PREPARATORY COMMITTEE FOR THE WORLD TRADE ORGANIZATION

RESTRICTED
PC/SCTE/M/3/Rev.1*
12 October 1994

(94-2063)

SUB-COMMITTEE ON TRADE AND ENVIRONMENT

REPORT OF THE MEETING HELD ON 15-16 SEPTEMBER 1994

Note by the Secretariat

Revision

1. The Sub-Committee on Trade and Environment held its third meeting on 15-16 September 1994 under the chairmanship of Ambassador Luiz Felipe Lampreia of Brazil. The agenda for the meeting, contained in PC/AIR/18, was adopted.

2. The Chairman recalled agreement at the July meeting to focus this meeting on the third item of the work programme, namely:

> "The relationship between the provisions of the multilateral trading system and:
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> (a) charges and taxes for environmental purposes;
> (b) requirements for environmental purposes relating to products, including standards and technical regulations, packaging, labelling and recycling."

He recalled that at the July meeting some delegations had indicated that this item could address measures such as packaging and labelling requirements including re-use, recycling and recycled content requirements, disposal, and deposit refund systems; energy taxes and other internal taxes for environmental purposes; emission charges; tradeable permits; waste management requirements, and requirements for life cycle analysis.

3. He referred to document TRE/W/20, entitled "Border Tax Adjustment", as a useful basis for initial discussion. Other relevant documentation included L/7402, TRE/W/3, and Add.1 and Add.2, TRE/W/4, TRE/W/6, TRE/W/9, TRE/W/11, TRE/W/12, TRE/W/13, TRE/W/15, TRE/W/16/Rev.1 and TRE/W/21. He suggested taking up first sub-item (a) charges and taxes and then sub-item (b) product requirements.

(a) Charges and taxes for environmental purposes

4. The representative of Argentina considered that this item initiated analysis of economic instruments that could be used in environmental policy to achieve what was known as the "internalization of environmental costs". In the Rio Declaration (Principle 16), the need to internalize environmental costs in order to achieve environmentally sustainable development was accepted. Nevertheless, this posed a challenge for possible consequences on competitiveness and international trade. If a country internalized environmental costs, it could lose competitiveness compared with another country that did not. This concern was legitimate to a point; finding this "point of legitimacy" would be a substantial part of the Sub-Committee's work which should start from the recognition that each country had a different endowment of economic resources, different abilities to absorb pollutants and different social priorities.

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* English only

5. It was these differences that gave rise to comparative and competitive advantages that justified and underpinned the growth of international trade. Nevertheless, the environment had to be preserved and economic resources had to be invested to look after it. This was not only costly, particularly for developing economies, but also could have trade consequences that went beyond those of healthy competition. It was therefore necessary to find valid approaches so that those responsible for designing national environmental policies could minimize the adverse trade effects.

6. The economic policy instruments that could be used in environmental policy might be classified into two major categories: (i) "market instruments", such as charges, taxes, tradeable emission rights, financial incentives and so forth; and (ii) regulatory measures, better known as "command and control" measures, chief among which were prohibitions and tolerated emission levels. Both categories sought to internalize environmental costs. However, the "market instruments" did so more transparently and respected price formation systems. Consequently, the "Rio Declaration" (Principle 16) considered that priority should be given to this type of instrument. The OECD also recommended the use of market instruments rather than "command and control" instruments, including in particular fiscal instruments, i.e. those that directly affected a product (thus discouraging its consumption) or a specific process and production method (PPM) (thus discouraging its use).

7. His delegation believed that the focus of the debate should be on the first of these types of fiscal instruments, namely taxes or charges that directly affected a product. This kind of tax, unlike those which affected PPMs, could be the object of border tax adjustment (BTA), which would make it possible to neutralize the possible adverse consequences of environmental policy on international competitiveness. In this way each contracting party could individually, and consistently with GATT Article III, estimate the environmental externalities generated by a product in its territory, whether during the production, consumption or disposal stage.

8. The environmental externalities that each country decided to internalize through a fiscal instrument directly affecting a product could then be discounted from the price of the exported product. Conversely, in the case of imports the environmental externalities produced during the consumption and disposal stage could also be the object of a border adjustment. Each contracting party would thus estimate and take responsibility for exclusively those environmental externalities produced within its own jurisdiction. This would not include environmental externalities with cross-border or global consequences, which would be the subject of discussions in the Sub-Committee in October.

9. This type of fiscal instrument had three major advantages from the trade standpoint. First, it provided a GATT-consistent manner for dealing with local producers' concern with respect to the possible adverse effect of environmental policy on their competitiveness. Second, it was relatively transparent, which facilitated quantification of the environmental cost and consequently created less room for dispute. Third, it preserved the ability of each contracting party to estimate the environmental externalities produced in its territory and the desirability of internalizing them.

10. To be able to "internalize environmental costs", it was necessary to begin by identifying and removing any distortions that existed in the price system. This aspect would have to be covered by discussions in November on the environmental benefits resulting from the elimination of trade restrictions and distortions. Nevertheless, he pointed out that in order to be able to internalize environmental costs, the first goal was that the price of goods and particularly commodities had to be equal to the marginal private cost of their production and distribution. It was therefore necessary to begin by removing subsidies. This situation was defined by the OECD

as the point at which the marginal cost of pollution abatement and the marginal cost of environmental damage were equal.[1]

11. This situation was also discussed in a document by the UNCTAD Secretariat as the point at which the price of goods (particularly commodities) was equal to the marginal social cost of production and distribution of the goods.[2] Only then could environmental costs be internalized or integrated into the system of price formation and countries thus be able to implement an environmentally sustainable economic policy as agreed in the Rio Declaration. In focusing on the taxes and charges which GATT Article III allowed to be adjusted at the border, the Sub-Committee should take advantage of the work already carried out by the OECD. The Sub-Committee's work could in turn serve to mobilize technical cooperation aimed at tackling both the problem of drawing up legislation compatible with the multilateral trading system and that of its enforcement. He stressed the importance his delegation attached to the need to "internalize environmental costs", for which it was necessary to begin by identifying and eliminating subsidies that had negative environmental externalities. On this point his delegation thought it would be desirable to have a Secrretariat document to facilitate the discussions in November when the Sub-Committee dealt with the environmental benefits resulting from the elimination of trade restrictions and distortions.

12. The Representative of Egypt said the possible increased recurrence in the near future of taxes and charges for environmental purposes, such as consumption taxes, product charges, emission and administrative charges, must be noted. Such measures should be constrained mainly by the requirement that they not amount to a higher level of protection for the like domestic product or lead directly or indirectly to discrimination against imports. The provisions of the relevant GATT Articles should prevail.

13. However, a similar distinction should be made between taxes on products and taxes on processes. In essence, whereas environmental product charges (namely indirect taxes) like environmental product standards might be applied to like imported products, the main challenge to the trading system was in the application of environmental process taxes (namely direct taxes). Irrespective of whether a tax was a direct or an indirect tax, the environmental benefits would accrue to the consuming country. Therefore it might be argued whether it would be justified to impose such a tax at the border at all.

14. Another point of contention was with respect to the necessity of differentiating between the purpose of an environmental tax, whether it was designed to raise revenue or for broad policy purposes such as discouraging or encouraging the use of a particular PPM. This raised the question of whether different interpretations of BTA were warranted and where to draw the line between environmental taxes that achieved policy objectives and those that were protectionist. Another question was when should such taxes be levied only on domestic products and when should they be extended to like imported products. He concluded that attention should be devoted to these issues in the future and that account should be taken of analytical work being done in UNCTAD.

15. The representative of Mexico noted that the EMIT Group had only briefly discussed taxes and charges, whereas considerable headway had been made in analyzing product requirements and regulations. He recalled that the main aim of the Sub-Committee's work programme was to make "international trade and environmental policies mutually supportive" and he asked what would be

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[1](OECD "Environmental Policy: How to Apply Economic Instruments", page 11; Paris 1991)

[2] ("The Internalization of Environmental Costs and Resources Values: A Conceptual Study", page 10; UNCTAD/COM/27 of 10 June 1994)

the most efficient way to achieve this aim through the use of charges and taxes for environmental purposes? This aim would not be achieved simply by ensuring "legalistic" compatibility between the rules of international trade and these instruments; the compatibility needed between these two elements in order to reach the goal of sustainable development was more a matter of substance and, at the same time, must be practical.

16. Therefore, before launching into a discussion of the legal relationship between the provisions of the multilateral trading system and charges and taxes for environmental purposes, he believed the implications and practical effects of applying these instruments, in particular on imported products, had to be examined. An analysis of such effects was the best starting point for assessing and then for promoting mutual support between trade and the environment in this area. He proceeded to look at these aspects, not from a national standpoint but with a view to developing ideas to stimulate an exchange of opinions in a cooperative spirit.

17. He outlined two fundamental parameters of instruments to ensure that they would be designed to make trade and the environment mutually supportive: they must be ecologically useful and efficient, otherwise the risk of instigating trade distortions or disputes would be pointless; and they must not provide a vehicle for disguised protectionism, otherwise they would be protecting inefficient industries instead of the environment. Leaving aside the question of GATT obligations to avoid looking at purely trade-related legalistic or technical aspects at this point, there were at least four practical considerations with regard to the application of charges and taxes in respect of interaction between trade and the environment: valuation, diversity, effectiveness and competitivity.

18. Regarding valuation, he noted that charges and taxes were inevitably expressed in monetary terms. Not all environmental goods could be measured in economic values, for example what was the price of a species of animal or being able to breath fresh air? Therefore, charges and taxes were not the answer for cases which could not be measured in terms of value, but only for those which could be calculated in monetary terms. The diversity of charges and taxes varied in degree which further complicated the use of this kind of instrument as a solution to ecological problems: there were thousands of different products and each of them had its own "ecological cost" (some polluted more than others); the ecological cost of the same product varied according to the technology used to produce it (outdated technology tended to pollute more than modern technology); and the ecological cost of products produced using the same technology varied according to the ecosystem in question (different ecosystems varied in terms of their capacity to absorb environmental externalities: for example, acid soil would absorb fertilizer faster than a less acid soil).

19. Against this backdrop, charges and taxes on imports would have to be established on the basis of one of the following alternatives: a single level of tax (the average, for example) to be levied on all like products or according to the sector of production, or different levels of tax according to the real ecological cost of the imported product. The first alternative (namely a flat rate for all like products regardless of their real ecological cost) would benefit ecologically less efficient producers as their costs would necessarily exceed the average, or if the rate were very high they would pay less than others in real terms. Instead of benefiting the environment, the most efficient producers would be penalized. The second alternative (a variable rate reflecting the real ecological cost product by product) would not only be impossible for customs to administer, but would also involve *in situ* inspections which would create further problems in that the cost would vary from enterprise to enterprise as well as over time as enterprises were modernized.

20. Regarding effectiveness, charges and taxes on imports to deal with problems related to production externalities (namely when ecological effects arose in the place of production) were

limited in at least several ways: the ecological effect remained in the exporting country (e.g. a mine pit), the charge or tax on imports would mean that the resources for dealing with the environmental impact (filling in the pit) would be transferred to the importing country which levied the tax and would therefore be divorced from the ecological solution in the exporting country, and a double payment would be exacted since the exporting country, in addition to paying the tax, would have to deal with the ecological damage to its territory.

21. If the ecological effect was cross-border (e.g. acid rain) or global (e.g. ozone layer) there would be no or less double payment. At any rate a transfer of resources that had nothing to do with the ecological solution would occur. Furthermore, because total production tended to be greater than exportation, it would be less costly for the producer to do nothing to solve the root cause of the ecological problem because the import taxes were only paid on exports. As a result, producers who did not export would not pay taxes regardless of whether they polluted or not. This tax would affect trade across the board but would be environmentally helpful only insofar as goods were actually exported. In fact, it was highly likely that a situation would arise whereby an ecologically efficient producer would pay more than one who was ecologically inefficient simply because the former would be export-oriented.

22. As not all countries suffered cross-border or global ecological effects to the same degree, presumably not all countries would apply ecological taxes. As a result, the environmental taxes could be expected to lead to trade being diverted towards countries which did not levy such taxes, thus also increasing pollution because of the additional transportation stemming from this trade diversion. Also, countries with large domestic markets which exported only a small part of their production would pay relatively little, regardless of whether they were large polluters or not.

23. Regarding competitiveness, a large part of the arguments for applying trade instruments in the form of import charges and taxes was based on the assumption that ecologically inefficient or irresponsible countries enjoyed unfair advantages with regard to other countries, a kind of "ecological dumping". They should internalize production or consumption externalities in order to re-establish conditions of fair competition through import charges and taxes. However, it was incorrect to attribute the level of competitiveness to ecological externalities. First according to studies carried out, ecological costs were not a significant part of total production costs, and second competitiveness was in itself a concept made up of many elements whose importance varied according to the circumstances of each case. In some cases, the most important aspect was financing, in others technology, economies of scale, geographical location, training, infrastructure, or strategic alliances. As a result, it would be wise to look at competitiveness as a whole and not just some of its aspects. Otherwise, the only countries to benefit from the discussion would be those whose competitive advantages remained outside the debate.

24. He concluded that import charges and taxes for the purposes of environmental protection were neither useful nor efficient for problems related to production externalities (moreover, in some cases they might be counter-productive). A similar exercise would need to be undertaken for problems related to consumption externalities. On this last point, the GATT and the future WTO provided for the application of any form of internal charge or tax, regardless of its purpose, as long as there was no discrimination under Articles I and III.

25. The representative of Brazil noted that this item of the work programme involved a number of different instruments used for environmental objectives. Each had its characteristics and specific effects and, therefore, the relationship with the multilateral trading system was different in each case. He recalled that in the Working Group on Environmental Measures and International Trade, it was considered necessary to separate the discussions on packaging from those on labelling. Therefore he suggested treating each topic of this item separately in the future work.

26. He considered that taxes were a central part of the effort to introduce market instruments to deal with environmental problems through the internalization of environmental costs. They were an attempt to translate into prices at least part of the environmental cost (ideally the whole cost) which society bore from the existence of a certain product. In this effort there were a number of valuation problems involved. There was the difficulty of determining the level of tax to be charged. This level had, at the same time, to be feasible (not so high as to eliminate consumption unless that was the objective) and to produce the desired effects. There was also the difficulty of evaluating the environmental cost that had to be internalized: was the cost of redressing a negative environmental effect (cleaning up costs) a good expression of the environmental cost to society? Before this, there was also the valorative problem of determining what constituted, for a specific society, an environmental problem.

27. When using taxes as an instrument for cost internalization, the environmental effect at which the tax was aimed could be related to the production, consumption or disposal of a product. A tax could act as an incentive to a specific action, for example diminish the emission of the taxed pollutant. It could also act indirectly, for example by taxing the consumption of a good that, when produced, resulted in emissions of a pollutant because it was determined that it was not possible to reduce the emissions but was better to reduce consumption of the final good. There was therefore also a distinction to be made between the stage where taxation occurred and the stage where the environmental effect which was addressed occurred.

28. This distinction was important as a basis for the examination of the relationship of this instrument with the multilateral trading system when the Sub-Committee would analyze the instrument's effects on trade vis-à-vis its environmental objectives. If the objective was to address an environmental problem at the production stage without transboundary consequences, there would seem to be no reason for taxing imports, even on the product, since the reduction of imports would not help to solve the problem. On the contrary, when the idea was to diminish problems at the production stage through reducing consumption, more imports instead of production at home would help to attain the objective. It would also not seem reasonable to exempt exports from the tax since more exports would represent more of the production-stage environmental problem at home.

29. When the environmental effects to be addressed occurred at the consumption/disposal stages it would, on the contrary, make sense to tax imports and exempt exports. But in this case great attention would have to be paid to avoid capture by protectionist interests. In particular, when a country produced a product similar to a taxed product that it did not produce, there might be a temptation to force BTA on environmental grounds on the non-produced product in respect of the national treatment rule. An interesting case that did not fit directly into this analysis was a proposed tax related to the recycled content of paper products. Although the environmental problem addressed was the disposal of the product (the excess of paper waste) and the tax was charged on the product, the measure tried to solve the disposal problem through production behaviour (recycling paper). The same basic reasoning as had been highlighted in past GATT discussions on the issue of recycled content requirements applied, namely that imports should not be subject to the measure since the behaviour of the producer of the product did not help to solve the disposal problem in the importing country.

30. In any case, it was not acceptable that countries try to arbitrate, through the taxation exercise, how and how much other countries should internalize their environmental costs, thus replacing other countries' exclusive rights to evaluate those costs. He did not intend to develop in detail his delegation's view of the relationship between the GATT rules and the application of taxes for environmental purposes but he mentioned some of the issues his delegation considered would merit the attention of the Sub-Committee. Besides the more general question of what taxes

were adjustable at the border in the light of Article III, his delegation would pose the question of tax differentiation of imports on the basis of production behaviour versus national treatment and MFN treatment for like products and, finally, formal national treatment versus effective national treatment. He added that developing countries had little experience with environmental taxes and would greatly benefit from presentations on the operation of those instruments by the countries that used them more extensively. His delegation would therefore welcome this inclusion in the submissions of information that delegations were providing on other aspects of their environmental policies.

31. The representative of Korea considered that the discussion concerning environmental taxes and charges was mostly about addressing domestic environmental concerns. These taxes and charges were levied in response to domestic environmental pressure resulting from the consumption or production of products. With this in mind, the level of taxes and charges would vary from country to country according to different environmental circumstances, recognizing that there were legitimate reasons for diversity in environmental regulations across countries.

32. He added that taxes and charges levied on production processes should not be applied to overseas suppliers as a surrogate process tax. This was reflected in paragraph 18 of document TRE/W/13. Further, countries with environmental tax systems should implement them so as to maximize their environmental potential while minimizing their trade effects. He considered that in view of the potential complexity and ambiguity, it would be useful to analyze the potential effects on trade caused by environmental taxes and charges on a case-by-case basis. Transparency would be enhanced by strengthening the notification and publication procedures to cover cases not found in the TBT Agreement and other GATT regulations.

33. He considered that the existing GATT rules relating to BTA had been developed with the goal of ensuring trade neutrality and avoiding protectionism. This must be borne in mind in the study of BTA, which must respect the MFN and national treatment principles. Concerning the non-discrimination principle within the context of BTA, some problems could occur if the country of origin adopted regulatory instruments while the importing country maintained fiscal measures, including environmental taxes. If environmental goals had been met and the manufacturer already bore additional costs due to compliance with the applicable regulatory requirements of the domestic country, the product could not be subject to BTA. Otherwise, double taxation would occur.

34. As recognized in paragraph 21 of TRE/W/20, in determining whether two products were alike, it was necessary to determine whether a differentiation was being made "so as to afford protection to domestic production". Nevertheless, the Sub-Committee should be aware of the possibility that an importing country could still make use of the differentiation based on minor differences in product characteristics or in production processes. According to Annex II of the Agreement on Subsidies and Countervailing Measures, specific environmental taxes on inputs were eligible for export rebates if the input was physically incorporated in the final product, and possible if the input consisted of energy, fuel and/or oil inputs consumed in the production of exported products. With regard to this footnote, he noted that practical problems might be encountered in identifying the correct tax rebate for exported products. He concluded that environmental taxes should be operated in conformity with GATT Articles II, III, and XVI, as well as Articles I, VI and VII.

35. The representative of Nigeria said his delegation wished to contribute to an exhaustive and rigorous discussion of the items of the work programme. In so doing, it wanted to look at the issues from all possible perspectives and identify the difficulties and problems because it was only after comprehensive and rigorous analysis that the Sub-Committee would be better placed to determine how next to proceed, without rushing into a consideration of the options. Also, his

delegation considered this a cooperative multilateral effort and that the area of trade and environment was too important to be subject to polarization. Although his delegation recognized that trade and environment policies were mutually supportive, it took an essentially trade view.

36. The area of taxes and charges was one of the vital connections between trade and environmental policy and would be subject to much discussion from various perspectives, such as economics and trade, law and politics. Proposals for taxes and charges for environmental purposes were based on essentially two objectives: to produce an expected type of trade behaviour in a target State or generate funding for some designated projects or activities. These were transparent and explicit objectives. A third possible unexplicit objective was the search for competitive advantage. He addressed only the first two objectives, not because the third did not exist but because he chose to read the best intentions into proposals for taxes and charges to achieve environmental objectives.

37. He asked if there was a one to one correspondence between taxes and charges and environmental goals? What impact would an environmental tax or charge have on a target country, on their production capacities or supply patterns, on the risk-taking orientations of producers in the exporting countries, on bilateral trade balances, and on overall world trade? The answer was that the effects would be uncertain based on a number of factors. First, a tax was not constant, it was a variable. Second, producers or exporters reacted differently to the application of a tax because of different income and substitution effects. And, third, a number of other variables intervened between a tax and charge policy and its stated objectives.

38. On the first factor, a proposed tax or charge could be calibrated as progressive, proportional or regressive. If the tax for environmental purposes was progressive it would mean that the applying country imposed or applied it to the increased export earnings of the target country. If the tax or charge was proportional it would mean that the applying country imposed or applied the tax as a predetermined constant fraction of the target country's export earnings. If the tax or charge was regressive it would mean that the applying or imposing country imposed the tax probably against a developing country or against a country on which some sort of moral judgement had been made about its social conditions, labour conditions, even possibly political conditions. A fourth possibility was that the tax or charge proposed could combine in determined ratios either more or less of the progressive, proportional or regressive elements.

39. The first problem he wished to emphasize was the problem that would arise in proposals to establish optimal tax rates to whatever was the desired environmental objective. His delegation considered that the optimality of tax and charge rates would at best be subjective. This subjectivity, which in itself would be a serious problem, would also be compounded by the uncertain effects of the taxes and charges on trade itself. There was contradictory evidence on the national and international effects of taxes because of income and substitution effects. It was sufficient to note governments that swung back and forth on fiscal policy arguing on the one hand that minimal or zero taxes were the best possible incentives for increased production and growth and, on the other, that increased taxes were needed to mobilize resources for programmes. However, would taxes and charges for environmental purposes work? Before suggesting an answer, he considered some possible effects.

40. If a tax or charge were imposed, one possible effect would be that the supply of the exported product might be reduced. If the export was taxed at the border and entered the market, it was priced out of reach. If the country unilaterally imposing the charge judged that the taxed product was being produced in environmentally unsound ways, then the tax would have had positive and desired effects; the exporting country would halt exports since the products would no longer be competitive. But the situation would not be that simple. Production for export might

not stop; trade diversion could occur; other markets could benefit and the opposite effect would occur. In imposing such a tax or charge with the objective of changing the production patterns or particular export of a target country it would have to be assumed that the product in question was price elastic. Suppose that the product were price inelastic (either insensitive or minimally so to price changes), of good quality, even if it was being produced in ways that had been judged as environmentally unsound by the applying country. In this case, that country would suffer because consumers would keep buying, but at higher prices. This situation was not so hypothetical; a quick survey of the balance of payments of many countries showed they had developed strong tastes for foreign goods. Also, although consumers would keep buying, the effect of the tax measure would reduce the volume of the traded product and would increase the world price of the product. In this case, there would be significant trade-distorting effects and an unintended outcome.

41. To sum up, if the product were price inelastic, competitive, of good quality, and possibly strategic, within the tax-applying country consumers would pay more, the current account would experience greater outflow of hard currency, overall bilateral trade would be reduced and distorted, and the tax imposing country would suffer. For the target country, if its exports were price inelastic, competitive, and it could achieve economies of scale and expand production, it could actually gain, even though its products had been judged as destructive to the environment. Thus there was a situation where a tax meant to achieve an objective had had an unintended effect by actually boosting the exports of the target country, which it was assumed were being produced in unsound ways.

42. Another scenario could be considered where the tax imposed actually had the desired effect. In this case, the tax or charge was imposed against, for instance a developing economy which depended on trade and export earnings for growth and economic development. If the tax had the desired effect, the export of products would drop off. But, if there was large scale dependence on this export, when the earnings were reduced or ceased it might be incapable of adjusting. Decreased export trade and reduced earnings resulted in deficits, economic crises and deepened poverty. The probable consequence was that there would be greater destruction of the environment, since the target country would now turn inwards to survive. In another scenario, where the tax or charge worked, unintended consequences, different from the objective, resulted. But again, only the surface of probable effects and uncertain outcomes had been considered. If the tax were unilaterally imposed by a major trader against another major trader, retaliation would follow, trade would be distorted, and the world economy would suffer losses in growth rates.

43. He added that there were also benefits to be had. If the problems he had cited never occurred and there was perfect symmetry between taxes and charges and environmental objectives, how then would the proceeds of the taxes and charges be distributed? Would they be used in the applying country or would they be sent back to the target country so that the proceeds from the taxes and charges could be used to improve their PPMs or other environmental considerations. These were also issues of great complexity and sensitivity to be discussed, and legal aspects to consider. However, his delegation stressed that the unilateral imposition of a discriminatory border tax or charge was dubious, highly questionable, and would be inconsistent with GATT rules. Other consequences emerged at the level of psychology and foreign policy, although this was not in GATT's competence.

44. He did not conclude from his analysis that taxes or charges should not to be contemplated or proposed to protect the environment. But these measures would have to be further studied from the perspective of trade. There was a strong need for more studies on the problems and ramifications that arose from the trade effects of environmental measures. He proposed that the Sub-Committee should commit itself to cooperate rather than seek short-term gains through unilateral actions; should foster transparency; that there was a need for economic assurances and

incentives against protectionism and for greater market access (this could be done by simulating models to determine whether an environmental measure with trade effects would distort trade rather than enhance it and was an area where contracting parties could work together with the Secretariat to produce reliable models for calculating the trade effects of existing or contemplated environmental measures); and should establish tests that proposed measures would have to satisfy. On the latter point, his delegation considered that such tests should include the elements of feasibility of the proposed measure and its necessity. It should incorporate existing GATT rules and be consistent with strengthening existing GATT discipline, and also include the obligation for such measures to be cooperative and multilateral.

45. In conclusion, he considered that unilateral measures for the enforcement of environmental standards which were domestically formulated would distort trade and, in both the medium and long term, would have harmful consequences for trade and the environment. In policy terms, his delegation could not agree to the application of domestic environmental programmes and standards to foreign imports; it would not only be ineffective and unfeasible, preliminary consideration of the evidence and logic suggested, it would be harmful both to trade and to the environment.

46. The representative of Malaysia, speaking on behalf of the ASEAN countries, believed that in this phase of substantive discussions on the work programme, all issues must be carefully considered so as not to arrive at hasty decisions. Because some of the issues were new, there was a need for in-depth analysis and, if necessary, further background material from the Secretariat. The time frame was sufficient, and there was no rush to conclude any item. His delegation's main preoccupation in the work was how to ensure that unimpeded market access and trade would continue to flourish despite measures taken for environmental protection; there must be compatible partnerships between trade liberalization and sustainable development.

47. He noted the general view that economic instruments, such as charges and taxes, were more effective in achieving the objective of preventing environmental degradation compared to other policy measures. However, economic instruments such as environmental taxes, whether imposed on the products or processes, had the potential to change the competitiveness of the product. This was why governments resorted to border taxes on imported goods so as to create a level playing field. He referred to the conclusion presented in document TRE/W/20 that BTA was allowed for "indirect taxes", taxes on products but, not for "direct taxes", taxes on processes. Since BTA could have an impact on competitiveness and international trade, certain conditions had been imposed on its use. Some conditions which ASEAN fully endorsed were that the application of charges and taxes on imports should not have protectionist effect and should respect fully the relevant GATT provisions and disciplines; and BTA should be imposed only on products and not on production or process conditions.

48. He added that in the current situation of environmental consciousness, BTA could become an instrument for governments to advance their environmental agenda. Notwithstanding this, BTA of environmental taxes could also be used as a convenient cover for protectionism. It was also unclear if BTA of environmental taxes could actually achieve environmental objectives. Furthermore, BTA rather than create a level playing field could actually grant an advantage to domestic producers. With this background and concerns, he raised some questions for collective reflection:

- Had BTA measures been really effective for attaining domestic environmental objectives? To what extent had such measures affected market access especially for those countries which had inherent comparative advantage, e.g. endowed with natural resources, and which were producing without causing any adverse effect on the environment?

- Did BTA allow the Polluter Pays Principle to be effectively practised?

- How could it be ensured that BTA was not used for protectionist or discriminatory purposes?

49. Environmental charges and taxes should be applied domestically in line with domestic environmental policy objectives and standards. Any charges or taxes would then be factored into the domestic cost of production of the goods which may be the most appropriate and effective way of incorporating environmental costs. Environmental charges and taxes on imported goods could be imposed only if their importation had adverse environmental impacts in the importing country. His delegation hoped to further develop these initial thoughts in the future.

50. The representative of Switzerland recognized the important role that taxes and charges could play for specific environmental purposes, as well as the complexity of the subject. She considered that a logical approach would be to subdivide measures into product-related measures and process-related measures. Such an approach was important to identify the points pertinent for an examination of the GATT-compatibility of taxes and charges. The next step could analyze the relationship between the different provisions of GATT and the specific characteristics of taxation systems, with their specific trade implications. For the time being however, her delegation would deal with the two categories of product-related taxes and process-related taxes. Even product-related measures were not so simple to examine. Concerning process-related taxes, her delegation would analyze them from three aspects: domestic production, BTA due to different environmental regulations, and product-related production measures altering the characteristics of a product.

51. Regarding domestic production measures, she used as an example regulations on national emission standards for the protection of water and air. By imposing taxes and charges on harmful process-emissions or on environmentally unfriendly production-inputs, the authorities aimed primarily at initiating a change in the pattern of behaviour. Such internal regulations were not directly related to trade and were, in principle, compatible with the GATT-provisions. The application of such measures was a contracting party's sovereign right.

52. However, when international trade was concerned, GATT-compatibility had to be analyzed when the taxation-system contained a specific remission and refund system. Document TRE/W/20 explained that the exemption of an exported product from duties or taxes borne by the like-product when destined for domestic consumption, or the remission of such duties or taxes in amounts not in excess of those which had accrued, shall not be deemed to be a subsidy. Indirect tax rebate schemes for products which were physically incorporated in the exported product could allow for exemption, remission or deferral of prior stage cumulative indirect taxes levied on inputs that were consumed in the production of the exported product. However, they could constitute an export subsidy to the extent that they resulted in exemption, remission or deferral of prior stage cumulative indirect taxes in excess of the amount of such taxes actually levied on inputs that were consumed in the production of the exported product.

53. On the second aspect, the BTA due to different production methods, there was a tendency for countries to demand from imported products the same domestic environmental production standards. While product-measures and domestic production-measures were applied for the protection of the (national) environment, the underlying motivation of applying production- and process-measures for imported products could be different. Countries might aim at the protection of specific environmental goods and try to influence the environmental policy of another country. A country might, furthermore, intend to protect its domestic industry against relatively cheap imports produced under lower environmental standards. This latter approach could consequently mean that a product could only pass the border without being taxed if it met similar process-method standards. However, such practices of equalizing national cost-disadvantages, and in

general, competitive disadvantages, by imposing taxes and charges on imported products were not compatible with current GATT law.

54. It was the sovereign right of a country to determine its own level of environmental protection. It seemed also established that countries could not apply taxes or tariffs at the border which discriminated against processing methods having different impacts on the environment. However, the notion of "like products" was not easy to define and further reflection might be needed. GATT dispute settlement panels dealing with the question of like-products had assessed this term on a case-by-case approach. As document TRE/W/20 stated, different criteria such as the end-users of a product in a given market, consumer taste and habits, the product properties, nature and quality were used to determine "likeness". All these criteria described the product itself or its use, not its production. This meant that the determination of a product by its process-methods was problematic under current GATT law and the relation between GATT provisions and such measures would have to be analyzed in detail.

55. The third aspect concerned a product-related process measure situated between the product and process-related measure. Such measures, often in the form of taxes, were aimed at specific production methods that changed the characteristics of a product. They were applied especially for sanitary and phytosanitary reasons. Obviously it might be difficult in certain circumstances to prove technically that an imported product contained a certain amount of specific health and environment damaging substances as a consequence of specific process methods. This meant that measures on imported products, such as border taxes, would be, according to the SPS and TBT Agreements, GATT-compatible only if the process-methods changed the characteristics of the product. The SPS and TBT Agreements stated that members may adopt or enforce measures necessary to protect human, animal or plant life or health, subject to the requirement that these measures were not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between members. As such taxes aimed directly at the product's characteristics, which were based on environmentally unfriendly process-methods, it could be argued that they were product-measures, not production-measures.

56. This brief illustration of the two categories, the product-related and process-related taxes, showed that there was scope for further action by the Sub-Committee concerning the relationship between GATT provisions and border taxes based on production and process methods. Her delegation believed that there was a growing need for clarifying and analyzing aspects of the expansion of product- and process-measures, in the form of border taxes, to imported products. Furthermore, the different taxation-systems for imported products often had an extraterritorial effect and might influence the environmental policy of another country. In this context, her delegation considered that international environmental problems, in contrast to domestic issues, called for solutions based principally on international cooperation, for example, in the form of the elaboration of international agreements.

57. The representative of New Zealand noted that document TRE/W/20 focused on the types of adjustments which may or may not be permitted under GATT rules; a question which was less than straightforward. At the outset of the discussion, however, it might be useful to consider how the extension to the trading system through BTA would alter the effectiveness of the domestic environmental measure; i.e. the internal tax or charge. This might provide useful background information for the Sub-Committee in its subsequent examination of the implications of GATT provisions. He emphasised that this analysis was not considering the necessity or effectiveness of the environmental measure *per se*: the environmental policy decision to impose the internal tax or charge was taken as given; the question was the effect of adding the tr[illegible]n.

58. At least two types of taxes or charges might be envisaged: (a) low level taxes or charges designed not to change the primary activity but to raise revenue for subsequent spending for environmental purposes, and (b) taxes or charges set at levels specifically designed to influence production and consumption decisions through changes in relative prices. He focused on the second type. In general, imposition of the second type of measure might be considered in situations where it was assessed that market prices failed to accurately reflect social costs of particular activities - the externality internalisation argument. In a generic framework, they related to the levels of production and consumption of the social "bad" and thus were not particular to environmental externalities that were under consideration in the Sub-Committee. As had been previously noted in this Sub-Committee and elsewhere, environmental externalities could arise in either production or consumption and be either local or global/transboundary in effect. He presented an analysis which considered the effect of adding a trade dimension to a domestically levied tax or charge in each of these situations.

59. In the case of a local production externality, the market outcome resulted in greater local production than was socially optimal. The internalising solution of imposing a tax or charge on the locally produced product resulted in a higher supply price and thus reduced local output at any given market price. The reduction in the environmental externality was achieved through this reduction in local output. In the case of alternative methods of production the externality resulted from excessive levels of the product produced with the "dirty" technology. The domestic tax or charge would therefore aim to distinguish between the alternative production methods to achieve a reduction in local output produced using the "dirty" method.

60. He then considered the trade dimension. In the case of an importable, imposing the tax on imports of the like product would increase the price of imports thus reducing (or possibly eliminating) the relative price effect of the tax between locally produced products and imports, rasing the domestic market price and lessening the output reducing effect of the tax on domestic production. In the case of an exportable, allowing for a tax exemption on exports would remove the relative price effect of the tax on that proportion of output which was exported, again lessening the output reducing effect of the tax on domestic production. For a local production externality, therefore, the purpose of the tax or charge was to reduce domestic production. Either imposing the tax on imports or exempting exports would lessen this output reducing effect of the tax, thus reducing (and in some cases possibly eliminating) the effectiveness of the measure in removing the environmental externality. Therefore taxes and charges aimed at production externalities might be most effective when there was no adjustment at the border.

61. Regarding the second case of a local consumption externality, the market outcome resulted in greater local consumption than was socially optimal. The internalising solution of imposing a tax or charge on the locally consumed product resulted in a higher price for the product and thus reduced local consumption. The reduction in the environmental externality was achieved through this reduction in local consumption. He then added the trade dimension. In the case of an importable, not to impose the tax or charge on imported like products would remove the price effect of the tax on that component of consumption which was imported, thus lessening the effect of the tax in reducing domestic consumption of the product. In the case of an exportable, there would seem to be no logical reason to impose the tax on products not being consumed in the domestic market. Moreover to do so would reduce the returns received by domestic producers from export markets with a resulting reduction in the price at which they were prepared to supply the domestic market, again lessening the effect of the tax in reducing domestic consumption.

62. For a local consumption externality therefore the purpose of the tax or charge was to reduce domestic consumption. Either imposing the tax on exports or exempting imports would lessen this consumption reducing effect of the tax thus reducing (and in some cases possibly eliminating) the effectiveness of the measure in removing the environmental externality. With

consumption externalities, therefore, adjustment at the border would contribute to the effectiveness of the domestic tax or charge.

63. He observed that this analysis had considered externalities arising from consumption of a final product. Some products giving rise to consumption externalities, however, might be consumed as inputs in a production process. Where externalities arose from consumption of an input, demand for the input was derived from demand for the final product. If the input was taxed to reduce externalities, adjusting taxes at the border to account for the imputed value of the input tax contained in the price of the final product would work against the objective of reducing demand for the input. Border adjustment would therefore be appropriate for imports and exports of the input, but not for imports and exports of the final product.

64. In the third case of a global/transboundary production externality, the externality was not dependent on the location of production within the set of countries (all countries in the case of a global externality) affected by the externality. In cases of taxes or charges imposed at the domestic level under such circumstances the conclusion in case one continued to hold, i.e. exempting exports from the tax or charge would lessen the effectiveness of the policy. Considerations on the import side were more complex, however. For example, if the production tax was also levied on imports, this might lessen the effectiveness of the tax in reducing the externality generated by domestic positive effects on the contribution of imported goods to the externality. Logically all sources of production (or at least the large majority of them) would need to be subject to measures aimed at internalisation of the externality. The assumptions of this analysis, however, would need to be developed in greater detail.

65. In the case of a global/transboundary consumption externality, the externality was not dependent on the location of consumption within the set of countries (all countries in the case of a global externality) affected by the externality. Again, as with the third case, effective internalisation of the externality would require all (or the large majority of) sources of consumption to be subject to internalisation measures. In cases of taxes or charges imposed at the domestic level under such circumstances, the conclusion in the second case continued to hold, i.e., imposition of the tax or charge on imports would contribute to the effectiveness of the domestic measure. Considerations on the export side were again more complex. In the third and fourth cases, consideration of these complexities involved further analysis of the context in which the domestic measure was being imposed. The prior assumption stated at the outset about the effectiveness of the original domestic measure did not automatically follow independent of such analysis. That analysis, however, was not confined to taxes and charges and would therefore be more usefully the subject of further consideration under item one of the Sub-Committee's work programme.

66. He concluded by noting that his analysis was only a beginning to the work on taxes and charges. Further analysis might usefully be done to consider elements such as: the effect of changing price elasticities and impacts of varying degrees of factor mobility; the effects of differing proportions of domestic production/consumption in relation to traded products; and differences between large country/small country effects. It would also be useful for the Sub-Committee to engage in some generic case study analysis, perhaps on the basis of the material being submitted to the Secretariat on country experiences with these various measures.

67. The representative of Sweden, speaking on behalf of the Nordic countries, noted that in considering charges and taxes for environmental purposes, internalization of environmental costs was a crucial issue in terms of sustainable development. Economic instruments, i.e. charges and taxes, were one way to internalize environmental costs. They were considered to be effective policy tools for taking account of environmental concerns. Uses of charges and taxes had so far

not created serious distortions of trade because they had been set at a rather modest level often due to competitive reasons. This might change in the future and an increased use of charges and taxes might potentially have considerable trade effects.

68. BTA was generally allowed for indirect taxes or charges on products but not for environmental charges and taxes that had been levied on the production process. Since countries should be free to use a mixture of measures, the present system of BTA might unduly influence the formulation of environmental policies. Did present trade rules therefore lead to bias in taxation and did this have implications for the attainment of environmental goals. In order to integrate environmental concerns in the multilateral trading system as well as to avoid distortions and disguised protection, the Sub-Committee should take a closer look at the extent to which the present system for BTA accommodated environmental needs for the use of economic instruments. Her delegation proposed that the Secretariat make a survey of existing environmental charges and taxes. An indication should then be made as to whether they qualify for BTA or not. Such a list in itself would be very useful for environmental decision-makers when applying economic instruments. To this list, could be added a description of what characteristics individual economic instruments must fulfil in order to be eligible for adjustment. In the further process, the Sub-Committee should look at economic instruments that were not considered eligible for adjustment under present rules and see if and what changes to the GATT provisions were called for.

69. In this context, and probably in other parts of the work programme, the issue of like product, would have to be addressed. Finally, her delegation considered that environmental subsidies should be also addressed when the Sub-Committee addressed economic instruments. Subsidies were often used to achieve environmental goals and this had been recognized in the new Agreement on Subsidies and Countervailing Duties as well as in the Agreement on Agriculture. A review of the relevant parts of these agreements could be important for the Sub-Committee.

70. The representative of Hong Kong said the subject of charges and taxes was highly complex. He supported the idea of voluntary notifications of measures and analysis of case studies at a later stage. He did not consider that the Sub-Committee's work should be academic but should be related to solutions and problems at hand. He observed that document TRE/W/20 showed that GATT rules in this area were few and related mainly to Articles II, III and I in the background. On the other hand, GATT jurisprudence on the issue was very rich and would become richer. It was useful to elaborate what was behind this jurisprudence for the benefit of both environmental policy makers and trade practitioners. The paper pointed to the fact that GATT rules provided a good degree of freedom for BTA measures. First, the policy purposes of such measures were not challenged in the GATT. Also, the paper made explicit that there was no prescription of methods or systems to be exactly applied and it was always optional for a country to levy a lower charge on imports.

71. Also important, the paper brought out certain useful principles for reflection such as the principle of equivalence and the principle that BTA could only apply to the product and not the input or the process as such. The body of the paper referred repeatedly and emphatically based on previous panel decisions to this concept of effective national treatment. Page 7 of the report referred to the Panel on Section 337's conclusion regarding the effective opportunity to compete. He added that page 11 referred to the Panel on Japan - Alcoholic beverages which made clear that, although a country could apply different measures, there must be no discrimination against imported products. Another important aspect coming out of this analysis was that the entire scheme could only work if the concept of like product was clear. Paragraph 17 on page 8 and paragraph 19 on page 9 of the paper clarified that there were no PPM considerations in the concept of like product at the present moment. The system could not be operated if this basic principle was changed.

72. He added that the paper offered a rich area for research and debate, but for the work to be useful the Sub-Committee needed a focus. From the environmental angle, the focus should be to see how GATT jurisprudence provided good enough guidance to avoid conflict between domestic environmental policy with international trade rules. From the trade angle, the focus should be whether existing rules and case law were sufficient to prevent trade distortions or protectionist measures in disguise.

73. Regarding internationalization of costs, he considered that a distinction should be made between efforts to internalize costs at the national level based on the product and efforts that were based on PPMs that impacted directly on international trade. His delegation did not have any problem with the Polluter Pays Principle and supported the use of economic instruments. But unless care was taken, the discussion could lead into an unmanageable situation before the analytical work was completed in a calm and non-confrontational manner. His point was recognized in Principle 16 in the Rio Declaration which stressed that internalization of environmental costs should be through efforts at the national level and always with a balance between public interest and maintaining no distortions to international trade and investment.

74. The representative of Austria noted that taxation for environmental purposes was becoming an ever more important issue. The imposition of such taxes could considerably modify the cost structure of production and trade and even modest changes in taxation might have effects on competitiveness. It was therefore essential that the GATT and the future WTO continued to take into account work which had already been undertaken to analyze the possible effects of taxation schemes on international trade. In particular, his delegation wanted to concentrate on the issue of BTA and share with the Sub-Committee some thoughts.

75. Present rules clearly indicated that taxes and products were eligible for BTA as contained in the findings of previous GATT working groups. On the other hand, the situation was more complex with regard to taxes on inputs and auxiliary materials to the final product. An additional question arose if the potential environmental impact was included as a basis for taxation. The original examination of the Working Party on BTA was based on the following definition for BTA: "any fiscal measures which put into effect in whole or in part the destination principle, i.e. which enables exported products to be relieved of some or all of the tax charged in the exporting country in respect of similar domestic products sold to consumer on the home market and which enables imported products sold to consumers to be charged with some or all of the tax charged in the importing country with respect of similar domestic products". The Working Party further agreed that the main GATT provisions to be considered in connection with BTA were on the import side, Articles II and III, and on the export side, Article XVI. Articles I, VI, and VII were also identified as relevant in this context.

76. The Working Party also agreed that the main provisions of GATT represented a codification of practices which existed at the time these provisions were drafted, reexamined and completed. It concluded that there was convergence of views to the effect that taxes directly levied on products were eligible for tax adjustment. It concluded further that there was convergence of views to the effect that certain taxes not directly levied on products were not eligible for tax adjustment. On taxes which the OECD had defined as consumption taxes on capital equipment, auxiliary materials and services used in the transportation and production of other taxable goods and on certain other taxes for example, property taxes, stamp duties, registration duties which were not generally eligible for BTA, a divergence of views remained.

77. He added that the Uruguay Round Final Act created a further development that went beyond the above mentioned conclusions. Some provisions which might be relevant to the Sub-Committee's further analysis may be the following: according to Article III and Annex I(g) in the

Agreement on Subsidies and Countervailing Measures, the rebate of indirect taxes on exported products in excess of what was levied on domestically sold goods had to be considered as a prohibited subsidy. Furthermore, this agreement dealt with the so-called prior stage cumulative indirect taxes. These multi-stage taxes were imposed where there was no possibility for subsequent crediting of the tax if the good or services subject to the tax at one stage of production were used in the succeeding stage of production.

78. As an example, indirect taxes on energy, fuels, and oils would fall under this category. If such auxiliary materials were used and consumed in the production process to obtain the exported product, taxes might be rebated even if not for products sold on the domestic market. It was worth noting that for imported goods, a similar provision was not foreseen. In such cases, only Article II, paragraph 2(a) of GATT applied; it was the condition of physical incorporation if BTA was made. It might thus be legitimate to attempt an analysis in which concrete cases went beyond the product stage and included the taxation of inputs and auxiliary materials as a legitimate case of BTA. He added that further discussion should therefore concentrate on such potential concrete cases.

79. He considered that the real purpose of environmental taxes should be to promote the protection of the environment, primarily the environment of the country levying the tax against adverse impacts. These taxes might take the form of product or process taxes or fees for certain services or transactions. When deciding which type of tax should be used in order to achieve an environmental goal, one would have to consider at which level production or consumption (i.e. upstream or downstream) the environmental effects predominantly arose. In some cases, they may arise in both. A product tax often did not allow for differentiation of a product according to the environmental characteristics of the upstream cycle. If the environmental damage was caused upstream during production processing or through the use of inputs, a tax on these and not of the product may be the more efficient economic instrument as it addressed the problem at the source of the environmental degradation. A production tax may be better suited to take these taxes into account. However, in order to qualify for BTA, according to the present understanding of GATT rules, a tax levied at the production or processing stage would have to be turned into a product tax. Consequently, the aim should be to achieve international consensus concerning the translation of the environmental impact from the production and processing to the product level.

80. The main unresolved problem was thus the translation process, i.e. how it could be assured that an adequate tax rate was reflected in the final product and was thus correctly adjusted at the border either in the form of a levy or a rebate. One of the critical points may thus be how to address the issue of competitiveness in the context of cross BTA of environmental taxes directly levied on goods while respecting the principle of non-discrimination, prohibition of export subsidies, as well as the prohibition of misusing the system for protectionist purposes. His delegation was aware that in this context, the issue of like and directly competitive or substitutable products would have to be addressed. Furthermore, his delegation was aware of the fact that BTA systems related to taxes levied on production systems may be excessively burdensome to administer. The Sub-Committee should nevertheless be prepared to reflect on possible innovative aspects of the multilateral trading system in order to establish a partnership between international trade and the environment. His delegation would thus strive to combine aspects of international trade and competitiveness with taxation systems aiming at internalizing environmental costs to the extent feasible and practicable and thus reflecting the Polluter Pays Principle.

81. The Sub-Committee should further consider the question of possible translation mechanisms as outlined above. TRE/W/20 provided useful information on the subject. In light of this meeting's discussion, he requested that the Secretariat develop its reflection further and present a revised version of this paper.

82. The representative of India reacted to some of the principles which had been referred to by previous speakers. With regard to comments about Principle 16 of the Rio Declaration which incorporated the Polluter Pays Principle, his delegation was concerned that taking out one of the Principles from the 24 constituting the Rio Declaration, claiming there was already unqualified acceptance of internalizing environmental costs and, from there, moving to measures to achieve this Principle was faulty reasoning. Even the language in the Principle spoke of national authorities "endeavouring". This meant that it was up to national authorities in their own territorial jurisdiction to try to promote the internalization of environmental costs. Use of economic instruments was mentioned in Principle 16 so it was therefore relevant to the discussion of this meeting. The Polluter Pays Principle could be taken into account but at the same time there was a caveat with regard to public interest and without distortion of international trade and investment. Because this Principle was within a set of parameters, his delegation had difficulty with referring to it in the abstract in order to justify measures. There were other principles as well in the Rio Declaration which were relevant at least to the trade and environment debate, if not to the subject of this meeting. Principle 2, for example, spoke of the sovereign right to exploit a country's resources pursuant to its own environment and development policies with a responsibility to ensure that activities within the country's jurisdiction did not cause damage to the environment of other countries. This was the transborder, physical spillover factor to which he would revert at a later stage.

83. He considered that Principle 7 of the Rio Declaration, which spoke of "common but differentiated responsibilities", captured well the Mexican reference to the different responsibilities of different countries. All countries had a common responsibility towards sustainable development, but it would have to be differentiated. He added that Principle 12 was also noteworthy in this context. He concluded that it was important to refer to the Rio Declaration from time to time either for guidance or for justification, but in doing so he did not think it fair to take isolated Principles out of context.

84. He added that the fact that BTA applied only to products was important. Articles I and III were important in this context, particularly as Article III spoke of effective equality of opportunities. The question of which taxes qualified for BTA was an issue that deserved further consideration as well as the important issue of like product. Paragraph 9 of TRE/W/20 made the important point that because a country decided to call a tax an internal tax did not automatically make it one. He extended this logic to the environment: would it be enough for a country to call a tax an environmental tax for it to be so?

85. He noted that most of the statements at this meeting concentrated on TRE/W/20. This was justified, but he considered that it was important to recall the mandate of the Sub-Committee which was to come to some kind of recommendation as to whether a modification to the provisions of the multilateral trading system was required at the end. To do so, he considered that it would be important to examine these provisions and, for instance, charges and taxes in order to determine whether existing GATT law prevented contracting parties from achieving their environmental objectives. He noted that TRE/W/20 pointed out that the purpose of Article III was not to prevent contracting parties from using fiscal and regulatory powers, i.e. a tax, for purposes other than to afford protection to domestic production. Perhaps it should be explained what was meant by "other than to afford protection to domestic production". On the other hand, if, as some delegations had hinted, existing GATT law was inadequate and there was a need to contemplate a modification to the provisions of the multilateral trading system, then he suggested, as others had, to proceed with an inductive reasoning from the specific case to the general law.

86. It would be useful to consider some of the existing national tax schemes against certain criteria. His delegation agreed with New Zealand that "effectiveness" would be a good criteria in

this regard. His delegation would be interested to see how the New Zealand analysis would apply to a specific case and to see the implications that would arise from such a case study. Another criteria would be the "necessity" criteria and GATT jurisprudence existed in this area as spelled out in several panel reports. He stressed that he was not questioning the environmental objective or standard as this was not within the competence of GATT. But even in suggesting that existing GATT law was inadequate and that modification of the provisions should be contemplated, his delegation would have to question the means adopted, i.e. the measure taken to achieve the objective, through a rigorous application of the "necessity" criterion. If not, then the existing GATT provisions were adequate although some clarification of them may be needed. In the absence of this criterion, it would be very difficult to have a general law to govern charges and taxes for environmental purposes. This could be done on the basis of specific cases brought before the Sub-Committee voluntarily to which the criteria would be applied. The Sub-Committee could then evaluate in what direction such analyses were going and then it could reach the stage whereby it could decide if there should be a general law for the theory that emerged.

87. He added that during this rigorous examination, the Rio Declaration would have to be relied upon. Ultimately, this would provide guidance and justification as it was accepted at the highest level of government. He suggested that at the next meeting, the Sub-Committee could move to the next stage of its analysis between the provisions of the multilateral trading system and charges and taxes for environmental purposes by considering whether existing provisions were inadequate, with demonstrable evidence of this inadequacy, and then by an inductive reasoning by looking at specific cases from which a conclusion could emerge. It could be decided whether the general law was sufficient or, if there was a valid case for charges and taxes specifically for environmental purposes, something would have to be done in this regard.

88. The representative of Australia observed that the complexities of this item of the work programme related both to understanding the range of economic instruments and regulations used for environmental purposes and to understanding the provisions of the multilateral trade rules on the trade-related aspects of these instruments and regulations. The item raised important questions in relation to all aspects of the Sub-Committee's terms of reference. For example, examination of the issues involved in this item would be central in helping the Sub-Committee to identify the relationship between trade and environmental measures, and how this relationship stood in regard to the promotion of sustainable development.

89. One important aspect of the agenda item was the issue of BTA. Document TRE/W/20 provided a useful examination of the GATT rules in this complex area and a number of themes emerged from this examination. First, that the GATT rules on BTA seemed to be based on the idea that countries should be able to take a number of measures with the aim of ensuring that internal taxes on products should, as the 1970 Working Party report put it, have "a certain trade neutrality". This objective of promoting trade neutrality encompassed both the extension of internal taxes on domestic products to like imported products, and the remission or exemption from internal taxes of exported products. The GATT rules on BTA seemed aimed at allowing countries scope to minimise the trade impact of certain internal taxes in a manner that did not erode the fundamental GATT provisions. In other words, BTA should not provide a means for countries to escape, or undermine, the disciplines that the GATT placed on a range of government measures which affected the competitive relationship between products in international trade.

90. Consequently, the GATT had not been concerned with the policy purposes of an internal tax, but with ensuring that the application of internal taxes to imported and exported products was done in a manner that conformed with basic GATT principles. These included: first the principle that protection to domestic producers should be provided through tariffs and not through internal taxation and regulation, and therefore that imported products should be treated no less favourably than the like domestic product in matters of internal taxation and regulation; second the principle

that imported products from all contracting parties should be subject to most-favoured-nation treatment; and third, that BTA on exported products should not provide a means of escaping the disciplines on the use of export subsidies.

91. The distinction made between direct and indirect taxes in the rules on BTA appeared to reflect the fact that these rules must be seen in the context of the GATT's broad aim of providing greater certainty in expectations of the competitive relationship between products in international trade, through disciplines on government measures on imported and exported products. The rules on BTA were not intended to infringe on countries' domestic tax policies or on the objectives countries pursued through these tax policies. Instead, the intention appeared to be to ensure that taxes levied on products were not applied to imported and exported products in a way that could undermine other GATT disciplines on government measures applied to imported and exported products.

92. The destination principle, which the 1970 Working Party drew on, would also appear to suggest that the rules on BTA reflected GATT's focus on those government measures which directly affected competitive conditions between traded products. The destination principle seemed to be based on the idea of taxing a product in the market where it was competing for sales and where it would be consumed. The limitation of the eligibility for BTA to taxes directly levied on products appeared to be based on GATT's concern with government measures directly related to competition between internationally traded products and with GATT's aim of not interfering with countries' pursuit of domestic policy objectives. It was only concerned with domestic policies to the extent that their implementation involved direct trade aspects, including the application of internal taxes to imported and exported products.

93. He added that the use of the "like product" concept must also be seen against this focus on competitive conditions of traded products; the features to be considered in determining like product status were those relevant to competition in the market where the product would be consumed. Four issues could benefit from further analysis to help understand the rules on BTA and their relationship to taxes and charges used for environmental purposes. The first was the rationale for the GATT providing countries with the scope to take BTA, including the conclusion of the 1970 Working Party that the underlying philosophy was to allow countries scope to ensure a certain trade neutrality for tax measures applied to products. How did this objective relate to GATT's broad aims and to the fundamental GATT principles? To what extent did this objective relate to countries' use of tax measures applied to products for environmental purposes? The second issue was the rationale for the distinction between direct and indirect taxes, including in relation to the focus of the GATT on disciplining government measures that directly related to the competition conditions of imported and exported products and GATT's intention not to infringe on countries' domestic policies, including the use of tax policy for environmental objectives, but to discipline those parts of the implementation of domestic policies which may have a direct trade aspect. A third issue was the distinction between direct and indirect taxes. In examining this issue it may be useful to look at various types of environmental taxes in the light of this distinction. A fourth issue related to whether the rules on BTA were identical on the import and export side. In particular, were the range of taxes eligible for tax adjustment in relation to imported products the same as the taxes eligible for exported products?

94. The representative of the European Union added to the debate with questions and some suggestions on how work on this item could proceed in an effective manner. From a trade perspective, it would seem that two main "factual" aspects of environmental taxation were relevant for the Sub-Committee's discussion. These were the trade effects, i.e. effects on the competitiveness of products when exported and effects on domestic competitive conditions between domestic and imported products, and the environmental effects, effectiveness, and

rationale. A third aspect was the "legal" aspect, in particular the rules on subsidies and countervailing duties, and those on BTA. Clearly, this "legal" aspect played an important role in determining the possible scope of especially the trade effects of environmental taxes. Having looked at the rules on BTA in relation to environmental taxes, his delegation had a number of remarks and questions.

95. He observed that BTA rules were intended to cover all taxes, not only environmental ones. They seemed intended to apply in principle in a similar fashion to imports as well as to exports. Document TRE/W/20 noted the conclusion of the Working Party on Border Tax Adjustment that GATT provisions on tax adjustment, even though worded differently for imports as for exports, applied the principle of destination identically to both. The document also included reference to a limited category of so-called prior-stage cumulative indirect taxes on energy, fuels and oils used and consumed in the production process. He added that Articles II and III had been less elaborated. Regarding the issue of inputs into production processes, which could or could not be incorporated into the final product, Article II(a) gave a basic rule, allowing (provided Article III disciplines were observed) imposition upon importation of a charge equivalent to an internal tax in respect of a product from which the imported product had been manufactured or produced in whole or in part. He noted that in French, this read "percevoir ... à l'importation d'un produit, une imposition équivalant à une taxe intérieure frappant ... un produit national similaire ou une marchandise *qui a été incorporée* dans l'article importé").

96. It could be interesting to compare this provision in a more in-depth manner with the provisions on BTA relating to inputs in production processes on the export side, especially those of paragraphs (g) and (h) of the Illustrative List of Export Subsidies attached to the Agreement on Subsidies and Countervailing Measures. In this context, his delegation agreed with Sweden that although the Sub-Committee should focus on taxes and charges under this item, it should also look at the GATT rules on other economic instruments, such as subsidies. In that context, the specific provisions relating to environmental subsidies in the Uruguay Round, not only in the Subsidies Code, but also in the Agriculture Agreement, deserved to be noted.

97. Since the BTA rules were different for different types of taxes, such as direct or indirect, he asked to what degree could they induce WTO Members to use certain types of environmental taxation rather than others? Might WTO Members choose to use types of environmental taxes which may be less economically or environmentally efficient, simply because those types were eligible for BTA? If so, this probably went for all taxes, not only environmental ones and did not automatically mean that the distinction drawn in WTO BTA rules between different types of taxes should be re-evaluated. He considered that there may be other good reasons for this distinction. In particular, with regard to inputs not physically incorporated in a product, one reason for the present system seemed to be that it might be difficult to verify whether certain inputs had been used in the production of a product. Such consideration of what we would call an "administrative" or "practical" nature, needed to be kept in mind in any theoretical discussions the Sub-Committee may have on the application of the present BTA rules to environmental taxes.

98. He considered that the current rules could benefit from clarification or at least an intensive discussion in this Sub-Committee. In particular, it could start its work on environmental taxes and charges by clarifying the application of BTA rules to the different types of environment taxes. He asked whether the WTO should distinguish between taxes with an environmental aim and others? If so, would any clarification of the rules be required to allow such a distinction? Would such a distinction depend on the geographic scope of the environmental problem at hand? He added that BTA rules appeared intended to apply to all taxes and charges alike, without distinction as to their purpose. For example, in paragraphs 5.2.5 and 5.2.6 of the Superfund Panel Report the EC had argued that imposing the Superfund tax on imported products ran contrary to the Polluter Pays Principle, because the fund was designed to combat local US pollution. The Panel correctly

pointed out that, because BTA was optional, the imposition of lower or no tax on imported products because their consumption or use caused less or no environmental problems, was allowed; thus the Polluter Pays Principle could be applied.

99. He added, however, that according to the Panel, BTA could be imposed even if arguably that would not conform with the Polluter Pays Principle. He noted that the standard terms of reference of a Panel was to examine the case before it " in the light of the relevant GATT provisions". This would remain the same under the Uruguay Round Dispute Settlement Body. Since the WTO Agreement would usually be the cited Agreement, references to sustainable development and environmental protection in its Preamble could also be taken into account when interpreting Uruguay Round agreements. This led to the question of whether the environmental aim of a tax should be taken into account when assessing its conformity with the multilateral trading rules?

100. He considered that the basic principles would always have to be established first: national treatment and no protectionist intent or effect. If this had been established, would the environmental aim of a tax play a role in evaluating it from a GATT perspective? For instance, should BTA on imports not be imposed if the exporting country had regulated the environmental problem at which the tax was directed by using a technical regulation? If the aims of taxes were taken into account, questions might arise. For instance, should one distinguish between taxes which were aimed at combatting environmental problems, taxes which dealt with regional problems and taxes with purely local aims. Or should a distinction be made between taxes for general revenue purposes or charges which were more specific. His delegation considered that these were open questions which would be useful to address at some point in the Sub-Committee's work.

101. The representative of the United States noted that a lot of questions had been asked and some answers had been attempted but it was important to bear in mind that the questions would have to be explored carefully before making any general prescriptions. Through reflection, his delegation immediately realized that looking at taxes and BTA touched on an area that was very much in an experimental stage. While there was much academic discussion and analysis of the relative merits of economic instruments as opposed to command and control type regulations, practical experience was limited, especially with regard to the former. This was important to keep in mind in understanding his delegation's approach to the subject and to its comments. This was also important to keep in mind as the Sub-Committee looked at the central questions before it.

102. From a general economic point of view, much argumentation had been put forward suggesting that, all else being equal, economic instruments were preferable to command and control instruments. There were some questions to this assumption, even in terms of the application of that assumption to specific contexts. There was also a problem of everything else not always being equal, so there was a matter of other realities influencing the choices that countries made about which instruments were most appropriate to a particular circumstance. He considered that great caution was thus called for especially to the extent that some of the interventions may have foreshadowed a need for greater discipline on BTA in order to address trade concerns. To the extent that the practical consequences of interpreting the rules of the trading system worked against economic instruments, it would not make the issues that caused nations to explore economic instruments go away. If those economic instruments became more difficult to utilize or if the present rules already made it difficult to utilize them, then the alternatives, such as regulatory command and control type of measures, and the issues that those measures were trying to address would have to be explored.

103. A number of interventions addressed specific issues in need of further analysis. His delegation believed that a comprehensive and prescription-free approach should be the starting point for the Sub-Committee's work which should be an analysis of both the trade and environmental aspects of the issues. When looking at economic instruments and the question of BTA, it would be important to understand the types of instruments currently in use or being contemplated. It would be important also to understand the objectives of such instruments, particularly which environmental objectives they were addressing, what were the relevant underlying concepts, to what did these measures apply - products, processes, inputs - and how did these measures operate.

104. From the trade perspective, there were also some important questions to address such as the relevant rules and principles, relevant jurisprudence and panel decisions, and how they applied to specific measures the Sub-Committee would need to identify and describe. He added that a number of more specific aspects of what he had outlined had already been elaborated by previous speakers. His delegation was interested in the intervention by New Zealand and would examine the underlying principles in it more carefully. This intervention raised an important aspect of the Sub-Committee's work; in looking at whether changes to the multilateral trading system needed to be considered, economic issues would need to be considered such as effectiveness. Similarly, examination of these issues would invariably lead to the question of whether it was necessary to consider changes and his delegation preferred deferring conclusion on this point until the factual analysis was concluded.

105. His delegation noted that the rules of jurisprudence in the area of BTA were few. A number of delegations seemed to draw conclusions from TRE/W/20 that his delegation did not see. For example, his delegation did not read that the document suggested the sort of conclusion that some drew regarding the application of taxes to PPMs. He was not sure that the paper attempted to go into a real analysis of this issue. His delegation agreed that the Sub-Committee would have to look at this issue as well as that of like products before drawing conclusions about the current state of play and what ought to be in the future. The Sub-Committee should examine the rules of the multilateral trading system as they applied to the various types of instruments that had to be identified by the Sub-Committee with a view to determining whether the trade disciplines met trade objectives and whether they provided at the same time sufficient scope for addressing environmental objectives.

(b) Requirements for environmental purposes relating to products

106. The representative of Egypt touched upon some areas of concern which his delegation believed should be at the heart of future work. First, the multilateral trading system did not put any serious constraints on a country's right to protect and improve its environment provided that where trade measures were taken for the attainment of environmental objectives, the basic principles regarding non-discrimination and restraint on use of trade restrictions were strictly followed, including the principles of non-violation, nullification and impairment. Second, environmental measures should not be enforced unilaterally or serve as a disguise for protectionism. Third, there was a need for adequate financial resources and acquisition of environmentally sound technology to enable developing countries to adapt to the new standards and regulations in the field of environment.

107. When addressing the relationship between standards and technical regulations and the multilateral trading system, a clear distinction should be made between those standards pertaining to products and those concerned with PPMs. The Agreement on Technical Barriers to Trade extended the coverage of technical regulations and standards to product characteristics or their related PPMs. In this context, and to ensure that "standards are not prepared, adopted or applied with a view to creating unnecessary obstacles to trade", as stipulated in Article 2.2, the

Agreement set three basic principles: the harmonization of product standards; the effective participation of all countries in the work on harmonization of standards, and; the acceptance of equivalent standards and regulations, as clearly stated in Articles 2.4, 2.6 and 2.7 of the Agreement, respectively.

108. Although the implications of setting standards and technical regulations for trading opportunities of developing countries would be adequately addressed under item six of the work programme, he made some initial points. From the point of view of trade policies, standards that were different, higher or stricter than multilaterally agreed standards for environmental reasons could lead to serious trade problems with major implications for developing countries. Such implications would certainly have to be addressed and seriously examined in the course of future work. Two major issues ought to be taken into account in this respect: assistance to developing countries to allow full participation in multilaterally agreed standardization activities as well as adaptation to the new standards and regulations with a sufficient time allowance, and a differential compliance schedule for developing countries in addition to the differential schedule for notifications which existed in the TBT Agreement.

109. In addition, careful attention should be given to the degree of flexibility allowed under the TBT and SPS Agreements for countries to deviate from international standards, especially in the absence of sound scientific evidence and in the context of the application of the "Precautionary Principle" provided for under the SPS Agreement. Furthermore, imposition of restrictions on imports on the grounds that the product had failed to comply with the importing country's PPM standards was only permitted if such standards influenced or affected the quality of the end product and did not have the effect of creating unnecessary obstacles to trade. In this context, adequate solutions would have to be found at the international level by encouraging countries to upgrade their standards through the provision of technical and financial assistance to developing countries on adequate terms to help them acquire environmentally friendly technology.

110. He noted that standards and regulations adopted by countries for environmental purposes often took the form of packaging and labelling regulations. There were growing apprehensions in developing countries that packaging and labelling requirements, though applied on a non-discriminatory basis to domestically produced and imported products, might have adverse effects on trade, particularly for developing countries. Although they were mainly domestically triggered, to respond to the requirements and concerns of domestic products and to the availability of domestic waste disposal facilities and recycling technology, the additional costs that would have to be incurred in obtaining labels or in meeting differing eco-labelling and/or packaging requirements could pose special problems to foreign suppliers, especially from developing countries, thus adversely affecting their foreign trade without necessarily responding to environmental needs and concerns.

111. There was no doubt that eco-labelling systems had gained considerable importance as a result of their increasing use for marketing of products and the recent work on developing eco-labels on the basis of the "cradle to grave approach", particularly with regard to products of export interest to developing countries, such as textiles and clothing, footwear and tropical timber. Furthermore, the narrowness of the selection of criteria and thresholds and the diversity and disharmony of the many eco-labelling systems would make it all the more difficult for compliance by developing countries.

112. In this regard, obligations assumed under the TBT Agreement, especially the provisions in Article 2 and in Articles 5 to 8, which apply to procedures for conformity assessment should be fully respected and adhered to. In addition, and in order to make environmental objectives and

trade mutually compatible, some basic principles should be observed in developing eco-labelling schemes. These included:

- full and effective participation of developing countries in the selecting and setting of criteria, particularly for products of export interest to them; in this context, it could be useful to look at the GATT list of products of export interest to developing countries and, if imported products constituted a large share of the total consumption, then eco-labelling criteria should not be formulated without full consultation with trading partners; and

- compliance of governments or related bodies and voluntary standardization organizations with the ISO "Code of Good Practices", to provide the necessary transparency and timely notification requirements and to ensure that labelling schemes are not set in such a way as to cause barriers to trade or to accord imported products less favourable treatment than that accorded to like products of national origin or originating in another country.

113. Thus, international cooperation was vital in the design and implementation of eco-labelling systems to ensure that certification processes were non-discriminatory and that criteria and thresholds were not set in a manner to discredit or disadvantage like-products originated and supplied by non-domestic suppliers. The elaboration of such criteria through multilateral negotiations would be consistent with both the spirit and objective of the TBT Agreement, which required countries to develop harmonized systems on an international basis for assessment of conformity.

114. The representative of Malaysia, speaking on behalf of the ASEAN countries, focused on the issue on labelling, particularly with regard to timber, since this was an area of concern to the ASEAN countries. The rationale for labelling timber was basically to differentiate sustainably produced timber from that which was not. Sustainability had been generally accepted as a justifiable and valid condition to govern future trade in timber. In this context, trade in timber produced from sustainably managed sources would be allowed and even facilitated through unimpeded access to markets. Timber which was not labelled as coming from sustainably managed sources was differentiated for possible prohibition of trade and use.

115. He noted that, in principle, labelling schemes which were being advanced in the name of sustainability were appreciated by ASEAN. However, there were many concerns in their implementation which needed to be addressed. First, many labelling schemes were promoted in consuming countries ostensibly in the name of sustainability but were governed actually by political and economic expediency. Second, some labelling schemes were unilaterally advanced without any reference to multilaterally agreed guidelines or criteria to suit the needs and interests of the consuming country. Third, many of these labelling schemes covered tropical timber exclusively thereby putting competitors, namely temperate timber and other like-products which were not subject to such schemes, at a distinct unfair advantage. Timber, to a certain extent, also competed with other substitutable materials in the market place, such as plastic, aluminium and steel, and comparable arrangements with regard to sustainability must thus be made.

116. He added that there had been a great deal of differing perceptions and interpretations regarding sustainability which could give rise to conflicts and misunderstandings. First, a producing country's efforts to address environmental concerns or impose certification were often viewed by third parties with scepticism and with the need for verification. On the other hand, third party initiatives, particularly in consuming countries, often lacked understanding of the situation prevailing in producing countries. This experience in timber labelling could also extend to other products and, in general, the key principles of non-discrimination and the avoidance of unilateral action should prevail.

117. The representative of Canada recalled that packaging and labelling requirements had been examined in the EMIT Group where some of the issues that had been highlighted included the relative cost of participation for domestic versus foreign producers, ease of access to information for foreign producers about programmes and how to participate in them, and transparency and access of foreign producers to the process of developing the programme. She considered that, in order to set the framework for analysis in the Sub-Committee, it would be useful to recall one of the central reasons why this item was on the agenda. It was clear that the Sub-Committee was not mandated to examine the relative effectiveness of packaging, labelling, recycling and eco-tax programmes, and certainly not their legitimacy; these programmes played an important role in environmental policy in many of countries. The Sub-Committee was required to examine the relationship between these programmes and multilateral trade rules. To do this, an analytical framework with the following elements was needed: an analysis of the effects of these programmes on trade; an analysis of the necessity and effectiveness of applying these programmes to imported products; and an analysis of whether, when imported products were subject to these programmes, they should be treated exactly the same way as domestic products.

118. She began by identifying the key issues. For example, was the application to imports of those aspects of a programme based on process and production methods not related to product characteristics. Many environmental programmes did not deal with process standards and these, too, could have an impact on trade. For example, requirements related to the disposal of packaging waste had important trade effects. This highlighted the need to also bear in mind that these environmental programmes differed one from another; that even within a certain category of programmes there could be quite different types of programmes; also some programmes were voluntary and others were mandatory which could have analytical implications.

119. In carrying out this work, the Sub-Committee may wish to continue the useful practice of examining case studies of specific types of environmental programmes with a view to achieving a fuller understanding of their effect. With these case studies the Sub-Committee would need to answer many questions, including: on what basis would non-product related PPM criteria be applied to products from other countries? The validity of applying to imports those aspects of environmental programmes related to the use and disposal of products was clear. These elements were aimed at protecting the environment from the impacts of consumption in the regulating country. The rules provided significant scope for setting these kinds of product criteria to address health, safety and environmental concerns. The value and appropriateness of applying to imports those aspects related to production were less clear.

120. In the absence of an international agreement or standard there was no common basis by which countries could assess the environmental impacts of production. This was complicated by the fact that the environmental impacts of a production process could depend on where the production took place. For example, the same level of emission of a polluting gas from a given source could have a different impact in two different locations depending on the overall level of emissions of the gas in question as well as the content of other emissions in the area. This reality begged the important question raised above: what was the necessity and effectiveness of applying the process requirements of environmental programmes to imports for which the processes in question were in foreign jurisdictions? Did their application to imports contribute to achieving their environmental objectives? If the programmes were based on conditions, values, preferences and judgements in the regulating country, how could their relevance to the conditions in exporting countries be gauged? Also, how could exporters selling into a number of different countries with different programmes that set out different process requirements meet them all?

121. The specifics of each kind of environmental programme, packaging, labelling, recycling or eco-taxes, provided their own contexts for these generic questions. Her delegation hoped to

explore all of them through the case study approach. For example, in the context of labelling programmes, her delegation would want to look at how the rationale for eco-labelling programmes, namely to provide consumers with information about the environmental attributes of products to allow them to make informed purchasing decisions, related to the application of process criteria to imported products.

122. Many eco-labelling programmes incorporated a life-cycle approach to the analysis of the environmental impact of products. This was a logical approach from an environmental perspective and when applied to domestic products it provided consumers with useful information about products' impacts. Likewise, those elements related to use and disposal, applied to imports, let consumers know how their consumption would impact upon the environment. But when production stage criteria influenced by domestic circumstances were applied to imports, the criteria might not reflect an objective assessment of the processes' environmental impact. In addition to the obvious environmental information implications, this could have the effect of favouring domestic over foreign producers, in particular those foreign producers who were unfamiliar with the conditions in the importing market. Several characteristics of life cycle analysis contributed to this and highlighted the problems associated with applying production stage criteria to imports.

123. First, to learn everything about a product's full life and its impact on the environment, including everything about every input and the life of that input and inputs to the input and so on, would be too expensive and too time consuming to be practical. Therefore, when using a life-cycle approach a subjective decision was made about what constituted the "life" of a product and what selected element of its life should be considered in the assessment. These decisions may be skewed by domestic circumstances and they may not reflect the environmental realities of a foreign market. Second, quantitative data about environmental impacts was difficult to find. Sometimes it was confidential business information, sometimes it had to be estimated, and other times it was only available by plant and not by product. Therefore, data was often "guesstimated". This raised two questions: was the data good, and was it influenced by domestic realities. Third, there was no common unit of measure for product inputs. Some inputs were measured in currency, others in BTU's or some other measure, and therefore, a subjective decision about the comparability of the different measures was made. Again, domestic circumstances would necessarily play a role in this decision. Finally, environmental impacts were difficult to quantify and compare. For example, what was the value, and relative value, of potential impacts on human health, on the survival of a species or on the preservation of a forest? Making these assessments and comparisons required another subjective decision, perhaps reflecting domestic values.

124. Presumably if there were a common, international understanding of life cycle assessment and how to address these issues and make these assessments there would be less concern about the trade impacts of programmes that focused in whole or in part on the production stage of products' lives and that were applied to imports. Considerable work on this issue was underway in various international fora and was not appropriate for discussion within the GATT. But as yet such a common understanding did not exist. She summarized that this brief discussion of eco-labelling focused on potential trade effects and environmental effectiveness. It was not intended to be a complete analysis of the issue. Referring back to the framework, it did not address elements of necessity such as whether it was possible or desirable to exclude imports from such programmes. She asked whether there were reasonable and realistic alternatives? Neither did it examine alternative ways of addressing imports in these programmes. That analysis was important to complete the picture, but must wait for a later stage.

125. She hoped, however, that this discussion had indicated how a generic analytical framework would apply to specific types of environmental programmes. This type of analysis

must be a key element of all work on this agenda item. Another element, for later discussion, was the application of the GATT and TBT provisions to environmental programmes.

126. The representative of the European Union pointed out that the notion of product related requirements was very broad. Three categories of measures were included in the item, standards and technical regulations, eco-labelling and packaging and recycling requirements. His delegation considered that each of these categories raised specific problems not only as regards their potential trade effects, but as regards the provisions of the multilateral trading system which were applicable to them. His delegation agreed with the suggestion to address separately each of the categories of measures in each of the future meetings of the Sub-Committee in order to have a more focused and more productive discussion.

127. In sharing preliminary reflections for the future directions of the work, he considered that there were already a comprehensive set of provisions in the multilateral trading system which governed the establishment and the operation of standards and technical regulations, including those for environmental purposes. These provisions had established mechanisms to ensure a high degree of transparency in the establishment and operation of standards and technical regulations and they included some substantive principles including the principle of non-discrimination which countries had to apply when defining their own national standards and technical regulations. Most importantly, the provisions of the multilateral trading system had been updated and reinforced in the Uruguay Round. As a result there was now a new TBT Agreement which would provide effective instruments to address undesirable trade effects resulting from the establishment and operation of standards and technical regulations.

128. He considered that if the objective of the Sub-Committee was to consider the relationship between the rules of the multilateral trading system and these categories of measures, this specific category should not be an immediate priority for its work. It would be premature to think about possible rules in the trading system before gaining some experience with the new TBT Agreement. International harmonization of standards and technical regulations was an issue that could be addressed since it could provide an effective tool to minimize negative trade effects resulting from the existence of different standards and technical regulations. But when doing so, it should be borne in mind that countries may need to establish a national level of standards more stringent than those internationally agreed. This was a possibility that was allowed under certain circumstances in the new TBT Agreement.

129. He added that three different types of eco-labelling schemes were listed in TRE/W/12, those based on life-cycle analysis of the product which were usually voluntary, single issue labelling which focused on a particular aspect of the product and were usually voluntary, and finally negative eco-labelling which informed potential consumers about the potential harmful effects of certain categories of products and were usually mandatory. The discussions in the EMIT Group focused on the first type where different concerns were expressed regarding, for instance, the lack of sufficient transparency in the development of national eco-labelling schemes, and the obstacles encountered by products from developing countries in being awarded the eco-label. He added that some of the interventions at this meeting, had also discussed some of these concerns. In view of these concerns, he considered that it would be logical to concentrate work on this type of eco-labelling scheme, even though because of their voluntary nature they did not result in the creation of direct obstacles to trade. Nevertheless they had an indirect effect on trade since they gave an advantage to those products bearing a label in comparison to those which had not been able to obtain the label.

130. The first issue that should be considered was whether the establishment and operation of voluntary eco-labelling schemes was governed by the rules of the multilateral trading system and,

in particular, by the TBT Agreement. He did not have an answer to this question. However, if the final conclusion of the Sub-Committee's analysis was that the TBT Agreement was not applicable, then it should be considered whether it would be appropriate to elaborate new rules to ensure increased transparency in the establishment and management of eco-labelling schemes and adequate participation by producers from third countries. Several options would be possible to achieve these objectives. For example, a specific code of conduct on eco-labelling could be elaborated and, although more work would be required, his delegation was willing and ready to explore all the options possible to achieve increased transparency. At the same time, his delegation hoped that increased transparency and increased possibilities of participation by third country producers could contribute to achieving a better understanding of how the life-cycle assessment approach worked in practice and also to dissipate some of the concerns expressed.

131. Finally, concerning packaging and recycling, despite the valuable work in the EMIT Group, more analytical work was needed. In particular, the Sub-Committee should clarify what was meant by "product-related" packaging and recycling requirements in order to identify in precise terms the instruments and the measures to be considered; there were certainly many packaging and recycling requirements which were not product related and therefore should not be considered under this item of the work programme. He considered it important also to complete a detailed assessment of the potential negative trade effects of each type of instrument and to identify the provisions of the multilateral trading system which were applicable to them. On the basis of this analytical work, the Sub-Committee should be able to identify and consider further steps to be undertaken focusing in particular on those instruments and those measures which had a significant trade effect and which, at the same time, might not be sufficiently covered by the multilateral trading system.

132. The representative of Chile recalled that the EMIT Group had reached a degree of consensus that some characteristics of voluntary eco-labelling programmes might affect trade. The impact on trade would depend on how the programmes were implemented. The choice of criteria for products may imply discrimination against foreign producers insofar as local producers and consumers were within easier reach of local products such as certain raw materials and energy, were aware of the environmental limits on the use of such resources, and the local consumers' preference for certain environmentally-friendly aspects of the products. Similarly, the lack of harmonization in eco-labelling programmes might lead to market fragmentation, making it impossible for foreign suppliers to compete if they were unable to adapt their products to the various criteria. In view of this, it was important for foreign suppliers to effectively take part in labelling programmes so that their products may be able to be labelled in the same way as domestic products.

133. With regard to packaging recovery standards being applied, his delegation believed that their impact on market access should be looked at more closely. His delegation's experience, for example, showed that its fruit and vegetable exporters had had to incur the following costs in order to adapt to such regulations: the technical costs of changing packaging, involving new machinery, training, new non-pollutant compounds, etc.; costs related to payments to packaging producers in the importing country for environmental labelling on the packaging; and potentially lower prices received by the exporter because, as a result of inelastic supply once the products were on the market in the country of destination, the importer would pass on the costs added by the handling and disposal of transport packaging.

134. Although these kinds of standards could not be classed as non-tariff barriers to trade since they were equally applicable within the domestic country for environmental purposes, smaller and more remote foreign producers were obviously disadvantaged in particular with regard to re-using the packaging. Further, as stated in paragraph 52 of document TRE/W/13, recovery, re-use and recycling requirements held significant trade-distorting potential. The competitiveness of imports

may be undermined by the costs of participation in, and the factors hindering access to, the importing country's handling and recycling systems. Finally, the discount applied by local enterprises to exporters' invoices to pay for the services of enterprises which collect packaging at points of sale for recycling may be seen as a hidden way to pass domestic environmental costs on to other countries.

135. The representative of Sweden, on behalf of the Nordic countries, recalled the compilations and analytic summaries of the information received from different countries on their national packaging and labelling measures. This and other documents produced during the work of the EMIT Group provided a good general and analytic picture of various measures and their trade effects. From this work, the Sub-Committee should now draw conclusions on how to proceed in the future work.

136. The task of the Sub-Committee was to review how, within this particular issue, the aim of making international trade and environmental policies mutually supportive could be promoted. To this end the provisions of the multilateral trading system, as they stood after the Uruguay Round, must be examined. Along with the General Agreement, her delegation considered that the Agreements on TBT and on Sanitary and Phytosanitary Measures particularly relevant. Whether the new or amended provisions were adequate for measures necessary to protect the environment must be assessed. At the same time it must be ascertained whether these provisions included sufficient guarantees against misuse for protectionist purposes and unnecessary barriers to international trade. In general, a preliminary answer to these two questions would be affirmative, but would need to be confirmed. This seemed to be the case in particular for packaging requirements related to the package itself. The idea of the new TBT Agreement was to provide an adequate balance between trade interests and environmental protection.

137. However, it must also be noted that certain important areas remained outside the scope of the present, specific provisions. These included recycling and waste management for which it would have to be examined what needs there were for new provisions or amendments. Another important issue that merited further study was whether eco-labelling was covered by the TBT provisions. If so, the present provisions in this regard could be sufficient; if not, the Sub-Committee should discuss options vis-a-vis the provisions of the multilateral trading system.

138. Solutions to resolve the deficiencies in the provisions could be either to widen the scope of the TBT Agreement or to negotiate a new agreement for the areas not covered. Whatever solution chosen, it was important that the central principle of the GATT system, the balance of rights and obligations, be taken into account when assuring that the provisions of the multilateral trading system give sufficient space for necessary measures to protect the environment and that these provisions could not be used for purposes contradictory to the principles of the GATT system.

139. The representative of United States noted that one of the key issues that arose in the context of a discussion of eco-labelling, packaging and recycling was the question of the application of the TBT Agreement. An important distinction in this regard was whether the measures were considered mandatory or voluntary. In thinking about the TBT Agreement, his delegation agreed that health and environment issues were part of the discussions and included in the work programme. In comments made at this meeting, some of the aspects of the TBT Agreement were going to be particularly relevant to the discussion of specific measures. A number of speakers had already addressed the issue of the term "related to" in the TBT Agreement which was relevant to discussions. It would be important to bear in mind how the TBT Agreement should be looked at and how the interpretation of this term would apply to the particular issues under examination.

140. On eco-labelling, he noted that the EMIT Group had done considerable work. He considered it important to note, in discussing the application of the trading system, that what was at issue were voluntary schemes and in this regard, the current disciplines were broad and tolerant in comparison to those applicable to technical regulations. On the other hand, it was important to note that the dividing line between voluntary and mandatory was not always clear and this grey area would need to be explored further to determine the adequacy of the current rules. In looking at these schemes, it was important to understand their environmental objectives and concepts. At the same time, it was also important to take into account the market consequences for business and trade.

141. His delegation would prepare, in advance of the next meeting, an outline that would attempt to bring together many of the points that had already been made in the EMIT Group. This outline would set out in a systematic framework some of the issues and concerns regarding eco-labelling in order to facilitate his delegation's analysis as well that of the Sub-Committee. In doing this, his delegation would synthesize the work done in the EMIT Group as well as elsewhere and add some additional thoughts. His delegation considered it important to begin with the question of why a label was needed to which various perspectives, including environmental, economic, business and governmental, would respond. This foundation would provide a helpful yardstick when considering the specific environmental and trade policy issues that arose with eco-labelling programmes. Next this outline would focus on the various aspects of the quality, utility and relevance of the information provided by eco-labelling. For example, what issues arose from the differences in types of eco-labelling programmes such as multi-issue versus single-issue schemes, schemes that had strict information disclosure versus schemes that drew comparisons between competing products, etc. In this context, it would be important to distinguish mandatory, hazard warning labels from eco-labelling programmes.

142. Additionally, the outline would examine the debate over life-cycle analysis as a methodological issue considering its strengths as well as its weaknesses. Issues with respect to what environmental impact eco-labelling schemes were seeking to address would also be raised. The trade related issues arising from these schemes had generally been well documented in the work of the EMIT Group and the outline would attempt to synthesize this and offer some additional perspectives in areas such as coverage of the trade rules, discrimination, transparency and costs and competitiveness. It was also important to consider the environmental perspective on the relationship with the trade rules, particularly since the development of eco-labelling programmes in many respects was still at an early stage and there were concerns that trade rules should provide adequate space for the development of effective eco-labelling systems. Finally, his delegation would conclude with a brief look at some of the international efforts that were going on with respect to methodological issues. In this regard the current work of the International Standardization Organization, UNCTAD, UNEP, and the OECD were also noteworthy.

143. The representative of Hong Kong sensed an undertone in some interventions that at the end of the process, the Committee on Trade and Environment would be considering modifying GATT principles, relaxing the rules or lowering the standards. He realized that at the present stage the Sub-Committee was analyzing the issues and collecting information and was far from a prescriptive stage. Therefore there should be no preconceived ideas or conclusions drawn. However, for the sake of balance, he noted that it was not necessarily to be considered that at the end of the work the GATT would have to be loosened: on the contrary, it might have to strengthened. The GATT principles might have to be reconfirmed, the disciplines might have to be added to or the standards increased. This was because the Sub-Committee's end results would have to provide contracting parties with more confidence in regard to trade distortions and disguised protectionist measures. The disciplines would have to also check unilateral measures.

144. The representative of Argentina aimed to set the discussions in the proper framework. National regulations on PPMs as instruments of environmental policy were aimed at legislating on environmental externalities generated during the production, consumption and disposal of the product. If the environmental externality arose during the consumption and disposal stages, the PPMs were considered to be "product-related". On the other hand, if the environmental externality arose exclusively during the production stage, the PPMs were not product-related. This type of externality may or may not have effects beyond national jurisdictions, and in the latter case may affect geographical areas shared by more than one contracting party. Consequently, the Sub-Committee should confine itself to analyzing the requirements for environmental purposes relating to products and PPMs that gave rise to environmental externalities during the stage of consumption and disposal of a product, i.e., "product-related" PPMs.

145. Nevertheless, when trade measures included in multilateral environmental agreements came to be analyzed, regulations on PPMs that gave rise to externalities during the production stage, insofar as they transcended national jurisdictions, could also be considered. He stressed that the requirements for environmental purposes relating to products and product-related PPMs, to the extent that they complied with the TBT Agreement, should not in principle be incompatible with the multilateral trading system. However, national regulatory measures of this kind tended to generate trade distortions that were particularly burdensome for developing countries and more especially those considered global traders. Therefore, and in line with the recommendations of the Rio Declaration and the OECD, his delegation advocated the use of market instruments which were more transparent and less likely to distort international trade.

146. His delegation considered that eco-labelling could be a useful tool of environmental policy, capitalizing on the public's interest in preserving its environment and guiding its consumption decisions towards products with externalities that were less damaging to the environment. Nevertheless, his delegation was concerned about some possible distorting effects related to the choice of product categories, the establishment of certification criteria, mechanisms of access to certification, and the possible cost of access to ecolabels for producers located outside the certifying market. These problems might be particularly serious for producers in developing countries. This concern was compounded by the fact that ecolabels fell within a more or less "grey" area of the international trading system. In cases where ecolabels included evaluations of the product's life cycle, they often included evaluations of PPMs with externalities that arose exclusively in the production stage, i.e., not product-related.

147. As the TBT Agreement confined itself to accepting standards related to the characteristics of products or product-related PPMs, ecolabels could not always fall entirely within the bounds of the TBT Agreement, and thus fell partially outside this regulatory framework. His delegation believed that this was a *sui generis* situation that should be analyzed more thoroughly during the Sub-Committee's work. It also believed that it was desirable for this Sub-Committee to try to reach a consensus, which could include recommendations it may wish to submit to the WTO Ministerial Conference. In order to arrive at this consensus it might be useful to seek the cooperation of UNCTAD and ISO; UNCTAD had worked on the evaluation of the possible effects of eco-labels on international trade, while ISO was working on the compatibilization of methods of access to ecolabels.

148. In this connection, he commented on aspects which would make it possible to make the most of the advantages of eco-labels as environmental policy instruments while limiting their possible distorting effects on international trade. These aspects were that: (a) ecological certification systems must have a clear environmental objective and not a trade objective;

(b) accordingly, it must be accepted that environmental conservation criteria applicable for the production cycle should take account of the factor endowment in each production location and not in the certifying market alone; (c) all environmental certification systems should provide for consultation with interested countries prior to the establishment of a specific criterion for a specific product; (d) environmental certification systems should be included in an international agreement aimed at mutual recognition of certification standards and criteria, mutual recognition of certifying entities, and a mechanism for prior consultation with interested countries.

149. His delegation considered that the work on packaging should focus on resolving the issues left pending by the EMIT Group. The discussions held in that Group reached a certain consensus on the possibility of assimilating requirements on permitted types of packaging materials to technical regulations which would mean that they were covered by the TBT Agreement and by the rules on national treatment. The fact that many of the packaging requirements had some type of legal coverage did not mean that they did not create difficulties for exporters. To minimize their adverse effects on trade, there must be strict compliance with the transparency provisions of the TBT Agreement, and the harmonization and mutual recognition of packaging regulations must be promoted. His delegation advocated respect for the national law of each country when adopting measures it deemed necessary to protect its environment, insofar as they did not include disguised discrimination and were based on transparent and provable environmental criteria. In addition, criteria and regulations should be harmonized so as to reduce costs and achieve greater transparency. It was therefore necessary to examine the methodology and institutional environment for carrying out such harmonization. His delegation appreciated suggestions from the Secretariat in this connection.

150. Systems for the recovery, re-use or disposal of packaging were very different. His delegation agreed with document L/7402, paragraphs 61 to 64, that they may also have major trade effects because all these systems were designed taking into account exclusively the needs of the home industry. To minimize the negative trade effects, these systems should be subject to obligations similar to those of the TBT Agreement for technical regulations and standards. Therefore, the future work on packaging should concentrate on analysing how this category of requirements could be incorporated into the TBT Agreement or some new legal instrument dealing specifically with this topic. His delegation was more concerned about regulations that established recycled content requirements on packaging, to which he referred next.

151. He drew a distinction between requirements that regulated the recyclability of a product (or packaging), and those that regulated the recycled content which a specific product (or packaging) must contain. The first type of measure sought to regulate an environmental externality arising in the consumption stage while the second type of measure aimed at regulating an externality that arose during the production stage and therefore should not have extraterritorial application. Whenever an environmental requirement was applied extra-territorially, this undermined the sovereignty of contracting parties. Insofar as environmental externalities did not have consequences outside a national jurisdiction, his delegation did not consider that there were sufficient grounds for accepting this situation.

152. Before accepting the possibility that an environmental measure should generate distortions in international trade, it was necessary to be very clear both about the problem and about the instrument with which it was to be resolved. The challenge was clearly the environmental unsustainability of a culture whose consumption patterns gave rise to a proliferation of waste that exceeded the environment's natural capacity to biodegrade it. Recycling was a valid but inadequate instrument for tackling this problem and should not be considered an end in itself. In addition, if these provisions were trade-distorting, far from serving their environmental purpose they would favour inefficient resource allocation. Given this challenge, the Sub-Committee's

objective should be to modify the environmentally unsustainable consumption patterns which were generally proportional to a society's income level.

153. The GATT/WTO was not the right forum for this discussion, but it was necessary to understand these concerns. Recycling was environmentally important but the efficient allocation of economic resources, including natural resources, fostered by free trade was environmentally much more important. If analysis did not start from this premise, it could justify environmental absurdities, such as the importation of waste in order to be able to re-export it as recycled content so as to meet the requirements of some environmental policy. He did not deny the environmental importance of promoting recycling, but it must be both environmentally and economically rational. Given the nature of this topic, the provisions of the TBT Agreement might not be sufficient. It could therefore be useful for the Sub-Committee to try to reach a consensus on the criteria these provisions should include in order to apply extra-territorially, and consequently give rise to trade consequences that we could then define as legitimate.

154. This consensus, like the proposed consensus for dealing with ecolabelling, should be included in a balanced package of recommendations that covered all the agenda items and emphasize multilateral rather than unilateral policies that may be submitted to the WTO Ministerial Conference. Broad lines of the criteria his delegation would like to see included in this consensus were: (a) recycled content requirements should only be applicable to foreign producers when they were based on the abundance of recyclable materials obtainable in the production area and should not give preference to the use of materials that were abundant in the consumer market; and (b) product recyclability requirements should only be applicable to foreign producers when they regulated an externality produced in the consumer market. The sole exception to this rule should be requirements adopted in the framework of a multilateral environmental agreement.

General discussion

155. The representative of Japan considered that, judging from points referred by previous speakers, sub-items (a) and (b) had common fundamental problems from the perspective of so-called necessity and effectiveness. His delegation saw the diversity and complexity of the measures in item three. These measures were taken to deal with the political, economic, social and environmental needs of each country. Their target setting, approach and employed method for implementation were different from one country to another. Therefore it was useful to explore what rationale lay behind the measures taken by each country. For this purpose continuation of the case-study approach would be most appropriate. Extensive study, as conducted for packaging and labelling, was necessary for the other listed measures.

156. He suggested in future work, the major tasks for this Sub-Committee were: (1) to ensure that measures would not become unnecessary obstacles to trade nor be abused by disguised protectionism, and (2) to examine the necessity and effectiveness of each measure for the purpose of environmental protection. The cases and points referred to in TRE/W/20 indicated that the issue of environmental taxes and charges had broad and complex implications. It required discreet steps for further study. He concluded that because the issues facing the Sub-Committee were various and complex it was more productive to take methodical steps according to the schedule agreed in July rather than seek hasty conclusions. For this purpose, his delegation would continue to make constructive contributions.

157. The representative of the United States spoke about involvement of environmental officials in the work of the Sub-Committee, and more generally about the discussions in this meeting. The U.S. had worked hard to achieve an effective dialogue between trade and environmental officials

and experts and understood that many other countries had gone through a similar process. Despite the difficulties, the active engagement of both sets of policy officials had paid dividends in promoting a more integrated policy in support of sustainable development. This experience suggested there was a high value in becoming educated on each other's respective concerns, and consulting experts directly in policy development.

158. The discussion had confirmed that active engagement by environmental as well as trade officials and experts would be essential to the Sub-Committee's work. Several delegations, for example, presented very detailed statements about when environmental charges and taxes would be effective from an environmental perspective. Similar points were raised with regard to packaging and labelling, for example by Canada. These were significant issues; indeed, the determination of which, among competing measures or instruments, was most effective and feasible to achieve its objective was perhaps the most basic question addressed by his Agency. As the Sub-Committee examined such issues to gain a better understanding of environmental policy concerns, it would be important to engage environmental expertise and perspectives, and to consider concrete examples.

159. He noted that New Zealand's intervention spoke of local versus non-local externalities. It had become increasingly difficult to distinguish between the two. Mexico spoke of the difficulties of quantification, and Argentina and others spoke of the challenge of cost internalization. Quantification was difficult yet environmental agencies and officials still had to make environmental policy decisions on the basis of the best evidence available, and do so in a manner that met the increasingly strong public demand for protection of health and the environment. The U.S. Environmental Protection Agency had just announced the results of a scientific study on the carcinogenic effects of dioxin that had already given rise to considerable controversy. Even in the context of such controversy, the Sub-Committee would need to make a judgement and, if appropriate, take further regulatory action. Malaysia, the E.U., Brazil, India and others also raised important questions related to environmental policy and trade that merited close examination.

160. In the WTO, there could be a tendency for environmental officials and experts not to be actively engaged in Geneva in the work of this Committee; he hoped that this would not be the case. His attendance at this meeting, and the participation of other environmental officials in his delegation, was one way of demonstrating the priority his delegation attached to this point. The development of mutually reinforcing trade and environmental policies required involvement of experts and perspectives from both policy areas.

161. In the same spirit, he had found the discussion of how trade rules applied to these environmental instruments, and the Secretariat [illegible] be most helpful in strengthening his understanding of trade perspectives and how tr[illegible]s might apply to environmental policy instruments that affected trade. He regarded it as an integral part of his work to understand and be responsive to the basic principles and concerns of international trade, in consultation with U.S. trade officials. As agreed in Rio, and on other occasions, the larger task was to integrate policy dimensions toward the broader objective of sustainable development. Accordingly, this Sub-Committee would need to examine both trade and environmental concerns in its analysis. Its terms of reference recognized this connection. They noted, for example, the need for rules to enhance the positive interaction between trade and environmental measures. In this regard, it was helpful to consider the specific role that the Sub-Committee could play with respect to environmental policy. His delegation recognized that the GATT/WTO was not competent to develop environmental policies per se. However, it needed to be responsive to environmental concerns and to avoid unduly limiting environmental protection measures, in support of sustainable development.

162. For example, the Sub-Committee had an opportunity to develop disciplines for trade aspects of environmental measures that preserved their environmental utility without unduly restricting trade. The Preamble to the WTO, reproduced in the Trade and Environment Decision, reinforced this general point, highlighting the broader objective of sustainable development. The Sub-Committee also could play an important role in identifying solutions to trade/environment issues that could be undertaken at least in part in other fora. As one example, the Sub-Committee could lend its support to the development, in appropriate fora, of more harmonized or compatible rules on packaging and/or labelling, to promote both trade and environmental objectives. Second, the Sub-Committee could call for strengthening transparency of domestic regulatory processes and meaningful opportunities for foreign entities to provide input in their regulatory processes in support of improved opportunities for trade and market access.

163. He added that particular effort should be given to coordinate work with other entities engaged on these issues that offered environmental or other relevant perspectives and expertise, including UNEP and UNCTAD. In conclusion, many people, ministries, organizations, and constituencies were watching the Sub-Committee's work. His delegation had come into this process believing that it presented a major opportunity to strike new common ground in support of sustainable development, and hoped to work in a spirit of cooperation toward that end.

164. The representative of Sweden, speaking on behalf of the Nordic countries, noted her concern with the discussions at the meeting. Some participants had painted large threats to the multilateral trading system from perceived environmental protectionists, others had stressed the havoc and administrative chaos environmental measures would lead to in international trade. Her delegation had a great understanding of the fact that some delegations were worried about this process and that there may be different approaches to trade and environment. On behalf of the Nordic countries, she reminded the Sub-Committee of why it had been established and the reasons for its ambitious work programme.

165. The reasons were that awareness of global, regional and national environmental problems had risen considerably and the problems themselves had grown larger and the threats to the common global resources and environment had mounted considerably. Many of these problems could only be solved through common efforts and multilateral cooperation and the multilateral trading system had a responsibility to see to what extent it might facilitate in this regard problems. A responsible start for this work would be to establish and clarify to what extent present trading rules accommodated the needs for taking environmental measures. This, she considered, could be done without any hesitation.

166. At a second stage, the Sub-Committee may find some environmental needs that could not be accommodated by the present rules and her delegation would proceed in this work with the highest possible demands for safeguarding against protectionism or misuse. Her delegation had a long history of promoting free trade and had drawn many gains from it. At the same time it had a high regard for environmental needs and was convinced that the two may and must be integrated for the sake of sustainable development. She underlined especially, that this was work to do in cooperative and on a consensus basis. This was the best guarantee that the trading system would be saved from a jungle of unilateral measures and from those who pretended to be more environmentally aware of imposing their standards or solutions.

167. Her delegation therefore hoped that all countries would engage in the work in a constructive way. Her delegation was convinced, that in many areas of the work programme, the present trading rules were more than adequate to meet environmental needs. In many of the areas her delegation believed that results must be reached sooner rather than later. And by the sole

process of establishing this, her delegation was convinced that many of the radical demands for changes to the multilateral trading system would be set to rest.

168. She circulated copies of a recent publication called "Trade and the Environment, Towards a Sustainable Playing Field, which layed out prevailing problems and interlinkages between trade and environment with which the Sub-Committee as well as other fora were dealing. This book did not provide solutions but laid out some of the more important aspects of the interlinkages in the debate from various perspectives. Its aim was to give an integrated approach to the trade and environment policy field and therefore the various chapters had been written by people with different academic backgrounds. Chapter 1 gave an ecological background and overview, Chapter 2 was written from an economic perspective and Chapter 3 laid out the institutional perspective including the institutions and rules at hand and what changes may be needed to accommodate environmental needs, Chapter 4 included conclusions with policy recommendations.

169. The representative of China observed that his country was a developing country with significant trade and environmental importance. His delegation recognized the appropriate relationship between trade and environment and that trade and environment should be mutually supportive. On the one hand, trade measures for environmental purposes should not conflict with the rules and principles of the multilateral trading system and should be employed on the basis of transparency, justifiability, non-discrimination and least trade restrictiveness. On the other hand, countries differed to a varying degree in environmental policy measures and regulations due to different levels of economic development as well as specific national situations. Therefore, it should be expected that one country's environmental policies and practices may not necessarily be appropriate for application in other countries. From a trade point of view, environmental measures must not serve as a means of disguised protection.

170. He stressed that the pertinent provisions in multilateral MEAs, especially those in favour of developing countries, should be fully taken into consideration while addressing issues in relation to the interaction between trade and environment. His delegation recognized charges and taxes as price-based mechanisms which could be used for sustainable development objectives. As an important economic consideration for environmental protection, the "Polluter Pay Principle" had been widely accepted in many countries including China. There was an evident trend that taxes and charges were being gradually introduced to achieve national environmental goals. It was his delegation's view that internal taxes and charges for environmental purposes and issues related to BTA should be handled with due care. Within the context of the multilateral trading system it would be both important and necessary to identify and examine fully the taxes and charges which were currently in place before passing judgement on the next steps to take. This could help to ensure the correct guidance to the process of trade, environmental and financial policy making.

171. Concerning sub-item 3(b), there was no doubt that technical requirements, packaging, labelling and recycling had recently gained considerable importance. His delegation noted that, due to different development levels, criteria for eco-labelling were different from country to country; therefore, one country's labelling system could not be completely or entirely applicable to other countries. The debate in this meeting and the Secretariat documents provided a good basis for discussions in this regard. In order to advance future consideration of the subject, his delegation hoped that the GATT Secretariat would collect more information on the eco-labelling practices in as many countries as possible. China had done a lot of work in respect of eco-labelling. In October 1993, China organized an International Environmental Labelling Exhibition. This year, it had established the National Certification Committee for Environmental Labelling, and the first set of six products would be certified very soon.

172. The Chinese delegation had a significant interest in and was ready to contribute actively and constructively to the work of this Sub-Committee. In order to exchange views and share experiences with other members of this Sub-Committee, it was prepared to supply to the Secretariat relevant information on China in relation to items 3(a) and 3(b).

NGO participation

173. The representative of the United States said that, in order to maintain a high level of credibility throughout the Committee's proceedings it was important to incorporate principles of transparency in its procedures, including allowing interested NGOs (which would include groups representing environmental, developmental and business interests) whose work was relevant to the Committee's work to observe its proceedings.

174. The majority of WTO signatories had already recognized the constructive role of NGOs in other contexts. Article 71 of the UN Charter established the legitimacy of an NGO presence in international activities. Chapter 27 of Agenda 21 built on this early directive and urged signatories to invite NGOs to take part in the formulation of policies and implementation of development programmes. Chapter 38 of Agenda 21 called upon all intergovernmental organizations to design open and effective means to achieve cooperation and interaction with NGOs. NGO work in implementing Agenda 21 was noted and it was agreed that NGOs should have access to any UN reports and information. The Uruguay Round Final Act recognized the value and legitimacy of consultation and cooperation with NGOs in Article V(2), which stated that the General Council may make appropriate arrangements for consultation and cooperation with relevant NGOs.

175. NGOs had observed UN proceedings for many years and UNEP, UNDP, UNECE, among others had taken proactive steps to address NGO involvement. The World Bank's current Directive on Disclosure of Information created a presumption in favour of disclosure, outside and within the Bank, in the absence of a compelling reason not to disclose. It had also established an Inspection Panel to ensure that the Bank's rules were being followed. The Bank's experience showed that external consultations enhanced the quality of its operations. In addition, the Economic and Social Council had granted NGOs consultative status to observe the proceedings of a range of UN organizations, such as UNEP and the Commission on Sustainable Development (CSD).

176. Other international bodies had also allowed NGOs to observe and in some instances participate in a more structured approach. The OECD input was channelled through advisory groups which represented specific interests. In 1962, the OECD had created the Business and Industry Advisory Committee (BIAC) and the Trade Union Advisory Committee (TUAC) which held consultative status with the Secretariat and met annually with the Ministerial Conference Chair and the Secretary-General. Such a structured approach permitted productive input but preserved the country-to-country nature of the organization.

177. His delegation thought that it was helpful for NGOs to observe the proceedings of the Committee since its work directly involved matters of broad public interest. In the area of the environment, NGOs had served a useful role as providers and disseminators of information and expertise. Many NGOs had been active in international fora for decades and had committed great enthusiasm, talent and money to educating lawmakers in environmental matters. Efforts had been characterized by sophisticated identification of and research on environmental issues and assistance to government agencies responsible for policy choices.

178. Many countries had expressed reservations regarding NGO observation due to numbers and possible disruption. His delegation agreed that permitting NGOs to observe Committee proceedings must not be allowed to interfere with its efficient operation. However, appropriate ways could be found to address these concerns by limiting the number of seats, with appropriate consideration to balance and diversity. The Committee should consider methods by which to structure NGOs to observe, drawing from the experience of other international organizations, which provided sufficient openness without compromising the Committee's country-to-country dialogue or impeding productive deliberations. The Committee might also wish to consider defining guidelines on when observation would be appropriate. Practical reasons existed for limiting NGO access to certain sessions as business could not be effectively conducted if every meeting were made available for public discussion. The specific needs of negotiations, for instance, would preclude the presence of NGO observers. However, relevant information on most meetings could be disclosed without problems. Non-transparent proceedings perpetuated a "fortress" image of GATT and diminished public confidence in, and support for, WTO work which contributed to misunderstanding and suspicion of the deliberative processes of the trading system. Insularity should not be allowed to undermine the WTO's progress, nor should openness compromise its effectiveness. Undue limitation on NGO involvement could impede the flow of ideas and information necessary for informed policy and complicated domestic trade liberalization agendas.

179. His delegation thought that the Committee could benefit from the "two-way street" that would result from allowing NGO observation of its proceedings. If properly structured, this practice could advance the Committee's deliberations and contribute to an open consideration of the complex issues that constituted its mandate.

180. The representative of Egypt considered that the FAO should have the same observer status as the World Bank, IMF and UNCTAD in the Sub-Committee. Reflecting on the US statement, he stated that although Egypt had opposed the idea of bringing environmental concerns into GATT much agreement had been reached which was evident at Marrakesh. Concerning transparency, he referred to the GATT's symposium on trade and environment and the derestriction of documents which had helped to remove suspicions about GATT's work. However, the main issue was that negotiations must remain between governments. As such, his delegation was opposed to NGOs having observer status in the meetings.

181. The representative of Sweden, speaking on behalf of the Nordic countries, agreed with the US that transparency in GATT was important and could be improved. Particularly in trade and environment, an issue that engaged people and organizations globally, many misunderstandings and misconceptions could be corrected if the mysticism around GATT/WTO disappeared. However, her delegation thought that this was best done through a greater openness of documentation and frequent dialogue between GATT and interested NGOs. She advised against admitting NGOs as observers, primarily based on the difficulty of deciding whom to admit. If GATT were to open to all interested parties, it would be filled with lobbying organizations from various groups, such as steel, agriculture, consumer groups. She asked how the screening would be done in order to admit only "legitimate" environmental NGOs and who was to determine that agricultural or industrial organizations did not have a legitimate right to observe. It would also be difficult to ensure a fair geographical distribution in participation.

182. In her delegation's opinion, the need for transparency should be met through other means. Not least would be to ensure thorough coordination and participation at the national level. GATT should contribute to openness but should not be a substitute for domestic transparency. Her delegation welcomed intergovernmental organizations, like UNCTAD, the World Bank and others, as the Committee would need analytical input from other sources. Therefore, the Sub-Committee should keep an open mind to admitting organizations that might provide assistance in its work. At

the CSD May session, participants had underlined the contribution by organizations such as UNEP and the OECD and recommended that they be involved in future work on trade and environment. Her delegations thought that these organizations should contribute to the work of the Committee and welcomed other relevant intergovernmental organizations to participate as observers.

183. The representative of Hong Kong stated that it was opportune to raise this subject as a substantive contribution to the Committee's mandate to provide input to the Preparatory Committee. He was encouraged by the fact that the Committee was exploring possibilities with no preconceptions. He stated that transparency did not equal participation and there were many ways to provide for transparency in GATT, such as the Trade and Environment Bulletin, the NGO symposium, and the derestriction of documents. But transparency could also be achieved at the national level, where regular mechanisms could be established with NGOs in recognition of the role they could play in providing ideas, disseminating information and increasing public awareness. Certainly, there could be no objection to establishing a channel of effective communication, but this must be done step by step. Participating in meetings was the highest level of transparency and his delegation felt that this might not be necessary. The experience so far with NGOs was that it was difficult to define what they were. The preparatory process would take up the question of observership and there were likely to be rather stringent criteria, even for intergovernmental organisations.

184. The representative of Japan appreciated the detailed explanation and concrete proposal of the US delegation. He recognized the increasing interest among NGOs concerned with environmental issues. He shared the concerns of Hong Kong and Egypt with respect to institutional efficiency, management and the nature of GATT/WTO as an organization of governments. His delegation could not accept the US proposal. Recognizing that there were environmental NGOs as well as other NGOs, including business, consumers and private persons, he wondered how criteria could be set to limit participation. In addition, at the end of negotiations, countries had to face difficult decisions and make compromises. With respect to transparency, he felt that there were other ways to improve the situation, including improving domestic mechanisms for transparency.

185. The representative of India referred to Article V of the WTO in order clarify the mandate and the rule with respect to NGOs which allowed for some discretion. Article V(1) stated that "the General Council shall make appropriate arrangements" and V(2) "the General Council may make appropriate arrangements." The central issue was not one of numbers or unmanageability but the danger of the politicization of the GATT/WTO. It was important to decide what kind of future institution the WTO would be. He said that there was a tendency to shift the responsibility for transparency to the multilateral institutions, namely GATT/WTO. The danger was that this might be extended to other areas in the future which would involve a serious transformation of the character of the GATT/WTO, which was a legal contract between governments with rights and obligations and an advanced dispute settlement procedure. Thus, he did not see where the comparison with the World Bank or OECD precedent lay. He saw national governments having a fundamental and primary responsibility for transparency with NGOs in their jurisdiction.

186. The representative of Austria supported the statement of the Nordic delegations. His delegation had expressed the view on several occasions that there should be openness with respect to the participation of intergovernmental organisations which might provide contributions to the work of the Sub-Committee.

187. The representative of the European Union welcomed the statement by the representative of the Environmental Protection Agency of the United States and assured him that there were a great number of environmental representatives in his delegation and their expertise was needed in

capitals and in the Sub-Committee in order to ensure an appreciation of environmental concerns. He had an open mind towards observership of intergovernmental organisations, specifically FAO. In this context, he noted that among the UN bodies, UNEP and the CSD had done important work in the area of trade and environment, and should be present at the meetings of the Sub-Committee.

188. He responded to India's statement which reflected on the differences in wording between "shall" and "may" in Article V. He noted that in the Decision on Trade and Environment, Ministers at Marrakesh had explicitly invited the Sub-Committee to give input in how relations between NGOs could be arranged in an appropriate manner and he considered that the Sub-Committee must act seriously on this invitation. He considered that if the Sub-Committee wanted to be taken seriously by NGOs, it had to take them seriously. In view of Article V, his delegation felt that the US proposal deserved careful consideration but, as other delegations had pointed out, there were many specific practical concerns which arose and he appreciated the US flexibility in its approach to this issue.

189. The representative of Malaysia, speaking on behalf of the ASEAN countries, supported the Nordic statement concerning NGO participation in the Sub-Committee. Many negotiating positions had been developed by countries through interaction with domestic interest groups and this domestic policy formulation process could be extended to the environment. He welcomed the US flexibility in this respect. There were many ways in which to enhance transparency in GATT. However, he agreed with the Indian delegation that transparency should not be the sole responsibility of GATT/WTO but of national governments.

190. The representative of Uruguay supported the statement of Hong Kong. Noting that this was not her delegation's final position, she said her delegation was concerned that the general issue raised in Article V of the Final Act was not limited to environment-related NGOs. The Sub-Committee's work on this topic should be done in parallel with or after, but not prior to, work of the Institutional Committee, taking into account all WTO bodies. Her delegation agreed with the delegation of Sweden that it was important not to turn the WTO into a forum for different lobbying interests. It was difficult to determine what preference should be given to environmental NGOs as opposed to NGOs with interests in other areas. Her delegation supported efforts to increase transparency but felt that it was necessary to consider internal transparency among contracting parties and the existence of guarantees ensuring their participation in WTO work. If transparency included participation of NGOs, there was a risk that their excessive participation might lead to more informal GATT meetings, to the detriment of some delegations.

191. The representative of New Zealand said that his delegation had listened with interest and would study the US proposal. Noting the range of options to consider, he said that transparency could be provided by building on the mechanisms of other organizations where concern had been taken to protect their country-to-country nature. He supported the statements concerning the nature of the GATT/WTO and the primary role of domestic mechanisms to foster transparency. Members of the OECD, as well as others, had agreed on guidelines on domestic transparency and on involving domestic actors in policy formation. His delegation recognized the need to promote transparency but this did not necessarily equal participation. For instance, his delegation would be concerned if mechanisms would actually result in transparency being lessened for geographically or financially disadvantaged NGOs. In this context, he was interested in the statement by the US Environmental Protection Agency concerning the involvement of environmental officials in the Sub-Committee.

192. The representative of Australia said that his government was currently examining transparency in the Sub-Committee and the wider WTO application. In Australia there was a consultation process involving both briefing and debriefing NGOs so their views could form part

of the Australian government's policy position in international institutions. On the basis of equity, he questioned whether it was fair that some NGOs would have a second opportunity to input into the system.

193. The representative of Mexico welcomed the US statement and said that her delegation would examine it. As stated by the delegate of New Zealand, her delegation did not always bring environmental officials to the meetings but this did not mean that they were not involved in domestic environmental policy process. She clarified that the question of effectiveness of environmental charges did not mean that her delegation was challenging the usefulness of this instrument for environmental purposes as every country had the sovereign right to decide on the best manner to design environmental policies. However, clarification was required as to the effectiveness of applying such measures to imports, which was related more to trade than environment and was relevant to an assessment of the trade impact of such instruments. She said that her delegation would examine the US transparency proposal; her delegation shared the concerns of other delegations that it was important to be clear about the type of character which was to be imparted to the WTO with respect to transparency.

194. The representative of Korea stated that his delegation could not support the participation of NGOs. Having listened to the previous speakers, he agreed that NGO input could be provided in the process of decision-making in each country.

195. The representative of the United States was encouraged by the positive reactions from a number of delegations to the proposition that it was necessary to improve transparency. He said that his delegation would take into account the concerns which had been expressed with regard to his delegation's proposal in order to be able to move forward. He noted that in the preparation of the statement, there had been a deliberate distinction drawn between participation and observer status. His delegation was aware of the numbers problem and was looking for practical ways to accommodate the need for outside observers yet address the physical and operational impediments which might result. Transparency would have to be a process which was managed both quantitatively and qualitatively and would take into account the need to ensure geographic representation. With respect to the notion of double input, there was a distinction between domestic processes and having NGOs observe Committee proceedings; this was a concept which was inherent in Agenda 21. He said that the process of engaging NGOs in discussions was constructive and productive. Once the process was opened up, those NGOs which had a interest in contributing and participating stayed with the process. In effect,his government had given the NGOs a stake in the process and they were better able to understand his perspective as a trade official as well as inform him on their perspective.

196. The representative of Pakistan inquired as to whether, if transparency was to facilitate NGO input, such contributions were only possible through observership. He said that participation would have to be discarded given the problems mentioned by many delegations.

197. The Chair concluded the discussions by stating that he detected that it was in the interest of all members to provide for an exchange of information and transparency with all appropriate actors legitimately involved in the issue of trade and environment. It would be necessary to find a way to organize a relationship with NGOs that would benefit the Committee's work. He said that he would conduct informal consultations on three points: the exchange of information and transparency; observer status for intergovernmental organizations in the Sub-Committee; and domestically prohibited goods. He said that DPGs might be an issue where progress was possible in the short term. He would give an interim progress report of the consultations at the October meeting. He also reminded delegations of his invitation to them to submit, on a voluntary basis,

to the Secretariat for compilation, information that reflects their own national experiences with measures that one covered under the third item of the work programme.

197. It was agreed that the Sub-Committee's next meeting would be held on 26-27 October.