consultations on this important issue.

*(d) Ratification of the WTO in the United States*

On environment-related issues, debate concerning approval of ratification of the WTO Agreement in the United States Congress mirrored the debate

concerning approval of ratification of the North American Free Trade Agreement (NAFTA) in 1993. Congress approved the WTO and its related agreements in December 1994 in the face of intense opposition from numerous environmental NGOs, likewise mirroring the outcome of the NAFTA debate. Perhaps more so than in respect to the NAFTA, the WTO approval debate in the United States focused on the alleged extent to which the sovereignty of the US government, and Congress in particular, would be undermined by the new WTO dispute settlement procedure. The new WTO dispute settlement procedure involves the quasi-automatic approval by WTO Members of the reports of dispute settlement panels and the creation of a new appellate body. Under the former GATT procedure, a consensus of all parties was required before a panel decision became the formal and binding judgment of the organization. Under the former GATT procedure, any party could block the adoption of a panel report, and thus in essence protect itself against an adverse decision. Environmental NGOs argued unsuccessfully to the Congress that the new quasi-automatic WTO dispute settlement procedure would put US environmental regulations at the mercy of a small number of dispute settlement panel members connected with the WTO who might not be sympathetic to the maintenance of high levels of environmental protection.

*(2) The NAFTA and Western Hemispheric Integration*

The NAFTA and the North American Agreement on Environmental Cooperation (NAAEC) entered into force on 1 January 1994. NAFTA-related activities with respect to the environment in 1994 centered largely on the establishment of administrative arrangements, such as the creation of the North American Commission on Environmental Cooperation (NACEC). The NACEC is based in Montreal, and the Executive Director of its Secretariat (Victor Lichtinger) has been appointed. As of the end of 1994, rules regarding implementation of the NAAEC complaint process were still under consideration. It does not appear that any formal demands for Secretariat factual determinations were made by private groups during 1994. Some environmental NGOs have expressed disappointment with the slow pace of NAFTA organizational efforts.

The NAFTA provides in Art. 103 that it takes priority over the GATT and other existing agreements to which the parties are party (other than certain environmental agreements per Art. 104). Article 103 does not specifically refer to GATT successor agreements, and this raises the issue whether NAFTA environment-related rules will take priority over comparable WTO rules. NAFTA rules will likely continue to take priority over those WTO rules that are continuations of prior GATT rules. However, it may be some time before this question is definitively answered.

During 1994, the US Congress refused to extend fast-track authorization

for negotiation of Chile's accession to the NAFTA, at least partially on the basis of Republican Party demands that its accession not include agreements such as the NAFTA supplemental agreements on labor and the environment. The Summit of the Americas Declaration, adopted in December 1994 by the Heads of State and Government of virtually all Western Hemisphere countries (*see* (→) *Conjunto Centroamerica-USA*), calls for conclusion of the negotiation of a Free Trade Area of the Americas by 2005. The Declaration calls for the creation of partnerships to promote environmental objectives and sustainable development. The governments support the convening of other regional meetings on sustainable development. The Summit of Americas Plan of Action recognizes the need to make trade liberalization and environmental policies mutually supportive.

Frederick M. Abbott

## 2. MULTILATERAL LENDING ACTIVITIES

During 1994, international financial institutions faced continued pressure to reshape their operational practices in order to increase transparency and embrace the goals of sustainable development. Among the most important reforms, particularly from an international law perspective, were the creation of independent inspection panels at the World Bank and several of the regional multilateral development banks (MDBs).

### (1) *The World Bank Group*

#### (a) *Is 50 Years Enough?*

This year marked the 50th anniversary of the signing of the Bretton Woods agreements creating the World Bank. Both the World Bank and its critics launched major efforts to evaluate, and reevaluate, the Bank's record and its ability to face today's challenges. In the largest coordinated challenge to the development model pursued by the World Bank, the "Fifty Years Is Enough" campaign, consisting of approximately 300 environmental, social, and development groups from around the world, questioned the efficacy of current development models for moving the poorest countries out of poverty and toward ecologically sustainable development. The Bank countered in what is proving to be a battle over both the history of the Bank and the future of development lending. This highly publicized and politicized debate will continue at least through 1996, when the Bank will celebrate its 50th year of operation.

#### (b) *The World Bank Inspection Panel*

On September 1, the World Bank's Inspection Panel began operations. The panel is authorized to receive claims about the bank's failure to comply