

THE INFLUENCE OF COMPLIANCE WITH ENVIRONMENTAL REQUIREMENTS ON COMMERCIAL COMPETITION

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ABSTRACT: *The gradual evolution of international trade and of environmental protection regimes continues to arouse conflict and contention opportunities. The international community is, in theory, engaged and involved both in trade liberalization and sustainable development in environmental matters. However, given the current system of economic activity, trade may also harm the environment.*

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One of the fundamental conditions for a functioning market economy, together with free movement of goods, persons, services and capital, is represented by an undistorted competition environment. Thus, traders, whether at national or European Union level should interact as freely as possible without any negative influences from the strong or privileged economic agents, associations of such agents or the state. In a functional market economy, respect for competition rules ensures economic progress, defence of consumer interests and competitiveness of products and services.

The gradual evolution of global, international trade and of environmental protection regimes continues to arouse conflict and contention opportunities. The international community is, in theory, engaged and involved both in trade liberalization¹ and sustainable development in environmental matters².

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¹ See the Uruguay Round. This was a round of trade negotiations held between September 1986 and April 1994 and that led to the transformation of GATT (General Agreement on Tariffs and Trade) into the WTO (World Trade Organization). See for more details on this process of transformation Elli Louka, "International Environmental Law. Fairness, Effectiveness, and World Order", Cambridge University Press, New York, 2006, p. 303 and following.

² See in this respect The United Nations Conference on Environment and Development (UNCED), also known as the Rio Summit, Rio Conference, Earth Summit held in Rio de Janeiro from 3 June to 14 June 1992. The Earth Summit resulted in the following documents: Rio Declaration on Environment and Development, Agenda 21, Convention on Biological Diversity, Forest Principles, Framework Convention on Climate Change. After ten years, the Johannesburg Summit was reissued on Environment and Development (24-26 August 2002), the event was known as Rio +10.

In principle, tracking performance of both objectives would be entirely possible and compatible³. According to the competitive advantages theory, trade enables specialization and requires states to produce goods and provide services to which they are effective. In other words, trade allows states to maximize production from a given quantity of raw materials available and this way of reasoning is a step forward in terms of sustainable development and environmental protection. Moreover, trade liberalization⁴ could ideally lead to the removal of state subsidies and of pricing policies that may cause artificial market distortions, on the one hand, and on the other hand, to a more efficient allocation of resources and encouragement of the use of clean technologies. A higher rate of income resulting from trade allows and leads to the generation of the necessary resources for investments aimed at protecting the environment.

However, given the current system of economic activity, trade may also harm the environment. As long as environmental externalities are not included in the prices of goods and services and are not taken into account in the decision making process, trade can be a catalyst for exaggerating the unsustainable patterns of economic activity, exacerbating problems related to pollution or the depletion of natural resources. In those situations where externalities are however incorporated (for example through an environmental tax), this process may take place invariably at different rates depending on each state. Even so, trade rules are established at international level and current GATT rules may not allow for each and every situation differences such as these between national efforts targeted towards environmental sustainability. Additionally, a state that has strict environmental regulations may fear that its economy will be undermined by competition coming from countries more relaxed in terms of environmental regulations (which might therefore have lower production costs for this reason)⁵.

Trade and environmental protection are therefore inextricably linked. Conflicts between trade liberalization and environmental protection have already erupted in some situations because some regulations drawn up in the idea of environmental protection and

³ There is an international concern regarding the interdependence of the two areas that presents interest for our work, interest resumed also in various provisions of international documents. See, for example, principle 4 of the Rio Declaration, according to which: "In order to achieve sustainable development, environmental protection shall constitute an integral part of the development process and cannot be considered in isolation from it." Agenda 21 also recognizes the need for international trade to ensure a climate of international support in order to achieve goals relating to environmental protection and sustainable development. See for a more detailed presentation of the problem Philippe Sands, "Principles of International Environmental Law", 2nd edition, Cambridge University Press, Cambridge, 2003, p. 940 and the following.

⁴ Free movement of goods and services between countries has represented, according to an opinion in the international doctrine, the exception rather than the rule in matters of international trade. States have regulated international trade through a series of tariff and non-tariff barriers, implicitly imposing restrictions on foreign products and services. The idea of trade liberalization, with the ultimate goal of protecting consumers interests, through the gradual elimination of these barriers launched in 1946 the negotiations that lead to the development of the World Trade Organization. See Elli Louka, cited above, p. 303.

⁵ See for a detailed presentation of the problem in Central and Eastern Europe: Andonova Liliana, "Transnational Politics of the Environment. The EU and Environmental Policy in Central and Eastern Europe", Cambridge, 2003; Andonova Liliana, "Openness and the Environment in Central and Eastern Europe: Can Trade and Foreign Investment Stimulate Better Environmental Management in Enterprises?", in „Journal of Environment and Development”, no. 12/2003, p. 177-204; Organization for Economic Cooperation and Development (OECD) "Environment in the Transition to a Market Economy", 1999, Paris.

sustainable development have been considered or interpreted as in fact raising barriers to trade.

1. USE OF TRADE MEASURES FOR ENVIRONMENTAL PROTECTION PURPOSES

The central goal of the General Agreement on Tariffs and Trade (hereinafter GATT)⁶ is to liberalize trade between the signatory or Contracting Parties. Article I of GATT provides the most favored nation clause, representing the provision included in trade and navigation treaties or in trade and payment agreements that binds signatory states to grant each other, in reciprocity conditions, all the advantages that have or will provide other countries in trade relations⁷.

GATT however, allows some unilateral trade restrictions in particular circumstances related to environmental protection⁸.

States may, therefore, prohibit or restrict imports of certain products that can harm their environment, as long as the applied standards are non-discriminatory between countries and between products of domestic or foreign origin. Reasons related to environmental protection and sustainable development have become increasingly invoked as a goal but also as a basis for the development and implementation of restrictive regulations in terms of trade, including here, primarily, measures aimed at controlling air pollution and toxic substances. However, any agreement that allows a restriction of trade is likely to fall prey to protectionist interests that use the environmental protection justification as a mask to hide intentions of a completely different nature⁹. To avoid such situations, there are intense concerns to ensure transparency of the standards set by these sort of measures.

2. PRODUCT STANDARDS

Generally, environmental standards apply to products or processes. Product requirements include rules or voluntary agreements governing issues such as labeling, packaging, recycling and recycled content. In an increasing extent, these requirements are based on estimates of product life-cycle, environmental impact during production, consumption and disposal of the product.

Clearly, these restrictions can be valuable tools for environmental protection policies, but enforcement of such standards and requirements on imported products may raise

⁶ Multilateral intergovernmental treaty signed in 1947 in Geneva, with 88 countries as contracting parties. It is applied de facto by 29 other countries. It was created under UN auspices and it represents the organizational-legal framework in which most countries negotiate a gradual reduction of customs duties, removal of quantity restrictions and of other non-tariff barriers, with the final goal of trade liberalization.

⁷ Usually this clause refers to the advantages that the signatory states undertake to grant each other in applying customs duties on import/export/transit, at the issuance of licenses for import/export, in the field of maritime and river navigation and in the legal situation of economic agents, trade representative or any other types of legal person exercising acts of trade in the territory of the other signatory countries.

⁸ See provisions of art. XX of the Agreement.

⁹ Duncan Brack, "Trade And Environment: An Update on the Issues", The Royal Institution of International Affairs, 1997.

numerous difficulties. Information, especially in terms of life-cycle assessments, could miss in part or fully. The characteristics chosen by the manufacturer for labeling may reflect the environmental priorities existing at national level and the criteria used in different countries, which have trade and competition relations, may vary greatly. Schemes used in a particular state that place the focus on a particular product could create artificial advantages for products that are not subject to similar standards in the country of origin, but which undoubtedly have a significant impact on the environment both from the production and the consumption point of view. Packaging standards that require re-usage (eg bottles) clearly create problems for non-domestic producers. Not only these combined problematic issues create barriers to trade and competition (particularly for countries undergoing economic development) but may also lead to a poor allocation of financial resources and potential inappropriate environmental policies.

One of the main goals of the Agreement on Technical Barriers to Trade (TBT¹⁰ below) is to ensure that such regulations do not create unnecessary obstacles to international trade, and environmental protection is highlighted as a legitimate objective which underlies the technical requirements and standards. The agreement calls for, *inter alia*, that all such measures are transparent to the greatest possible extent and based on international standards. CTE, who spent most of the discussions on this point on a voluntary eco-labeling system, stressed the importance of compliance with the Agreement's provisions together with the principle of open access to foreign products. OECD has proposed a series of steps in order to minimize the undermining of trade, including here also transparency, the transitional adjustment period, attention regarding non-domestic conditions, particularly the special needs of developing states as well as transition economies, greater harmonization of life cycle methodologies, a requirement for true environmental justification for all measures of this nature.

A specific issue related to trade - imported products - is the export of nationally prohibited goods. Goods that are restricted on domestic markets, on the grounds that they pose a danger to health or life of animals, humans or plants or the environment can sometimes be legally exported. This reality can cause problems to the importing States, where information on whether that product is prohibited or not in the country of origin or the reasons why it is prohibited may be missing: exporters may draw-up false documents accompanying the goods, customs authorities (particularly in the case of developing countries) may lack the adequate means of testing imported products, and an undeveloped or ineffective legislation on consumer protection could, for example, permit the marketing of such products even after their expiry date.

The legal requirement of a so-called "prior informed agreement" for export is becoming a tool increasingly used in the European Union (an example for the requirement of an agreement of this type is the case of export of restricted regime chemicals) and may

¹⁰ Recognizing the importance of standardization, a cooperation between the WTO and the main global standardization organizations was initiated. To this end the Agreement on Technical Barriers to Trade was signed, under which WTO members (151 in total) are required to ensure that technical regulations, voluntary standards and conformity assessment procedures do not create unnecessary obstacles to trade. See for more details, Nicolai VĂLCOV, "Comitetul electrotehnic român participant activ la standardizarea internațională", paper presented of the Symposium "Tendințe în dezvoltarea industriei electrotehnice europene. Probleme actuale în electrotehnica românească", Bucharest, 2009.

represent another step forward in the way of progress towards an effective environmental protection.

3. PROCESSING AND PRODUCTION METHODS

Environmental protection provisions based on processing and production methods, as opposed to product standards, interact more deeply and frequently with trade. Despite the fact that GATT provisions on similar products were not regulated with strict reference or taking account of environmental issues, a GATT panel held that these can also be applied in the famous case of 1991 on tuna and dolphin between the U.S. and Mexico¹¹. The panel determined that the trade restriction with tuna (U.S. banned imports of tuna from Mexico because they used for catching fish nets that also killed dolphins) consists in a violation of GATT provisions because the discrimination of that certain product is made on the basis of how the product was produced and not on its features.

The key issues addressed in this case to the WTO could be summarized in two, as follows:

- can a state impose environmental regulations to another state?
- do trade rules allow taking of action against the method used for the production of a good?

The decision of the panel regards on the one hand the fact that the embargo imposed by the United States is not legal because of the grounds on which it is based, namely that Mexican environmental regulations do not meet U.S. requirements, and on the other hand the fact that the rules established by the GATT do not permit a state to use trade measures in order to try to impose its own laws in another country.

What was the reasoning behind the Panel's decision? If the U.S. arguments would have been accepted, and the measures taken by the U.S. would have been considered acceptable, then any State could at any time prohibit the import of a certain good from another country just because the exporting country has different environmental, health and social policies of its own. This scenario could easily reach the situation where any country could apply trade restrictions unilaterally - and such actions would be aimed not only at strengthening of its own legislation, but also to impose their own standards in other states. Clearly, a number of possible abusive protectionist measures would arise.

The meaning of "similar products" notion has become one of the most problematic issues in the environment-trade relationship. In 1994, another GATT panel, giving a decision on a dispute between the EU and the U.S. on imported cars, gave a slightly more relaxed, less encroached definition, considering that vehicles with different fuel efficiency standards might not be regarded as similar products. It however outlined a series of strict boundaries for this conclusion, arguing that GATT Article III refers only to "a product as a product, from the moment it is placed on the market until its final consummation."¹² Elements related to the manufacturing of the product before it can be placed on the market are therefore irrelevant. Another GATT Panel considered in 1996 that the domestic gas and

¹¹ There are a number of other cases against the U.S. brought before the WTO Committees on the extraterritorial application of U.S. environmental law and violation of GATT provisions. See for a presentation of these cases, Elli Louka, cited above, p. 386-394.

¹² GATT Case - US: Taxes on Automobiles (1994).

the chemically identical imported one are identical products regardless of the environmental standards that both producers have to comply with.¹³

Although many discussions may arise about the point of view adopted by the GATT, trade measures based on environmental issues can be difficult to justify. Different countries in different parts of the world vary considerably in terms of ability to assimilate pollution, depending on factors such as climate, population density, different levels of existing pollution, prioritization of environmental risks, etc. Environmental regulations best suited in the case of industrialized nations, characterized by high population densities and average pollution subject to more than 200 years, might be completely inappropriate for newly industrialized countries, with less dense populations and levels of pollution legacy. Despite these obvious realities, trade measures based on processing and production processes seek to impose higher environmental standards, regardless of anything. Following the logic of economics, imposition of similar production processes can deny the so-called comparative advantage in terms of commercial competition, which starts from the assumption that each state has different production costs. No wonder the reaction of developing states, who see the attitude of those who wish to introduce such measures as protectionist in nature.

Measures based on production processes are increasingly becoming more and more important in sustainable development strategies. Especially in those cases when the use of energy is required (basically any production activity), the resulted pollution has as source the production process itself and not the product. In terms of trade measures, an important distinction must be made between those production processes that cause pollution within the boundaries of that particular state and those causing cross-border or global pollution.

Among the few subjects on which there is broad consensus concerns the fact that the nonusage of commercial practices that distort the market as well as subsidies in agriculture or energy areas would have a beneficial effect both on trade (leading to a more efficient allocation of resources) and environmental protection (removing support from unsustainable activities in terms of environmental protection). Moreover, removing the increasing tariff system practice, whereby developing states pay higher taxes for the export of finished products than raw materials and primary products (especially common in the case of timber and wood products), would encourage economic diversification and would help close environmentally harmful systems of resource extraction.

4. INTERNATIONAL COMPETITION

The impact of environmental regulations on trade competition and competitiveness is subject to extensive debates. Companies located in countries with very high environmental standards and consequently compliance costs might fear being shot down by competing

companies from states with less stringent environmental regulations and standards and thus lower compliance costs. Theoretically, this could lead to relocation of entire industries to states with lower environmental standards, the so-called "pollution havens". Among the

¹³ GATT Case - US: Standards for Reformulated and Conventional Gasoline (1996).

solutions proposed in order to avoid a generalized decline of environmental standards includes the equalization of costs through a series of countering obligations. The end of these measures (also known as eco obligations) is to equalize the market by ensuring that products imported from countries with lower environmental standards are subject to tax obligations or fees that counter the default subsidy due to lower environmental protection costs.

In practice, however, there have not been massive relocation of industries from countries with stringent environmental standards to those with lower ones. For most industries, the costs attributable to environmental regulations and financial obligations arising from these seldomly exceed a threshold of 1.5% of the total production cost.

On the other hand, states that initially had low environmental standards are not immune to pressures exercised in order to raise these low standards and align them with a international minimum standard. Indeed, one could argue that in a dynamic business environment, high environmental standards could act as a spur for innovation and competitive success. Trade can be a key factor for increasing environmental standards, as the producers want to expand the market horizons of the products they manufacture to countries with high environmental standards. Competitiveness issues may become more relevant and topical as the costs derived from environmental standards compliance increase.

5. DISPUTE RESOLUTION

The WTO Agreement on conflict resolution has established a unified system that applies to all WTO agreements¹⁴. This Agreement operates in more stringent time limits and is more transparent than the GATT system it replaces. The resolutions given by the dispute settlement committees are automatically adopted by WTO members unless they decide otherwise by consensus. WTO Members have stressed the importance of respecting this procedure in case of trade - environment interconnections – although recognizing at the same time that it does not fall within its jurisdiction to question the merits of environmental standards and national and international objectives.

6. CONCLUSIONS

The environment-trade dispute is certainly far from finding a solution or answer. On the contrary, increased trade together with the accumulation of evidence of the increasingly diverse and consistent global environmental degradation, along with pressure for international action that will result, seem to lead to increasingly more serious controversies. Additionally, it may be that the World Trade Organisation by itself will not be able to resolve the trade-environment conflict. One of the problems inherent in this issue is that debates are conducted within, but rarely between, two separate communities, each encompassing governments, international organizations, NGOs and businesses: some of these groups are motivated by trade liberalization and others by environmental protection. All of these formations possess different assumptions, values and means of operating,

¹⁴ See for more details Richard Eglin, “ Environmental Sustainability and The Global Trading System“, The Clarke Center at Dickinson College, 1997.

and tend to lack a full understanding and appreciation of each other's position. Therefore, it is highly unlikely that a middle ground solution is to be found in the near future. Those concerned about the World Trade Organisation trade rules getting in the way of environmental policy-making should note that a wide range of trade-related measures, taxes and regulations can be applied by World Trade Organisation Member governments to protect environment resources without running a risk that they will face a commercial challenge under World Trade Organisation rules.

