

## **SUSTAINABLE PROSPERITY / CISDL**

### **COP 16 EXPERTS PANEL REPORT**

#### **Innovative Sustainability Instruments for the Green Economy: A Law & Policy Experts Panel on Strengthening Carbon Markets by Integrating the Environmental and Social Impacts of Trade & Investment**

*Thursday, 09 Dec 2010,  
Azul Sensatori, Cancun, Mexico*

#### **Executive Summary**

Sustainable Prosperity, a green economy policy research network based at the University of Ottawa, and the Centre for International Sustainable Development Law (CISDL), based at McGill University, hosted an international policy experts panel during the 16<sup>th</sup> Conference of the Parties to the UN Framework Convention on Climate Change, in Cancun, Mexico, on Thursday, December 09, 2010, as part of the *ICTSD Symposium on the Role of Trade and Markets in Addressing Climate Change and Sustainable Development*. The Experts Panel Event focused on the role that new instruments, such as impact assessments and carbon pricing tools, can play in helping to address climate change and secure more sustainable development. It addressed questions such as what key climate change challenges have been raised in recent impact assessments of trade and investment treaties, and how are new market based instruments being deployed to address them; how can these instruments support the transition to a low carbon economy and harness trade & investment for sustainable development; and what can be learned from recent EU, Canada and US experiences, and from policy experiments in developing countries.

The Experts Panel Event was chaired by Ms Sarah Mason-Case, Associate Fellow, CISDL / McGill University. It started with a joint keynote by Prof Markus W. Gehring, Tutor in Sustainable Development Law, Cambridge University / Lead Counsel, CISDL / University of Ottawa Jean Monnet Chair in Sustainable Development Law, who is leading a research project supported by Sustainable Prosperity and the SSHRC, and Prof Marie-Claire Cordonier Segger, Senior Director of Research for Sustainable Prosperity, who also directs the Centre for International Sustainable Development Law (CISDL). Excellent and substantive presentations of research on market based instruments were made by speakers Prof Konstantia Koutouki, CISDL Lead Counsel / University of Montreal, who presented the outcomes of her research on carbon offsets and ecosystem services among First Nations communities; Dr. Moritz von Unger, Senior Legal Advisor of Climate Focus; and by Lic. Andres Pirazzoli, LL.M., Asociación Interamericana para la Defensa del Ambiente (Chile). Two Canadian law graduate students, Benoit Mayer and Sarah Mason-Case of McGill University, also received awards for their work on two leading Legal Research Papers that were launched as part of a Series of 10 papers at the COP 16. Prof Marie-Claire Cordonier Segger, Senior Director of Research for Sustainable Prosperity, introduced Dr. Charlotte Streck, Director, ClimateFocus and Lead Counsel for Climate Change, CISDL and she presented the award to the students.

## Building the Green Economy for Sustainable Development



*Left to right: Moritz von Unger, Anr s Pirazzoli, Sarah Mason-Case, Markus Gehring, Marie-Claire Cordonier Segger, Konstantia Koutouki*

Market-based instruments are the primary means of finance for climate change mitigation. Effective financial instruments are also necessary to provide support and additional resources for sustainable development more generally.

Trade and investment rules are a double-edged sword. They can encourage the adoption of innovative new market-based instruments in key instances, but can also have repercussions on their effectiveness. Moreover, trade and investment rules can indirectly affect environmental integrity and socio-economic development if they are negotiated without due regard for externalities, such as natural resource use and greenhouse gas emissions.

This legal experts panel organized by the CISDL and Sustainable Prosperity provided negotiators, academic experts, climate policy-makers and other interested participants with a series of short, clear and up-to-date legal briefings on the top trade and investment law issues related to climate change, focusing on how to promote the identification and adoption of innovative market-based instruments through the application of international law on trade, investment and climate change.

## Activating Innovative Sustainability Instruments in Bilateral, Regional and Free Trade Agreements

The keynote speakers, Professors Markus Gehring and Marie-Claire Cordonier Segger, are specialists in international trade and investment law for sustainable development. They commenced the conference with a high-level discussion on the climate aspects of bilateral, regional and free trade agreements, examining how these economic treaties might promote the adoption and use, in appropriate circumstances, of market-based instruments for a low-carbon economy.

Prof Markus Gehring spoke to the opportunities and challenges that the rules of the World Trade Organization (WTO) can pose for stimulating innovative trade and investment for a low-carbon economy. His keynote was based on a survey, supported by Sustainable Prosperity and SSHRC, of the environmental pricing reform measures that have been notified to the WTO's Trade and Environment Committee over the past two decades. This survey found that generating and redirecting economic resources for a low-carbon economy may involve several distinct strategies.

### *International trade*

- building comparative advantages of diverse renewable energies
- increasing trade in low-carbon technologies
- redirecting subsidies and other non-tariff barriers to trade in climate-friendly goods

### *Private investment*

- private and intra-company carbon markets
- equity investments in low-carbon projects
- increased private research, development and testing of low-carbon technology
- private commercialization of clean technologies

### *Domestic measures*

- emissions trading
- carbon taxes
- clean subsidies
- renewable energy support/feed in tariffs
- energy efficiency support/labels
- carbon budgets
- bioenergy projects
- other carbon pricing instruments

The relationship between climate change and trade law is not black and white but grey. The WTO is already struggling with this “grey” relationship through its Committee on Trade and Environment (CTE). The CTE maintains a WTO Environmental Database, which is updated annually with all environment-related notifications. The adoption of new instruments such as these has become common in WTO Member countries, as was demonstrated by Professor Gehring’s research. However, these strategies may overlap conflict with trade and investment law if they are characterized as impermissible barriers to trade under WTO or trade agreement rules.

Trade and investment law can also promote the adoption of market-based instruments to enhance sustainable development. For instance, if negotiations are successful, they can take down barriers to the flow of low-carbon goods and services, as is being seen now in the WTO Doha Round of trade negotiations to liberalize trade in environmental goods and services. Investment treaties, according to some experts, may also promote stability and thereby helping countries to attract capital-intensive projects such as renewable energy and clean technology.

One key ingredient in this process is the effective use of sustainability impact assessments. If these assessments are carried out prior to the negotiation of a new trade and investment agreement, they can increase information and participation, and effectively identify tailored mitigation and flanking measures, including opportunities for the adoption of appropriate market-based instruments such as carbon pricing tools, tradeable fishing quotas, or habitat banking mechanisms, among others identified in the survey of the WTO TREMS Database. Trade and investment impact assessments could apply cutting-edge new working methodologies to international trade and investment agreements (i.e. European

Union's Sustainability Impact Assessments, United States Environmental Reviews and Canada's Environmental Assessments). Currently, impact assessments are underutilized, but they have potential to create important synergies that trade and investment have to offer, including for carbon markets and other flexible mechanisms.

Marie-Claire Cordonier Segger elaborated on the potential of trade and investment law to facilitate a low-carbon economy, as a complement to the important efforts being made by States in the UNFCCC and the Kyoto Protocol negotiations. Presently, global rules governing low-carbon trade include the WTO Agreements, and over 350 free trade agreements (FTAs) and Energy Charter-type initiatives. The rules governing low-carbon investment include over 2700 bilateral investment treaties (BITs), many of which adopt and apply the rules of the UN Commission on International Trade Law (UNCITRAL) and the International Centre for Settlement of Investment Disputes (ICSID). The WTO Doha Declaration also identifies sustainable development as one of the objectives of the world trading system. Examples of existing BITs, FTAs and RTAs with explicit sustainable development provisions include, NAFTA, Canada-Chile FTA, US-Chile FTA, Mercosur Framework Agreement on the Environment, UK-Uruguay BIT, and Germany-Trinidad and Tobago BIT.

Trade treaties may support sustainable development and assist in government efforts to address climate change by facilitating the adoption of market-based instruments for the low-carbon economy, including:



#### *Potential benefits of trade treaties*

- stimulating innovations in clean technology development (agriculture, transport, construction, forestry, industry, energy)
- making low-carbon goods and services more available (industry and consumer access to low-carbon goods and climate-friendly services)
- stimulating green growth and providing advantages to early actors (comparative advantages in efficiencies, reputation gains and consumer goodwill, avoiding litigation and potential liability)

BITs, FTAs and regional trade agreements (RTAs) can achieve those potential benefits by developing 'value-added' social and environmental cooperation strategies. These may take the form of (a) parallel agreements, exceptions or chapters for cooperation on the green economy; (b) the development of institutions for climate cooperation (i.e. North American Commission for Environmental

Cooperation); (c) common work programmes on specific adaptation or mitigation projects; (d) impact assessments; and (e) reporting or complaints mechanisms.

There are now examples of such measures, adopted within the text of economic cooperation and free trade treaties, from which much could be learned, and upon which improvements could be built. Prof Cordonier Segger's research, together with Prof Gehring, has surveyed over 68 of these regional and bi-lateral trade and investment treaties, and it will be particularly interesting to see what is agreed in the coming Canada – European Union Economic Cooperation Agreement.

## **Economic Instruments in the UNFCCC and Kyoto Protocol**

Dr. Moritz von Unger introduced the attendees to instruments for the green economy in the UNFCCC and the Kyoto Protocol. Trade and investment under the UNFCCC process is limited because only industrialized countries that have signed onto the Kyoto Protocol have emissions targets. There are three flexible mechanisms under the Kyoto Protocol: (a) carbon emission trading between industrialized countries, (b) Joint Implementation (JI) of emission-reduction or emission removal projects between industrialized countries and (c) the Clean Development Mechanism (CDM), which allows industrialized countries to invest in emission-reduction or emission removal projects in developing countries for credit. The CDM has taken on speed since the Kyoto Protocol commitment period came into effect in 2005. There are approximately 4000-5000 projects expected to have been approved by 2012, totaling USD 1 billion.

Nevertheless, more financial and technical investment is needed for climate change mitigation and adaptation and recent efforts reflect the scaling-up of prior carbon market mechanisms. At the 15<sup>th</sup> Conference of the Parties (COP) in Copenhagen, industrialized countries pledged USD 100 billion a year by 2020 in finance. At COP16, the parties adopted the NAMAs approach (nationally appropriate mitigation actions) first enunciated in the Bali Action Plan and which may assist in preparing nation-wide and sector-wide economies for climate finance. Furthermore, although new market mechanisms have not yet been designed for the UNFCCC, they are on the agenda for COP17 in Durban.

## **Renewable Energy, Private Sector Investors and Indigenous Communities**

Professor Konstantia Koutouki addressed the impact of international trade rules on renewable energy projects using the two examples of feed-in-tariffs (FIT) and private investment agreements with Indigenous communities. As an active member of the Sustainable Prosperity policy research network, she based her presentation on the outcomes of a research project that she has just completed, together with students Tracey Coates and Alexandra Harrington, supported by Sustainable Prosperity and the SSHRC. Concerning the former, Professor Koutouki discussed the recent FIT initiative in Ontario, which has been challenged by Japan as a subsidy in contravention of Canada's WTO commitments. The Ontario FIT sets a fixed price for electricity generated by renewable sources such as biomass, biogas, landfill gas, and wind and solar power. However, it also requires companies to award a percentage of

their project content to Ontario goods and services. In response, Japan has filed a complaint with the WTO (Dispute DS412), claiming that, *inter alia*, the domestic content requirement constitutes an impermissible subsidy and is a protectionist trade measure. The resolution of that dispute is outstanding and both the United States and the European Union have joined consultations thereon.

On the subject of private investor and Indigenous community partnerships for renewable energy, Professor Koutouki remarked that impact assessments can act as an important safeguard. Indigenous communities are increasingly embracing projects with foreign private partners instead of domestic governments (i.e. Membertou First Nation joint-venture business partnership with GrupoGuascor of the Basque Country of Spain, to market renewable energy in US and Canada). Special considerations arise from those partnerships that require impact assessments not only of the environment but also of culturally appropriate forms of economic development for Indigenous communities. As suggested previously by Markus Gehring and Marie-Claire Cordonier Segger, existing state regulated impact assessments can be utilized in private trade and investment agreements to account for both the potential environmental and development consequences of investments.

## Implementing Innovative Instruments for the Low-Carbon Economy in Chile



Jurist and expert in Chilean environmental law, Andrés Pirazzoli, concluded the experts panel with an example of the specific measures that Chile has adopted to promote the low-carbon economy, and to respond to the country's environmental impact assessments of development projects in a way that can to meet its international climate change promises. In August 2010, Chile announced that it would implement NAMAs to achieve a 20% deviation below the business-as-usual emissions growth trajectory by 2020, as projected from the baseline year of 2007. The sectoral focus of Chile's commitments is energy efficiency, renewable energy, land use and forestry.

The Chilean Strategic Environmental Assessment (SEA) is a systematic and formal pre-project approach to include environmental aspects in decision making for zoning and land use planning. The SEA applies to policies, plans and programs in an effort to internalize environmental costs and assess the impacts of a plurality of projects.

Despite the stated preventative approach of the Chilean SEA, however, Pirazzoli recommended that improvements be made to the structure of the SEA in order to further advance climate change mitigation. Beyond its established terms, the SEA could include:

*Innovative impact assessment considerations*

- the study of alternatives when assessing project adequacy
- valuation of environmental ecosystem services
- consideration of cumulative impacts
- consideration of the full energy life cycle of projects
- evaluation of greenhouse gas use on projects and related policy for mitigation

While Pirazzoli identified the above considerations as supplementary to the Chilean SEA, his suggestions are innovative instruments that could be employed in yet other circumstances to improve upon the benefits of impact assessments in international trade and investments law for the green economy.

## **Conclusions**

The relationship between international trade and investment law is not black and white but grey. WTO and free trade agreement rules can have negative repercussions on environmental integrity and socio-economic development, if they allow projects to proceed without due regard for natural resource use, greenhouse gas emissions and benefit sharing, among others. Nevertheless, trade and investment law tools can also enhance sustainable development by stimulating the green economy and by requiring tailored assessments of project impacts.

In this law and policy seminar, expert panelists specialized in international and domestic trade and investment law addressed today's key challenges at the intersection of trade and environment. They answered questions such as: what obstacles can trade and investment law pose to climate change mitigation and adaptation measures; how are new market based instruments being deployed; how can those instruments support the transition to a low carbon economy and harness trade and investment for sustainable development; and what can be learned from recent EU, Canada and US experiences and from policy experiments in developing countries?

Generating and redirecting finance for a low-carbon economy involves various instruments that could be construed as barriers to trade liberalization contrary to WTO and free trade agreement rules. Innovative instruments include: building comparative advantages of renewable energies, applying subsidies to trade in climate-friendly goods, emissions trading, energy efficiency labels and other carbon pricing instruments. The permissibility of those instruments is a live debate at the WTO, including within the Committee on Trade and Environment, generally, and in Japan's complaint against Canada for Ontario's FIT program.

Arguably, trade treaties such as BITS, FTAS and RTAS, can obviate certain WTO and free trade agreement rules by developing "value-added" social and environmental strategies. Parallel agreements, exceptions and chapters on the environment can promote cooperation on the green economy. Trade and investment partners can also create institutions for climate change mitigation and adaptation and common work programmes. As a result, trade treaties can stimulate clean technology development;

increase the availability of climate-friendly goods; and provide competitive advantages in efficiencies, reputation gains and consumer goodwill.

Of particular importance in addressing the challenges of trade and investment for sustainable development are impact assessments. Impact assessments, such as the EU's Sustainability Impact Assessments and Chile's Strategic Environmental Assessments, are already existing domestic working methodologies that reveal unrecognized synergies: they can assist with monitoring, evaluation and accountability based on environmental and socio-economic criteria and at the same time promote green investments. They can identify opportunities where market-based instruments for the green economy might be useful, and effective. For instance, Chile's SEA is a pre-project approach that identifies measures to take environmental aspects into account in decision-making on land use planning, and can support both the valuation of ecosystem services, and the adoption of carbon offset programs from reforestation and other reductions in emissions from deforestation and land degradation. Additionally, impact assessments can be used to ensure culturally appropriate forms of development for Indigenous communities, inspiring new renewable energy private partnerships. It is important, in this regard, to focus on asking the right questions, and to update the laws and policies on impact assessment so that they take non-tradition, non-command and control instrument choice options into account.

Trade and investment law can inspire the use of market-based instruments for sustainable development, indeed, there is a serious effort being made to design, adopt and implement such instruments in developed and developing country trading partners. However, these instruments are as novel as the green economy itself and continue to evolve alongside it. Therefore, the expert panelists concluded this session by offering concrete areas for improvement such as incorporating the valuation of ecosystem services into market based approaches to sustainable development, and designing new tools to monitor and track the cumulative impacts of multiple projects in impact assessments. In sum, ongoing improvements in trade and investment law are real and encouraging for the success of a low-carbon economy, but much remains to be done.