

**Report of European Commission Regional Workshop on
Sustainable Development and Regional Trade Agreements**

San José, Costa Rica

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Radisson Europa Hotel & Conference Center

OPENING SESSION: The workshop was opened by *Allan Flores Moya*, Vice-Minister of the Environment and Energy of Costa Rica and *Ambassador Tomas Abadia Vicente*, Head of the European Commission Delegation in Costa Rica. Mr. Flores stressed the importance of the DR-CAFTA agreement, and the need to balance economic and environmental priorities within the agreement, noting that expanded commercial relations should increase employment and wealth. The Vice-Minister said that the issues that need to be addressed include increasing education; clarifying the implications of trade on poverty; defining equity as a crucial component of sustainability. He noted that the imposition of unilateral trade measures did not coincide with sustainable development. Ambassador Abadia noted that the approach of the European Union entailed cooperation and dialogue; measures to protect human rights; expanding trade and investment; and strengthening governance and related measures to support sustainable development. He underlined the importance of the region for the EU and the latter's desire to develop further its partnership.

SESSION ONE: SETTING THE CONTEXT IN INTEGRATING SUSTAINABLE DEVELOPMENT AND REGIONAL TRADE AGREEMENTS

Pierre Defraigne, former Deputy Director General, DG Trade, European Commission, began by noting that sustainable development implies stable economic growth, without inflation; social progress, including reducing inequality and poverty; and supporting environmental sustainability. In looking at the challenge of sustainable development, he noted that China and India in the context of globalization represent a new paradigm and radical change: international mobility continues to accelerate; comparative advantage, particularly in manufacturing and services, is changing rapidly. For example, India is combining cheap labor and high-end technology, while China continues to experience high rates of economic growth, fueled by huge purchases of oil and other resources, which are benefiting commodity producers, but placing new pressures on environmental balances. For Costa Rica and the Central American countries, these changes continue to create dramatic pressures, demanding a leap-frog in regional integration rather than leisurely gradualism. He cautioned that a radical regional integration supported by domestic reforms is needed to save Central America from marginalization.

Mr. Defraigne pointed to different models of regional integration: that of the European Union, MERCOSUR, the Andean Community and others. While there is clearly not a "one-size-fits-all," each regional trade agreement must be compatible with the World Trade Organization (WTO). He noted that the European Union is comprised of countries of diverse size but that most are small (a point relevant for Central American countries in their own efforts at regional integration), with benefits including economies of scale and strengthening competitiveness at the regional level in order to face the global economy. He noted the genuine complexity of trade and development: while there can be no

development without trade, trade does not in itself bring development. An important component of development is good governance and quality of domestic policies, pointing to the importance of flanking policies in order to share benefits and burdens of trade adjustment. He underscored that domestic policies do not come for free: there is a need for efficient, fair and transparent tax policies to support flanking policies, pointing to countries with both high tax rates, high levels of productivity stemming from investments in infrastructure; and high levels of per capita GDP. He concluded by noting that regional agreements can see the convergence of various measures -- environmental, sanitary and other norms -- and opens the possible harmonization or mutual recognition at the regional level. He pointed that regional agreements are effective in spurring development; and create momentum through "peer pressure." He concluded that the European Union would never impose its own priorities on its trading partners, but looked forward to cooperation.

Jaime Granados of the Integration Department of the Inter-American Development Bank looked at regional integration from a trade perspective, and explored how trade can help support deeper integration in Central America, and how sustainable development goals can be supported. After recalling the definition of sustainable development framed in the Brundtland Commission report, articulated at the 1992 Rio Summit and put into practice through various Multilateral Environmental Agreement (MEAs), he recalled that the main characteristics of regional trade agreements (RTAs) include an increase in trade; reforms of domestic policies; and support of democratic practices. He pointed to the experience of NAFTA in this regard, where regional security has become an overarching issue under the NAFTA. In recent years, some 60 different trade agreements have taken shape in the region, with a new generation of agreements increasing. He noted that since the 1990s, trade has increasingly been a vehicle to promote investments. However, major problems with RTAs continue: most fail to address agriculture, subsidies, and labor mobility and migration issues, but also are more flexible in issues like rules of origin for textiles, as well as problems (such as carve-out for sugar). He noted that while there has been a lot of rhetoric about the supporting mechanisms and cooperative agenda, it is difficult to identify actual programs with a supporting, new budget. He noted that several RTAs contain general preamble language regarding environmental protection as well as an environmental chapter and this an advantage. He asked how environmental chapters can be enhanced, including if and how progress in addressing production process methods can be address. He noted that RTAs coincide with and are supportive of a number of other reforms, including tax reforms; the need to increase competitiveness; support juridical and administrative support, including private property rights, and develop the private sector and civil society. However, he cautioned that despite the positive aspects of trade, it has been proven unable to alleviate poverty and halt environmental degradation. He concluded by pointing to the urgent need to strengthen domestic institutions, cautioning that the Washington consensus is not enough, with the new role of the state still emerging.

Alice Mattice, Director for Trade and Environment Policy Planning of the Office of the United States Trade Representative (USTR), discussed the experience of the US in supporting environmental provisions in RTAs, including agreements with Chile, the CAFTA-DR, and negotiations underway with Panama and the Andean community. She noted that the CAFTA-DR and its Environmental Cooperation Agreement represents the

most forward looking agreement, with a potential to make a real difference in advancing environmental objectives. She noted that the approach of the US was to include environmental provisions within the core text of the legal agreement, in order to give environmental provisions high visibility; and to promote coordination between trade and environmental ministries, in support of three main provisions: (a) the obligation to maintain high levels of domestic environmental regulations; (b) the obligation to effectively enforce domestic environmental laws. She noted that this provision continues to attract attention, because of its link with formal dispute settlement provisions; and (c) the obligation that parties do not weaken regulations to attract investment. She noted several other important features of the agreement, including its commitment to strengthen environmental governance; to promote public participation and awareness; to establish a Council structure; to promote voluntary mechanisms involving the private sector; and to undertake environmental reviews of trade. Ms. Mattice noted other advances in the CAFTA-DR agreement, including innovations in the public submissions process; which although modeled on the North American Agreement on Environmental Cooperation Article 14 and 15, differed in that a clear link is set out between the provisions and capacity-building. She pointed that the CAFTA-DR also supports good environmental regimes, but resources are a problem, and enforcement is a key challenge: CAFTA recognizes cooperation and capacity-building. She noted that the work-program for the Environmental Cooperation Agreement is currently being elaborated, with an emphasis on promoting enforcement; supporting the CITES convention; improving transparency; managing natural resources; and supporting clean technologies.

Discussion: *Alejandra Aguilar*, Environmental Advisor of the Ministry of Foreign Trade of Costa Rica, moderated the discussion following the first session of the workshop. She noted that all speakers emphasized the important role of RTAs in development and their potential to support sustainable development. They can help provide stability for local governments, training, and provide valuable links to small and medium-sized enterprises. She noted the importance of tax reform as highlighted by the first speakers. During discussions, several speakers noted that indirect and unclear link between trade and economic development. One questioned the role of sanctions in general, as well as why the fines imposed in the CAFTA-DR were comparable to the fines in the Chile-US FTA, given the difference in GDP between Central American countries and Chile. With regards the cooperative program, some questioned if the current program had been accorded a lower priority, particularly since the level of funding has not been clarified. During discussions, *Ms. Mattice* observed that while the fine structure was in place in the CAFTA-DR, based on the over decade-long experience of the NAFTA in which a case never emerged, it was unlikely that fines would actually be imposed. With regards the budget, it was noted that the financial commitment to the cooperative work program was under review by the US Congress, with an emphasis on improving the coordination and use of existing resources, and allocating the \$20 million currently allocated by Congress in 2005 for labor and environment. Three approaches of the EU were noted by *Pierre Defraigne*: (a) its preference for RTAs over bilateral agreements. He noted that the real benefits of RTAs are mainly changes within region: they are a catalyst to change policies, and deliver development. Easier to bring about change when partners work in tandem, bring about synergistic effects; (b) the use of the asymmetry of market access to compensate for

asymmetry in competitiveness between different trading partners; and (c) trade agreements need to be seen as part of a broader package of cooperation policies, including financial package: between 2002 and 2005, the European Commission has committed 250 Euros for Central America to deliver key development policies. *Pierre Defraigne* noted that the Central American region is lagging behind more and more, because of lack of adequate domestic policies and the main bottleneck is tax policy. Tax reform is more important than trade. But trade can help create a sense of urgency in introducing active social and environmental policies.

SESSION TWO: TRADE-RELATED INVESTMENT AND SUSTAINABILITY

Roberto Echandi, Former Lead Negotiator for Investment and Services of Costa Rica, explored the relationship between trade-related investment provisions and expanding commercial activity. He noted that trade-related investment provisions important but not sufficient to promote development. In general, he noted that RTAs are not part of a strategic development policy, but represent an important political process. However, often civil society has little knowledge of what free trade agreements contain, and what they set out to achieve. In general, free trade agreements include social, political, and other goals in support of development. However, these secondary objectives can lead to the wrong perception that they can solve problems of inequality, social upheaval and distrust. The lessons of NAFTA and Chiapas are too high expectations of trade in solving social problems can lead to a backlash. He then noted that the current CAFTA-DR investment provisions modeled on the NAFTA Chapter 11 Investment provisions have been beneficial in clarifying expropriation procedures. He noted that international investment provisions have existed since 1959. However, NAFTA marks a new direction in investment rules, by linking those rules to trade. He noted that expropriation provisions are based roughly on US “takings” laws. There has been some fear that these provisions would have a chilling effect on investors. However, he noted that since 1994, when NAFTA entered into effect, there have been a total of 40 Chapter Eleven disputes, of which only one – the Metalclad case – accepted the direct expropriation argument. Moreover, he argued that the test is not whether disputes arise with market integration, but whether formalized dispute settlement rules are in place. Based on the NAFTA model, the CAFTA-DR includes national treatment provisions, enabling the state the freedom to regulate. CAFTA Article 10.12 and Annex 10.c: in fact clearly state that countries are free to regulate, and his main conclusion was that investment chapters in general do not reduce the capacity of the state to regulate. He noted that no contradiction exists between investment and environmental provisions. He also pointed to several carve-outs, including telecommunications. In general, Mr. Echandi noted that Central America needs to diversify manufacturing and agriculture, and pointed to deep structural problems, including very high rates of migration and high unemployment levels.

Julie Raynal of DG Trade of the European Commission, EC, began by noting that the new generation of trade agreements include investment, competition, services and other provisions, as a recognition that tariff reduction alone is not enough to support market integration. She pointed to recent analysis by UNCTAD and the World Bank in stressing

the importance of foreign direct investment in supporting development, including financing of infrastructure to facilitate development. At the same time, she noted little empirical evidence between bilateral investment treaties (BIT) and changes in FDI. Despite public concerns, she noted that trade-related investment provisions did not undermine the right of countries to regulate. She questioned the general perception of some groups that BITs are regarded as opening space for investment, while RTAs that contain trade-related investment provisions were seen to impede right to regulate. Instead, she argued that RTAs in general adopt a positive approach to liberalization; that countries can use MFN and national treatment exceptions, and hence, ensure high levels of flexibility. When a country wants to facilitate technology transfer, investment provisions can help such efforts, and more generally support environmental protection. She cautioned that increased market access is not linked to deregulation; they are two distinct and separate initiatives. Moreover, trade can increase the need for increased regulation, as has been seen in the liberalization of some service sectors. She noted that the private sector has an obligation in ensuring investment liberalization is supported by corporate social responsibility; and referred to the OECD guidelines for Transnational Corporations as being an example. The OECD guidelines have been signed by a number of non-OECD countries, including Brazil, Chile and others, noting that in the EU-Chile agreement, there is a reference to the OECD guidelines. These guidelines promote disclosure and transparency; ensure that technology supports the domestic science and technology agenda; and takes into account domestic environmental laws. She noted that countries should not seek exceptions as a pre-condition of investment, and commitments need to be supported with monitoring. There are other examples of investment frameworks, including the Kyoto Protocol and its Clean Development Mechanism; the US-Cambodia textile agreement. She concluded by proposing that a Forum be established between the Central American countries and the European Commission, in which to exchange best practices regarding investment in support of sustainable development.

Ana Lorena Guevara, Manager of the Bioprospecting Division of the Instituto Nacional de Biodiversidad of Costa Rica (INBIO), examined the potential that biodiversity endowments can play in supporting increased trade. Biodiversity provides a source for new products, particularly in the pharmaceutical sector. Central America has a huge potential, but there's still need to increase current efforts to increase scientific knowledge, apply innovation, and create new avenues for development. She noted the positive partnerships that have taken place with pharmaceutical companies, which have opened new opportunities for the commercial application of genetic or biological diversity resources. A number of different applications of biodiversity have been explored, including traditional medicine, water treatment, biotechnology, pesticides and others. These applications can deliver measurable benefits from investors. However, challenges remain in extracting services from nature. With support from the IDB, work continues in developing pharmaceutical, bio-pesticides, the production of generic drugs (and modification of patent laws), and ornamental plants. With RTAs, companies will invest in INBIO-related products, as well as invest in research and development for products and services. However, support is needed in training for small and medium-sized enterprises.

Discussion: *Carlos Murillo*, of the Centro Internacional de Política Económica para el Desarrollo Sostenible (CINPE) moderated the discussion following the second session. The importance of dispute resolutions was suggested. The possibility of expansion of Costa Rican melon exports to the United States with the CAFTA-DR was also discussed and it was also noted that in the CAFTA-DR, there are no quotas for melons. Moreover, other possible export opportunities under the agreement for a range of products, including tuna, sugar, textile, tuna, and leather products were discussed. It was noted that CAFTA-DR contains a distinct tariff-rate quota for organic sugar. The experience of NAFTA Chapter 11 was pointed, suggesting that it was not compatible with sustainable development, and the need for a paradigm shift. Another participant noted that while the benefits of biodiversity use were considerable, mechanisms were needed to ensure those benefits were distributed to rural communities. Concern was also expressed about the risk of stop bio-piracy, in which foreign companies would develop commercial products and services, drawing upon the genetic or biological resources, without sharing the benefits with host countries and communities. For example, the use of traditional knowledge has been shown to save 20 years of research and development for the pharmaceutical sector. It was noted that more needed to be done to widen the distribution of benefits. To that end, several agreements have innovated through shared patents and copyrights, and an agreement with the University of Costa Rica whereby 50 percent of benefits would be shared by the owners of the genetic resource. It was noted that bio-piracy is a risk. However, striking the right balance between regulations and an enabling environment. Excessive regulations could hamper innovation. There are many laws at the national and global level regarding protecting biological diversity. However, in all countries of the region, there is a need to increase capacity, particularly with communities so they can negotiate with large pharmaceuticals. One participant noted that the OECD guidelines referenced in the EU-Chile FTA are intended to remind companies to guidelines wherever they operate, rather than setting out obligations. It was also noted that different approaches to investment exist in different agreements: while the NAFTA follows a negative approach, the EU investment provisions are based upon a positive listing approach. .

SESSION THREE: REGIONAL TRADE AGREEMENTS AS AN ENGINE FOR SUSTAINABLE DEVELOPMENT

Geoffrey Garver, Director of the Submission on Enforcement Matters Unit, of the North American Commission for Environmental Cooperation (CEC), provided an overview of the background, mandate and functions of the CEC. He began by recalling the background of the NAFTA debates, including the fear that free trade would create pollution havens, have a chilling effect or backsliding of environmental regulations, and concern about the scale effects of trade. NAFTA was the first trade agreement to include environmental provisions within the legal agreement, as well as implementing parallel environmental and labor agreements. Among the higher-profile aspects of the North American Agreement on Environmental Cooperation are measures to ensure the effective enforcement of environmental programs, including a series of provisions regarding the access to remedies set out in Articles 14 and 15. This approach has been repeated in the DR-CAFTA and Canada-Chile, but not in the US-Chile. The CEC contains four main program areas:

pollutants and health; environmental law and policy; the conservation of biological diversity, and trade and environment. In addition, the Secretariat of the CEC – located in Montreal – can initiate independent reports under its Article 13 provisions. After ten years, among the lessons of NAFTA forwarded by an independent panel include the following: the dire predictions of pollution havens or a race to the bottom have not occurred; environmental laws have not dampened the economic benefits of trade. NAFTA and the CEC have helped in capacity building and information sharing; in promoting right-to-know and access to information; and undertaken some harmonization efforts. He noted some of the specific program areas, including the phasing-out of DDT in Mexico – a program now being shared with Central America through a partnership with the WHO and PAHO -- and supporting the sound management of chemicals; children's health and the environment; supporting shade-grown coffee in Mexico. Turning to the submissions on Enforcement Matters Unit, Mr. Garver noted that submissions are received from individuals regarding regulatory enforcement matters. The Secretariat determines if a threshold is met, and if so, recommends to Council if a factual record should be prepared. Council can either approve or reject the recommendation. To date, the CEC has 10 active submissions under determination, and four factual records are under preparation. In total it has received 50 submissions, of which roughly half are from Mexico. Mr. Garver noted the developments of CAFTA-DR around enforcement matters, and the cooperative agenda more generally, and offered the experience of the CEC as a useful reference in what worked and what did not.

Oscar Sanchez, of the Fondo Nacional de Financiamiento Forestal of Costa Rica (FONAFIFO), explained Costa Rica's program to support payments for environmental services. He began by noting the importance of social preferences, including the importance a society places in forestry conservation, noting that Costa Rica has a great potential in biodiversity and forestry. At the same time, there are limits to environmental services markets, particularly involving the number of buyers. He noted that Costa Rica was interested in sharing the experience of the FONAFIFO program with neighboring countries. Mr. Sanchez, mentioned a new area of work of FONAFIFO that entails pursuing carbon-related credits in the context of the Clean Development Mechanism of the Kyoto Protocol, and the Prototype Carbon Fund of the World Bank. Other examples include the link between forests and watersheds, and developing various non-timber forestry products (medicines, tourism and recreational services). He stressed the importance of linking services to the internalization of environmental externalities. Programs need to be transparent, and develop auditing and monitoring programs. The result of the FONAFIFO program has been a significant expansion of forested areas, and an alleviation of poverty.

Sergio Musmanni, Director, National Cleaner Production Center, Costa Rica, examined the role of cleaner production, noting its potential to increase the efficiency of production, reduce waste and strengthen financial performance. He noted that in the CAFTA-DR agreement, cleaner production was identified as a priority area in the Environmental Cooperation Agreement (ECA). He noted that for several key sectors, including coffee, bananas, and sugar, the current production methods were the same as those of 50 years ago. Considerable potential exists in these sectors, as well as in the hotel and other sectors. He

noted that consumers are changing their preferences; while technical barriers to trade (TBT) and sanitary and phytosanitary measures (SPS) identify various barriers to trade, such as packaging and labeling, other mechanisms are needed to alert producers/exporters to changing consumer preferences. He noted the importance of improving the quality and dissemination of information. He provided several examples of cleaner production in Costa Rica, including reducing waste generation; improving the water and energy sectors; targeting small and medium hotels; developing environmental indicators such as life-cycle analysis in order to support extended producer responsibility.

Discussion: The discussion after this session was moderated by *Diego Masera*, Coordinator of the Industry Program of the United Nations Environment Program, Regional Office for Latin America and the Caribbean, who, began by noting that environmental service payments and cleaner production offer new trade and development opportunities for Central American countries; the latter in particular provides new lessons in technology transfer. Discussing the experience of the CEC, it was suggested that the completion of a factual record was never intended to be the end of the exercise. The exercise anticipated from the outset that various stake-holders would use the factual records to bring attention to issues. The CEC has examined how the submission process has affected policies, beginning with the first Article 14 case involving a proposed cruise-ship port expansion in Cozumel. In general, the CEC has also improved the coordination between trade and environment officials. The discussion then turned to the FONAFIFO program, that has supported environmental education and the need to protect the forestry sector. It has helped turn around the very high rates of deforestation of the late 1980s, by creating fiscal incentives to owners to lower rates of deforestation. The program uses certificates for forest areas, which are not restricted only to those who pay rents. Since 1995, the program acknowledges that forests yield a diversity of services, and the program increasingly is looking at financial resources beyond local sources, including the CDM and Kyoto Protocol. With regards cleaner production, it was noted that while the green agenda in Costa Rica is very strong, the brown agenda is less so. Innovative approaches are needed, including using user charges for waste generators. Examples of technology transfer include solar technology as well as soft technologies such as waste treatment; beverage production technologies; the development of bio-pesticides and other products.

SESSION FOUR: REGIONAL TRADE AGREEMENTS AS A CATALYST FOR SUSTAINABILITY IN BUSINESS

Juana Galvan, Central America Regional Specialist for Policy and Trade Negotiations of the Inter-American Institute for Cooperation in Agriculture focused on how RTAs can create new opportunities for agricultural and other environmental goods. She noted that RTA present challenges by accelerating changes faster than anticipated. She pointed to the changes in agricultural processing and technologies needed to meet quality standards, and the increasing importance of consumer demand for product criteria that includes environmental, social, and labor standards, as well as a strong interest among consumers in stringent health, food safety and nutritional standards. Compounding these changes is the concentration of distribution within large companies, like supermarkets and Wal-Mart.

Large buyers are going directly to producer, and often criteria is imposed directly upon them. One example is the emergence of organic produce, in order to help meet health, labor, environmental and other criteria. She noted the need for producers to keep pace with technological innovation, including complying with both mandatory and voluntary standards. There are various new challenges that arise from voluntary standards, including: the role of differing disciplines in the WTO, NAFTA, CAFTA-DR and other agreements; the unfinished agricultural agenda, particularly related to subsidies; the diversity of domestic environmental laws and the need to improve the dissemination of market information to track changing consumer preferences. She noted that Central American countries have a potentially strong comparative advantage in organic agriculture, and noted the space CAFTA-DR opens with the quota for organic sugar. She asked if other organic produce could be explored because of this opening, for other produce.

Robert Dilger, Coordinator of the Program Sustainable Management of Natural Resources and Promotion of Entrepreneurial Competences, of GTZ Nicaragua examined the role of public private partnerships by explaining a program with organic cocoa in Nicaragua, and the model it could provide for other products in Central America. He noted that historically, Nicaragua has produced cocoa since the Maya, but today, it has become relatively a very small exporter on the world market. This is partly because of a very large domestic demand for cocoa. In 2004, it exported 550 tons of cocoa, of which 150 tons were organic. A key challenge is to increase the efficiency of production, in order to target the growing demand for chocolate and organic chocolate in Europe and China. He noted that trade is open, since there are neither tariffs nor quotas imposed on cocoa. Cocoa is considered an agro-forest product, in which no agro-chemicals are used, in which yields support agro-biodiversity goals more generally. However, there are various risks in organic cocoa, including damages from fungus. He noted the need to ensure high levels of quality and support certification systems, including both product and certification of origin certification systems. Finally Mr. Dilger highlighted that the GTZ initiative is very innovative in the sense that it has incorporated a series of stakeholders from the private and public sector. In fact, he said it is a major partnership between GTZ and the Ritter Sport Chocolate Manufacturer in Germany.

Ron Steenblik Senior Trade Policy Analyst of the Organization of Economic Cooperation and Development (OECD), discussed the extent to which RTAs could support trade in environmental goods and services. He noted that most negotiations in this area are taking place at the multilateral level. A more challenge in negotiations entails classification issues and lists. One list that is a basis for negotiation in the WTO is based on the OECD-Eurostat list, and the APEC list. Although this issues was identified by the Doha Round as a priority, no international definition of environmental goods exists. By contrast, the WTO definition of environmental services includes wastewater, sanitation services, and other (for example, air pollution services). He noted the potential RTAs have to promote EGS, in the same manner that RTAs promote trade more generally. He suggested that the CAFTA-DR ECA has the potential to support environmental compliance more generally, which could in turn support high levels of environmental protection and the promotion of environmental goods and services.

Discussion: An important question addressed during the discussion following this session, concerns the question of production process methods (PPM) in the trading system, and whether examples from Central America, in areas like forestry and organic produce, could benefit from the inclusion of some PPM criteria. However, it was noted that most developing countries in the WTO and regional trade agreements remain opposed to the inclusion of PPMs in a definition of environmental goods and services, because of problems that include customs clearance and administrative issues, as well as more general legal scope issues. Although some suggestions have been made by developing countries to include a narrow list of agricultural products in the WTO negotiations, most discussions of environmental goods are taking place in the non-agricultural market access negotiations. As a general point, it was suggested that while most discussions assume that regional trade agreements are trade creating as opposed to trade diverting; it was unclear of the overall effects of the CAFTA-DR and other RTAs on trade patterns.

FEEDBACK SESSION: SUMMARY OF FIRST DAY AND GENERAL COMMENTS

Robin Ratchford of the DG Trade European noted the points of general agreement from the previous sessions included: there are considerable potential benefits of RTAs in supporting sustainable development. However, there was recognition that trade alone was insufficient to propel development, and there was a need for additional funds and stand-alone capacity-building programs. Trade is not only about tariff reduction, and a key question is how far integration will take place in Central America because of trade and market integration, and whether there is a strong enough foundation to build convergence. There was also general agreement regarding the importance of transparency and accountability. At the same time, several key challenges were highlighted, including: the role of small and mid-sized enterprises in coping with the potential benefits of trade. What will be the pattern of winners and losers in the region, and how will costs be absorbed. Will trade be enough to spur competitiveness? Several examples of innovative approaches were examined that build upon the region's comparative advantage, including: the FONAFIFO environmental payments program; cleaner production and organic agriculture. While progress continues, major challenges in certification, overcoming market information barriers. There were different proposals, including sharing the experience of NAFTA; and creating a forum for best practices in investment. It was noted that given that the tone of interventions was uniformly positive, one wondered why some trade negotiators remain so allergic to trade to sustainable development, and why some non-governmental groups continued to oppose trade liberalization in general?

In the discussions that followed participants intervened to make the following comments:

It was noted that promoting sustainable products by differentiating them based on PPMs created challenges to the trading system, particularly administrative and bureaucratic challenges. Goods need to be differentiated at the border, based on customs (HS) codes. If there is a disagreement about the characteristics of products – for example if it is energy efficient – then it is impossible for a customs official to verify countering claims. For example, in the area of sustainable fisheries, there are objections of some governments to

sustainable fisheries standards developed by the Marine Stewardship Council. Another problem relates not so much to meeting the standards, but problems of conformity assessment. But RTAs can support the development of regional standards, and explore cooperative actions in areas like marketing, common certification systems, and other areas. Another speaker noted that while non-governmental standards are booming, reflecting changing consumer preferences, the trading system is not keeping up these market-based developments. The need to elaborate the concept of sustainable goods was noted. When officials examine PPM issues, there is a need to acknowledge differences in environmental norms, and related differences in social preferences. There is a need to approach this issue as a package: in which developed countries compensate asymmetries in development with asymmetries in market access. In general, it was noted that sustainable development is an issues that will not go away: it has taken a lull since Seattle, but issues of worker rights, core labor standards, human rights, the abuse of children, are not dependent upon the level of development of a country but rather are basic rights.

It was noted that private standards evolve as the perceived needs of sustainability are not begin addressed by governments. Corporate social responsibility programs have their own internal accountability mechanisms, which are built on trust. Some standards, such as organics, reflect clear and precise legal definitions. In general, it was noted that RTA are primarily economic instruments, and will not support sustainable development goals within the region. It was felt that the definition of the relationship between free trade and sustainable development needed to be defined clearly: free trade is a tool that support development; but also can increase problems like migration, the exploitation of natural resources, and the ability of regulators to regulate. One noted that ten years after NAFTA, Mexico still had huge poverty levels, income inequality gaps, and a smaller number of companies engaged in export than before NAFTA. At the same time, the political instability in the region is growing, in Ecuador, Bolivia, Peru and elsewhere. It was noted that fiscal reform is urgently needed, and responsibility of additional investment and capacity building should come from the industrialized counties. It was noted that countries needed to shift from the current situation of low wages, low taxes, and high levels of corruption, to high wages, high taxes, and a reasonable level of corruption, so that the benefits of trade would be more evenly spread.

SESSION FIVE: CORPORATE SOCIAL RESPONSIBILITY AND FAIR TRADE

Daniele Giovannucci noted the growing importance of market mechanisms that include sustainability principles, including fair trade and ethical issues. He noted that the fair trade, organic and eco-friendly mechanisms differ somewhat in their definition, but they continue to grow on world markets. Viable strategies are needed to help poor countries cope and benefit from this demand growth. He noted a study by the World Bank and UNCTAD, suggesting that of 25 major commodity groups, only 10 groups have the potential to expand, and of those, most involve large-scale agricultural plantations. These developments appear to do little to help the poor. A key challenge for developing countries is to capitalize on the importance that branding plays in world markets: brands are associated with quality, and bring with them a price premium. He noted that many large

corporations are setting their own definition of sustainability, and appear to be mainstreaming those definitions within all product lines, creating a challenge for small-scale producers looking to carve out a market niche and premium. Indeed, he noted that almost all large companies are developing their own social standards, in order to differentiate their company from competition, as well as to hedge against the risk of bad press. Overall, companies are aware of need to manage risk social risk: examples include Chiquita, GAP, Nestle, Starbucks and other companies that are developing standards. Although companies are clearly interested in standards, they are also concerned about the predictability and quality of supply. This in turn suggests a potential paradigm shift, in which the increasing demand for standards places additional challenges on small-scale producers in developing countries. He suggested that countries needed to intensify their dialogue and partnership with the private sector, and identify specific roles in which governments can provide support, including in certification, overcoming market information barriers, supporting extension services; research and development, and other areas. Challenges remain, including confusion among different standards, limited markets, as weak domestic institutions, and the potential that standards can act as barriers to trade.

Rene Vossenaar, Former Head of the Trade, Environment and Development Branch, of the Division on International Trade in Goods and Services, and Commodities of UNCTAD, examined how to address environmental criteria in trade, including their implications for competitiveness. Specifically, he noted that environmental goods and services bear costs to producers and exporters, including certification costs and maintaining information related to product chains, etc. He noted that the number of certification groups has grown steadily, from 300 in 2002 to over 430 in 2004. During the same period, total sales have doubled, in products like coffee, sugar and honey. The global organic market has grown by 20 percent a year, albeit from small market shares. Growth rates in Europe appear to be slowing, but still favorable. In coffee markets, while trends suggest an increase in organic production, data on trade remains imprecise. He noted that Costa Rica is on the European Union list that accepts equivalent standards. This is important, since 40 percent of farm exports from Costa Rica are destined to Europe. He noted the need to provide assistance to small-scale producers to raise awareness, and help them comply with standards.

Jason Potts, Coordinator of the Sustainable Commodity Initiative, of the International Institute for Sustainable Development (IISD), explored the challenges faced by small scale producers in meeting fair trade systems. He noted that fair trade has raised awareness of wage and equity issues, but remains a very small percentage of total markets and has not entered the mainstream. It is difficult to set out a single definition of fair trade, but all definitions include reference to fair wages, the upholding of core labor standards, and a commitment to be environmentally friendly. He noted that with market failures, these systems have been developed on the consumption side to various failures. Supply chains have their own governance structures, which are innovative but fragile. Mr. Potts mentioned that various problems persist in this area, including a gap in the willingness-to-pay of consumers; constraints in the capacity of small-scale producers to access environmental markets; high transactions costs; problems of multiple certification and related costs; a lack of micro-financing; and lack of infrastructure to support small-scale farmers. In addition, small-scale farmers in developing countries have a limited role in shaping different

systems: the criteria for fair trade systems usually set in the north, and may create a bottleneck. Overall, RTAs can create some opportunities, by helping to establish standards at the regional level and identifying supporting mechanisms to exports in these niches.

Patricia Barbuscia of the Instituto Ethos de Empresas e Responsabilidade Social provided an overview of general trends in corporate social responsibility, and recent partnerships in Brazil. She noted that general perception that trade and globalization are not meeting public preferences; she noted that while something is wrong with globalization, it is unclear how to improve it. She noted that the main force of fair trade originates with consumers. By contrast, CSR originates with companies, and involves companies looking at risks and how best to respond to those risks. She noted that in Latin America, poverty has a gender and a color: high rates of poverty affect women and black populations. The objective of CSR is to develop a business strategy that promotes ethical and other values. It shifts the focus of business orientation from shareholders to stakeholders, and looks at business performance beyond minimum compliance.

Discussion: The discussion was moderated by *Chris Wille*, Chief of Sustainable of Rainforest Alliance in Costa Rica. Participants raised the issue of producers bearing the cost of adopting fair trade, organic and eco-friendly product labels, and companies adopting CSR obligations, and whether it was possible to measure the benefits as well as the costs in adopting such systems. It was noted that enterprises involved in fair trade are a tiny percentage of the market, and problems remain in overcoming multiplicity of standards. It was suggested that trade is not the best mechanism to solve a range of non-trade social issues. Moreover, the countries did not need trade as much as they needed good governance to solve problems like corruption, and oversee the conduct of the corporate sector. It was noted that certification poses a real cost to producers, and this remains complicated because of multiple certification bodies. At the same time, the trend seems to suggest that standards are increasing, and it is likely that the majority of all goods will have some kind of seal or branding in the next twenty years.

SESSION SIX: ASSESSING THE EFFECTS OF TRADE

Eric Peters of DG Trade, European Commission, explained the approach of the European Commission to Sustainability Impact Assessments (SIA). He began by noting that while optimal trade outcomes assumes that liberalization is always conducive to development and equitable growth, in the real world, there are market distortions and failures, and winners and losers from trade. The SIA is intended to avoid simplistic answers to complex issues, and help obtain a fuller understanding of the complex effects of trade, including differentiating trade impacts at the global level, where they are diffused, as opposed to impacts at the local or sub-regional level. An important part of the EC SIA approach was to ensure a broad consultation process, based on the following themes: (a) examine trade and sustainable development, as opposed to a more narrow trade-environment nexus; (b) examine effects beyond the countries of the Commission, in order to seek global and region-specific views; and (c) ensure a legitimacy in the public consultation process. He noted the need to RTAs with national and regional governance structures. Among the

results of the work to date includes a better understanding of general effects of trade; the view that trade exacerbates existing trends, rather than introduces new pressures. However, questions remain regarding the scope of scope analysis; the challenge in modeling different WTO disciplines outside of tariff reduction. Despite these and other challenges, it was felt that the consultation process has been wide; and the SIA has helped inform trade negotiators.

Benjamin Simmons of UNEP examined the relationship between RTAs and sustainable development, noting that the Bruntland definition of sustainable development called for a balance of differing priorities. He noted that everyone agreed to sustainability in general, but when one looked at the trade-offs required to strike a balance in particular sectors, then decisions in support of sustainable development became difficult. For example, in the farming sector, how to balance the trade-off between farmers losing their jobs because of technological innovation versus lower prices of produce for consumers. He suggested that a useful follow-up workshop should examine a scenario in one or two sectors, and then work through the different implications of that scenario to understand differing interests. He explained the background the approach of UNEP to Integrated Assessments, which in many ways are similar to EC's SIA: that is, they involve examining the economic-social-environmental nexus. He noted that assessments increase information available to decision-makers, enhance policy coordination, help to build consensus; save time and money insofar as they entail up-front costs to run assessments, but recommendations from them can help avoid more costly negative impacts. Helpful to define national objectives, in which the scope of assessment helps define its end-use. He noted that the process of assessments is very important, in building local capacities in a transparent and inclusive manner. He also stressed the importance of engaging local actors to understand the implications of liberalization: for example, in one study, although trade was supposed to lead to a price reduction for one commodity, consumers did not benefit from any price drop because of the pre-existing oligopoly structure led to a price cartel. In another case, even with the decline in rice prices, producers did not exit that market because the amount of rice is seen as a status symbol among local communities. UNEP has conducted a number of assessments, including studies in Chile (mining), Ecuador (the banana sector), Colombia (the rice sector) and Argentina (the fisheries sector). He noted challenges in assessments, including the problem of valuation, selection of environmental indicators, and the need for better training of experts and stronger institutions.

David Brooks, Director for Natural Resources Policy and Environmental Reviews in the Environment and Natural Resources section of the Office of the U.S. Trade Representative (USTR), explained the US experience in trade assessments, noting that the US has a long history in conducting written reviews of trade, beginning with the NAFTA environmental review in 1992. He pointed the 1999 Executive Order requiring written reviews of trade to be undertaken. To date, five environmental reviews have been completed for the WTO, the FTAA and 4-5 regional or bilateral assessments. He highlighted three lessons to date: the importance of the process; the need for flexibility in methods; and the benefits in looking at the policy relevance of reviews. On process issues, he noted that the process of reviews often more important than the document produced. The process involved collecting information, and supporting a framework to discuss the implications of findings among

different government agencies, and between the government and the public. He noted that the timely exchange of information is a critical element in the success of reviews, noting the need to start the process early; adjust the timing to coincide with the critical elements of the negotiations; invite public to comment on each step of assessment (scope). Second, with regards the flexibility of methods, he noted the use of different analytical tools needed to capture all factors. A common analytical framework entailed: (a) the analysis of economic-derived environmental effects, and (b) analysis of the possible effects of the US in the ability to regulate possible effects. Although reviews examine primarily the effects in the US, they also examine implications of trans-boundary or global environmental effects. He noted the need to cast a wide net in the review process, to take into account a variety of information, including the situation of trading partners to understand their interests. The final lesson is that reviews, which are ex ante, have become an intrinsic part of trade negotiating process.

Silvia Chaves Executive Director of CEDARENA, noted the importance of reviews taking into account the particular legal, institutional and juridical processes and conditions of countries of Central America, as well as changes in export-intensive sectors. She noted that the countries of the region continue to experience important structural problems, political and geographic differences that need to be taken into account. She pointed that the purposes of assessments entail identifying areas of potential cooperation, as well as specific sectors in need of capacity-building assistance. She provided some highlights of their work in Costa Rica and Guatemala, noting that in general, Costa Rica has a clearly-defined agenda to define the environmental benefits and impacts of trade, while Guatemala had less defined regulations, and fragile environmental capacities. She pointed to potential impacts on soil, water, and biological diversity of increased trade in two sectors (sugar and melon) analyzed in an assessment conducted within an OAS program, and the need to develop standards and norms, as well as a system to monitor impacts, and the need to modernize systems and support clear regional cooperation efforts. She proposed three specific areas of priority action: (a) the need to reform national laws and modernize regulatory and oversight capacities; (b) the need to engage private producers in helping to improve the understanding the effects of trade, and align normative standards and other enforcement with private sector participation; and (c) identify the maximum opportunities likely to arise from free trade, and identify specific areas of cooperation to help ensure those benefits are realized.

Discussion: The discussion after this session, examined the relative merits of ex ante versus ex post assessments, noting that the former well designed to inform negotiators of likely effects of trade agreements that should be taken into consideration. It was felt that not many sustainable development assessments of regional agreements had been undertaken to date, while mitigating measures developed after assessments were difficult to identify. It was felt that ex ante reviews did not release a public document until the negotiating text was known, and ex ante helped identify all positive and negative outcomes.

SESSION SEVEN: LESSONS IN INTEGRATION AND FUTURE STEPS

Rita Mishaan, Advisor to the Ministry of Environment of Guatemala, recalled the history of integration in Central America, and its implications for sustainable development and the CAFTA-DR agreement. She recalled that regional integration began in the 1970s in Central America, but the region still faces strong challenges, such as inflation, migration, unemployment, corruption and low levels of capital inflows. At the time integration began, she mentioned most countries of the region lacked Ministries of the environment. While today all countries have environmental Ministries, many are weak institutions. She noted the discussions in the CAFTA-DR agreement, including the environmental provisions set out in Chapter 17 including the legal facilitation of disputes, public mechanisms for environmental law, and other provisions. She recalled that in 1994, the Presidents of Central America developed an Alliance for Sustainable Development, with a pledge to address the three pillars of sustainability and in so doing, reduce poverty and support development. She noted that since the 1992 Rio Summit, the countries of the region have signed a number of environmental conventions, including Stockholm, the Convention on Biological Diversity, and other accords. In addition, the countries of the region have contributed to the Millennium Development Goals, but noted that progress has not been positive in meeting those targets. She cautioned that most countries are not complying with these treaties/statements; that the gap between rich and poor continues is growing; that the current agenda of MEAs does not respond to the balance between development and environmental protection. She warned that there cannot be environmental protection while there is still hunger, but noted optimism that trade agreements could close the gap between rich and poor countries.

Lawrence Pratt, of the Centro Latinoamericano para la Competitividad y el Desarrollo Sostenible (CLADS) of INCAE in Costa Rica, explored the prospects of regional integration in supporting sustainable development. He assumed that countries of the region have embraced the logic of regional integration, but still need to examine if they will compete at international level given their natural resources, limitations in labor markets, lack of capital and other constraints. He suggested some national policies needed to point countries in the right direction, beginning with the following points: international trade pushes higher environmental standards; Central American countries are a price taker and a rule taker; so that the success of the Central American countries depends on its capability to meet rules. Implementing rules requires institutions and structures. A chief barrier involves the proliferation of non-tariff barriers, including SPS measures, minimum content of products, third-party certification, and other obstacles. He noted that to compete, Central American companies must comply with these requirements as a pre-condition of market access. The problem is that many companies in the region do not understand these rules. He noted the systemic problems of competitiveness, and the absence of mechanisms to help companies comply with standards: there are no institutional mechanisms to allow exporters to demonstrate compliance, and noted that in general if there is a bad national and regional image on one set of products, it will generally impact all other producers. Therefore, it is essential to improve the image of Central American producers, by adopting environmentally-friendly standards.

Discussion: During the following discussion two trends in Central American markets were noted: foreign companies that adopt high environmental and social standards of products intended for export, and local producers that are not in compliance with domestic regulations. Participants noted the risk of market access of pesticide and other residue, and also warned that new standards related to methyl bromide and restrictions on plastic waste could harm local producers. It was pointed out that environment negotiators in RTAs have less experience and a lower profile than trade negotiators, and efforts are needed to strengthen

the Ministry of Environment in each country and ensure that Ministers are able to support the environmental agenda in negotiations. The question of melon production and exports was noted, and it was felt that differing standards needed to be addressed.

CONCLUSIONS AND NEXT STEPS

Pierre Defraigne noted that the global economic system has undergone dramatic change since the 1980s, fueled by technological change and the neo-liberal revolution. At the same time, China is transforming globalization. He noted that globalization is a necessary and irreversible trend, contributing to greater interdependence, but it is fraught with threats and dangers. For all promises, he said, if globalization is left without rules and appropriate domestic policies, it can push social and environmental strains to a breaking point. Regional integration with sustainable development is the best answer for small and medium sized economies. In looking at trade and development, consensus exists that there is a strong link between the two, but with two qualifications: first, causality can work either way. In some cases trade is driving force behind development; in some other cases, it is vice versa. In all instances, the quality of domestic policies, and good governance will determine the benefits of trade liberalization. He argued that RTAs can support good governance, and can go farther than WTO by tackling obstacles behind the borders, including addressing investment, intellectual property and other areas. He stressed the importance of partnerships among countries in sharing principles and values to support integration. There must be flexibility and common responsibilities in RTAs with different modalities based on differing capacities of the partners. He suggested that a common observatory to follow the environmental and social aspects of RTAs would be useful.

Carlos Murillo, stressed that trade should not be isolated from other priorities. He emphasized the relationship between trade and development, noting that trade per se will not lead us to development, and that not all countries receive the benefits of trade equally, noting that one of the goals of the WTO Doha round was to ensure that the developmental benefits of trade were realized. He noted that taxation appears to be less of an important issue in the region, given the list of Singapore issues before countries. However, he argued that tax reform and productivity were essential challenges. The low tax levels in the region meant little money for governments to invest in infrastructure and social safety nets. He noted the importance of the regional process, and the opportunity presented by negotiating as a regional group. He concluded by noting that regional agreements have played an important role in the development of environmental policies, citing NAFTA as an example. He noted that environmental-related trade opportunities that are opening in the region, including bio-prospecting, organic agriculture, cleaner technologies and technology transfer. He stressed the important role of the private sector, noting that if commerce is to be sustainable, it must be profitable. He noted that important lessons related to transparency, citizen participation, and good governance arise from RTAs, and noted that some governments are afraid of some of these issues. In view of this, these agreements oblige countries to deal with many of these governance issues. There is great fear in the governments because of participation – this makes many of the governments feel uncomfortable. Finally, he noted that cooperation is important, but noted that no country

has changed from developing to developed status simply through cooperation. Cooperation is helpful but not the solution.

Gustavo Mayen noted that countries of the region are in a transitional period, and it is important to keep the future in perspective. He highlighted the need to adopt a broader vision of regional integration, one in which a union of Central American countries is indispensable. CAFTA is an economic instrument rather than a development instrument; it needs to be complemented with clear developmental goals. The twenty-first century will be known in history as the century of trade agreements and the century that changed its production patterns towards environment and sustainability.

The meeting was formally closed by *Robin Ratchford* of the DG Trade European Commission.