



COMMENTARY

# Response to the United States Trade Representative's Stated Objectives on NAFTA Negotiations: *An environmental perspective*

Nathalie Bernasconi, Liesbeth Casier, Ashley Racine and Scott Vaughan  
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This week, representatives from the United States, Canada and Mexico will continue North American Free Trade Agreement (NAFTA) negotiations. One of the key issues being discussed is the environment. Trade agreements like NAFTA can affect environmental objectives in two different ways. First, they may outline explicit environmental provisions, such as those incorporated in investment chapters or side agreements. Second, they may outline provisions that are not environmental per se, but that nevertheless have environmental impacts. Among others, these may include provisions regarding investment, public procurement and the establishment of standards. *The IISD–UN Trade and Green Economy: A Handbook* provides a better understanding on the interlinkages between international trade, the environment and the green economy. *A Sustainability Toolkit for Trade Negotiators* helps negotiators in processes such as the NAFTA renegotiation to position international trade and investment as a driver of sustainable development.

In July 2017, the United States Trade Representative released its list of NAFTA objectives.<sup>1</sup> Several of these directly or indirectly relate to the environment. The section on environment includes a fairly long list of objectives.

## Environmental Institutions and Processes

The environmental objectives outlined by the United States Trade Representative (USTR) propose a fundamentally revamped NAFTA environmental regime, one that entails embedding environmental provisions within the legal agreement, thereby terminating the NAFTA side-agreement model that was created amid a fierce public debate in 1994.<sup>2</sup>

<sup>1</sup> Office of the USTR. (2017, July 17). *Summary of the objectives for the NAFTA renegotiation*. Retrieved from <https://ustr.gov/sites/default/files/files/Press/Releases/NAFTAObjectives.pdf>

<sup>2</sup> "Bring the environment provisions into the core of the Agreement rather than in a side agreement" (p. 13).



Currently, NAFTA comprises environmental provisions embedded within the legal text, as well as a separate environmental side agreement: the North American Agreement on Environmental Cooperation (NAAEC). The centrepiece of NAAEC, the Commission for Environmental Cooperation, has supported a range of cooperative environmental programs since it opened its doors more than two decades ago, from North American-wide trans-border data and monitoring to capacity building and expert exchange regarding the prevention of toxic pollution. The commission has attempted, though with only limited success, to create an innovative cross-border environmental assessment process and supported a unique citizen complaint process. This work has been country-led, supported by a small secretariat and tiny annual budget.

Shutting the doors to the commission, whatever its shortcomings, may recall how a previous Canadian federal government closed the National Roundtable on the Environment and the Economy. If the current commission mandate ends with a new NAFTA, then government action is needed now to preserve more than two decades of data and research. More importantly, its replacement must perform beyond the current institutional model.

The prevailing trade–environment model supported by most countries in bilateral and regional free trade agreements (FTAs) entails embodying environmental provisions within the trade text. This approach is found among many trade agreements, including all U.S. bilateral agreements, the Canada–EU Comprehensive Economic and Trade Agreement (CETA) and the draft Trans-Pacific Partnership (TPP). Thus, the USTR objectives would move NAFTA to the currently prevailing model, which does not set up a permanent institution along the lines of the NAAEC.

But does the prevailing approach lead to a more effective environmental regime linked to trade? It depends.

The 2007 Korea–U.S. Free Trade Agreement (KORUS)<sup>3</sup> environmental chapter uses environmental language from previous bilateral U.S. agreements. Notably, this language refers to a standard non-derogation and related effective domestic regulatory enforcement required under U.S. fast track authority. Additionally, it includes reference to some Multilateral Environmental Agreements (MEAs)—notably the Convention on International Trade in Endangered Species of Flora and Fauna (CITES)—as well as reference to addressing illegal wildlife traffic and fisheries. A new NAFTA will undoubtedly include these measures.

It's hard to measure what outcomes KORUS has achieved in environmental protection through these provisions alone. Normative principles of an environmental chapter were issued by South Korea and the U.S. in 2007. An Environmental Affairs Council was created, along with 18 other committees, in 2012, when the agreement was signed. One senior bilateral meeting of the two governments under the newly established council was held in 2015. There appears to have been one joint air quality project—the KORUS–Air Quality between the U.S. Environmental Protection Agency (EPA) and the Korean National Institute of Environmental Research.

Another example of an active work stream from a U.S. bilateral free trade agreement is the 2006 U.S.–Peru Free Trade Agreement<sup>4</sup>. According to U.S. assessment, U.S.–Peru environment cooperation has leveraged the non-derogation and effective enforcement provisions in the trade agreement to strengthen the investigative arm within a newly established Ministry of Environment to verify compliance, improve environmental impact assessments and create an independent forestry oversight body that carries out regular audits of forestry concessions to combat illegal logging. Joint work between 2009 and 2013 has also included strengthening enforcement mechanisms, including **steeper fines and nullifying forestry concessions as a result of non-compliance**, as well as improved oversight of CITES export permits for big-leaf mahogany and Spanish cedar.

Of the USD 59 million allocated in total through the U.S. Agency for International Development and other partners, including the U.S. Forest Service to Peru, USD 49 million was allocated to environmental provisions in the U.S.–Peru Free Trade Agreement.

<sup>3</sup> See: <https://ustr.gov/trade-agreements/free-trade-agreements/korus-fta>

<sup>4</sup> See: <https://ustr.gov/trade-agreements/free-trade-agreements/peru-tpa/final-text>



The two examples illustrate the wide difference in environmental outcomes, based on a similar model. If NAFTA ends the side agreement and adopts a new model, it is important that a proactive environmental agreement moves ahead.

## Investment

The July 2017 USTR objectives are very cursory in relating to investment and have no explicit reference to the environment. In focusing on market access, the document advances the aim of establishing rules that “reduce or eliminate barriers to U.S. investment in all sectors in the NAFTA countries” (p. 9). This is a sweeping statement. The current market access provisions in NAFTA’s investment chapter are: (i) pre-establishment national treatment and (ii) the prohibition of performance requirements. There is a long list of exceptions to liberalization commitments—negotiations in this respect will not be easy. The United States itself has extensive exceptions. It is doubtful that other NAFTA parties would consider opening up further without the United States doing the same.

However, any negotiation on investment liberalization should include a consideration of related environmental impacts. Investors have already successfully challenged environment-related measures based on NAFTA provisions prohibiting performance requirements. Given the history of past Chapter 11 proceedings, NAFTA renegotiations would provide an opportunity to reassess the current NAFTA provisions on performance requirement prohibitions and parties’ ability to channel investment into sustainable development pathways while advancing economic, environmental and social objectives, including the clean energy transition.

The other investment-related objective stated in the USTR document is to “secure for U.S. investors in the NAFTA countries important rights consistent with U.S. legal principles and practice, while ensuring that NAFTA country investors in the United States are not accorded greater substantive rights than domestic investors” (p. 9). This statement raises a number of issues. Interestingly, it avoids referring to investment protection or any specific international standard. It reflects the desire to base the rights on U.S. principles rather than some autonomous standard developed by arbitral tribunals. This could open the door to a discussion on what NAFTA parties are actually trying to achieve through investment chapters in trade agreements and whether codified international approaches to investment protection are the right solution.

The statement relates to Canadian or Mexican investors investing in the United States and appears to respond to the critique, expressed throughout the TPP debate as well as the presidential campaign, that foreign investors in the United States are granted greater rights in comparison with national investors. One scholar interprets this<sup>5</sup> as the wish to limit investment provisions to non-discrimination and to move away from “absolute” standards of “fair and equitable treatment.” Whether this is what the U.S. administration has in mind, or if it imagines different standards applying to the United States on the one hand and the other NAFTA parties on the other, remains to be seen. The unease to have higher protections for foreign investors than domestic investors is a concern that was also raised in EU member states in the context of the trade negotiations between Canada and the EU. Discussions centered on the question why one environmental or other measure should lead to compensation for a foreign investor under the trade regime, but to no compensation for domestic actors in the same or similar situations.

Finally, the USTR document is conspicuously silent on investor–state dispute settlement (ISDS). If NAFTA countries were to respond to the biggest critique voiced with respect to the trade agreements in the United States and Europe, then scrapping the mechanism altogether (and relying on the state–state mechanism) would be the most direct response. Under “dispute settlement,” the document indeed appears to cover only the state–state mechanism. Whatever the actual intent behind the silence, any discussion on ISDS reform will be heated. Canada has already jumped on the bandwagon with the European Union to promote the creation of a more formalized investment court that would replace the private arbitration system, and discussions on investment dispute settlement will begin at the end of October 2017 at the United Nations. It is time to rethink the value and form of ISDS. NAFTA parties will not be able to ignore the winds of change in this area.

<sup>5</sup> See: <http://worldtradelaw.typepad.com/ielpblog/2017/07/the-new-calvo-doctrine-of-the-trump-administration-renegotiating-the-investment-chapter-of-nafta.html>



NAFTA parties could seize the opportunity and begin discussions around the creation of a more holistic mechanism on investment that would be less focused on formal adversarial dispute settlement and more on solution-finding and accountability. This could include setting up a dedicated mediation mechanism that would be capable of managing multi-party mediation processes (for example, including not only governments and investors but also affected local communities). In addition, to enhance environmental compliance through the private sector, NAFTA parties could discuss the creation of an accountability process similar to the ones set up at the International Finance Corporation. Such mechanisms could be permanent or in the form of a roster system.

## Procurement

The renegotiation of NAFTA offers the opportunity to strengthen the public procurement chapter to help position it as a tool for delivering on a low-carbon (or zero-carbon) innovation agenda. It is essential—and in line with international best practice—that this objective be included in the preamble to the chapter. It can also make reference to the Paris Agreement commitments, and the Sustainable Development Goals (SDGs), under which sustainable public procurement was already identified as a means to shift towards more sustainable consumption and production.

The July 2017 USTR objectives document takes a step in that direction: It calls for the establishment of “fair, transparent, predictable and non-discriminatory rules to govern government procurement in the NAFTA countries” (p. 15) and includes a reference to maintaining “the ability to provide for labor, environmental, and other criteria to be included in contracting requirements” (p. 16). However, for the rules to allow for green or sustainable public procurement, these criteria should also be allowed to be used in the technical specifications of the tender. NAFTA parties may want to look at the language included in Art X:2 of the World Trade Organization (WTO) *Agreement on Government Procurement*: “set out the technical specification in terms of performance and functional requirements, rather than design or descriptive characteristics; and base the technical specification on international standards, where such exist; otherwise, on national technical regulations, recognized national standards or building codes.”<sup>6</sup>

Similarly, as in the investment section, it is worth noting that the USTR objectives document calls for increased market access of U.S. firms in the public procurement markets of NAFTA countries, while it will exclude any coverage of public procurement on the U.S. sub-federal level. It thus remains to be seen to what extent the NAFTA parties will open up their procurement markets. An important part of public spending takes place at the sub-federal level. It is currently unclear what the real impact of the exclusion of sub-federal procurement will mean for sustainable development: on the one hand, sub-federal levels would be given sufficient flexibility to use public procurement as a lever for spending in the local economy and can help drive a local shift towards more sustainable, innovative and clean production. On the other hand, for clean innovation and technologies to be deployed across the globe, and for best value-for-money public spending, procurement agencies will need to outweigh the costs of spending locally. For example, this could include boosting the participation of domestic small and medium-sized enterprises in government contracts versus potentially cheaper options for goods and services, and infrastructure from abroad, as long as they meet the same quality, environmental and social standards. The NAFTA renegotiations on the public procurement chapter also offer an opportunity for renewed discussions on performance requirements of suppliers that bid for government contracts.

The devil, as always, will be in the details. The impact of a renewed chapter on government procurement will be dependent on which sectors and shares of public procurement will be opened for foreign suppliers, and on what grounds. Similarly, as with investment, opening the public procurement market should not lead to lower environmental or social standards among NAFTA parties, but should incorporate standards developed from the perspective of contributions to the SDGs, as we further elaborate below.

<sup>6</sup> WTO. (n.d.). *Agreement on Government Procurement*. Retrieved from [https://www.wto.org/english/tratop\\_e/gproc\\_e/gp\\_gpa\\_e.htm](https://www.wto.org/english/tratop_e/gproc_e/gp_gpa_e.htm)



Ultimately, for public procurement to shift to a strategic government function, it needs a clear legal framework that will reduce uncertainty for public procurement agencies to:

- Engage with suppliers in a transparent manner so that they can procure the best available technologies in the market
- Use specifications that refer to environmental and social criteria
- Award tenders beyond lowest price

The recent EU Public Procurement Directive (2014; effective 2016)<sup>7</sup> is regarded as best practice to elaborate on procurement procedures that can be used and under which circumstances: open competitions, restricted procedures, competitive procedures with negotiation or competitive dialogues. The directive was drafted to support the broader low-carbon innovation agenda of the EU and provides procedural certainty to achieve this goal. It also places the “Most Economically Advantageous Tender” principle at the core of the tender procedures. This allows for the movement away from awarding contracts based on lowest price, to best value-for-money across the life cycle of goods, services and infrastructure.

The NAFTA parties may wish to ensure that the procurement chapter allows for mechanisms such as framework contracts and specific set-asides for disadvantaged suppliers and to discuss how they can be best used to advance environmental, social and climate change goals.

## Non-Derogation and Enforcement

The USTR July 2017 NAFTA objectives report sets out several objectives related to non-derogation, including the support of enforceable domestic environmental regulations and the elaboration of rules to ensure that no derogation in environmental laws occurs as a result of action to attract trade and investment.<sup>8</sup>

Few countries pursue trade monitoring and enforcement as rigorously as the United States. It is estimated that in 2016 federal U.S. agencies spent USD 100 million and employed 700 full-time people to monitor and enforce U.S. international trade commitments.<sup>9</sup> Some portion of this enforcement oversight will presumably focus on environmental provisions, in addition to the usual list of trade irritants such as remedies and dumping, intellectual property, state-trading and pricing.

However, the new NAFTA will also be a test case as to how other countries will approach the Trump Administration’s stated position to gut domestic environmental laws, roll-back regulations across areas and sectors, and focus trade on repatriating jobs. In the short time that the Trump Administration has been in power, domestic environmental actions have comprised the rolling back or cutting various environmental regulations—notably the Clean Power Plan, the Clean Water Rule, loosening federal regulations on mercury emissions, proposing to slash federal environmental scientific research by half, as well as reducing the number of employees at the U.S. Environmental Protection Agency (EPA) by 40 per cent and its overall budget by one third.

Hence, the U.S. boilerplate language on non-derogation to be inserted in NAFTA takes place at a period when federal environmental leadership faces unparalleled retreat.

Interestingly, the USTR objectives relating to environment also seem to indicate that there is some willingness to strengthen the role of dispute settlement in environmental issues. The document proposes to “[e]stablish strong and enforceable environment obligations that are subject to the same dispute settlement mechanism that applies to other enforceable obligations of the Agreement” (p. 13). The effectiveness of this proposal would depend, of course, on what “enforceable” environmental obligations are actually agreed upon. Nevertheless, the stated objective responds

<sup>7</sup> See: <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32014L0024>

<sup>8</sup> “Establish strong and enforceable environment obligations that are subject to the same dispute settlement mechanism that applies to other enforceable obligations of the Agreement. Establish rules that will ensure that NAFTA countries do not waive or derogate from the protections afforded in their environmental laws for the purpose of encouraging trade or investment. Establish rules that will ensure that NAFTA countries do not fail to effectively enforce their environment laws through a sustained or recurring course of action or inaction, in a manner affecting trade or investment between the parties.” (p. 13)

<sup>9</sup> See: <https://www.gao.gov/products/GAO-17-399>



to a long-voiced critique of the current system, saying that while trade and investment provisions are enforceable, environmental provisions are not. Any discussion on environment-related dispute settlement and enforcement should also include a discussion on how to improve the current complaint mechanisms under NAFTA.

## Environmental Cooperation

### Protecting Nature

The only Multilateral Environmental Agreement (MEA) highlighted in the USTR objectives is CITES.

The U.S. has communicated varying references to wildlife-related issues in bilateral agreements. As noted above, many U.S. FTAs contain provisions related to combatting illegal logging and trade in illegal forest products. The USTR 2017 negotiation objectives propose NAFTA provisions to “Protect and conserve flora and fauna and ecosystems, including through action by countries to combat wildlife and timber trafficking” (p. 14). This is in line with the TPP, as well as the majority of U.S. bilateral trade agreements, include reference to forestry and actions to combat illegal harvesting and illegal timber trade. Drawing on the 2008 Lacey Act, provisions in different FTAs reference CITES to cover timber illegally harvested in other countries and imported to the United States. By contrast, CETA’s language goes further, by noting the environmental functions provided by forests, as well as the importance of supporting trade in sustainably managed forests.<sup>10</sup>

Fisheries are highlighted in the TPP and most other bilateral trade agreements, including an outline of different provisions for marine capture fisheries, such as combating illegal fishing, as well as reducing and eliminating fishing subsidies. The TPP language around fisheries provides a useful template for NAFTA, especially its references to regional management agreements and the importance of best-available evidence to monitor fish stocks. The USTR negotiation objectives signals the continued importance of these issues, noting the U.S. proposal to include NAFTA provisions to:

Combat illegal fishing, unreported, and unregulated (IUU) including by implementing port state measures and supporting increased monitoring and surveillance. Promote sustainable fisheries management and long-term conservation of marine species, including sharks, sea turtles, seabirds and marine mammals. (p. 14)

While the WTO tries again to come to a conclusion about fisheries subsidies at its Ministerial Conference in late 2017, too many missed deadlines at the WTO means that NAFTA should take up this issue with urgency and call for the elimination of fishing subsidies.

The TPP, as well as the majority of U.S. bilateral trade agreements, include, as noted in the U.S.–Peru FTA, reference to forestry and actions to combat illegal harvesting and illegal timber trade. Drawing on the 2008 Lacey Act, provisions in different FTAs reference CITES to cover timber illegally harvested in other countries and imported to the United States.

### Energy and Climate

As the Trump Administration announced its slashing of key U.S. EPA programs, it also noted its priority commitment to air and water quality, and ensuring the safety of chemicals in the workplace, as well as noting the importance of infrastructure (see section on procurement above).

The NAFTA objectives document is remarkably skinny when it comes to energy. This is surprising given the historic reforms in Mexico’s energy sector as well as the cross-border trade in energy:

Preserve and strengthen investment, market access, and state-owned enterprise disciplines benefitting energy production and transmission and support North American energy security and independence, while promoting continuing energy market-opening reforms. (p. 16)

<sup>10</sup> CETA, Chapter 24. Retrieved from <http://ec.europa.eu/trade/policy/in-focus/ceta/ceta-chapter-by-chapter/>



Given this singular focus on market access and pricing transparency, coupled with the Trump Administration's insistence on removing climate from the G7 and G20 communiqués and his exit from the Paris Agreement, inserting climate per se in NAFTA will be challenging. However, a new NAFTA without reference to clean energy solutions and trade would be a step backwards.

A starting point is thus the current TPP language (Art. 20.15<sup>11</sup>) with regards to the transition to a low-emission and resilient economy, leaving space by citing, at a higher level, ways to accelerate trade in clean or renewable energy technologies and services.

Other U.S. FTAs also include within the MEA sections reference to the Montreal Protocol on Substances that Deplete the Ozone Layer to reduce illegal trade in ozone-depleting substances. As one of the architects of the Montreal Protocol, the U.S. EPA estimates that millions of lives have been saved because of its implementation. In addition, the 2015 Kigali Amendment to the Montreal Protocol controlling production, consumption and trade in hydrofluorocarbons (HFCs) will have powerful climate-related effects.

To backstop its commitment to clean air, NAFTA should also include within the MEA section the Clean Air and Climate Coalition (CCAC) of which the United States, Canada and Mexico are members. In addition to supporting action on HFCs, the CCAC is supporting action to lower dirty pollutants from diesel and black carbon. Given that most NAFTA trade in goods is shipped by trucks, and an especially thorny NAFTA dispute involved Mexican trucks operating in the United States, highlighting the CCAC in the NAFTA as a common platform to tackle dirty diesel is welcome.

So too is referencing the MARPOL Agreement in NAFTA, as it is in the TPP, as a means to accelerate progress in reducing air and water pollution from marine ships.

## Environmental Goods and Services

The other way that NAFTA can link trade and a clean air/climate agenda is by including a section on Environmental Goods and Services. A good starting point is the Asia-Pacific Economic Cooperation (APEC) list of 54 environmental goods,<sup>12</sup> upon which the current WTO Environmental Goods Agreement is working to carve-out 300 tariff lines in such goods clusters as clean energy systems—solar cells, wind turbines, polysilicon materials—pollution control technologies, environmental monitoring systems and analysis, and various environmental services that extend beyond engineering and marketing to green financing.

## Standards

Finally, the USTR July 2017 press release announcing the NAFTA objectives notes that the U.S.:

negotiating objectives aim to apply the highest standards covering the broadest possible range of goods and services to ensure truly free and fair trade that supports higher-paying jobs and economic growth in the United States.<sup>13</sup>

Depending on what is meant by “highest standards,” and the reference to “fair trade” could mark a new beginning on discussions on standards from an environmental, climate and sustainability perspective. NAFTA should promote the highest standards across a range of goods and services. One way to think about a new generation of NAFTA standards is from the lens of the SDGs. The European Commission Trade Commissioner has repeated that the SDGs should be at the heart of Europe's trade policy, and that their evolving approach to the SDGs and trade is primarily through standards. Taking such an approach within NAFTA would avoid 20 years of frustration in some quarters of WTO jurisprudence around standards and hotly debated WTO dispute settlement findings related to the necessity, appropriateness and effectiveness of domestic standards.

<sup>11</sup> See: <https://ustr.gov/sites/default/files/TPP-Final-Text-Environment.pdf>

<sup>12</sup> See: the list here: [http://www.mofa.go.jp/policy/economy/apec/2012/pdfs/aelm\\_annex\\_c\\_en.pdf](http://www.mofa.go.jp/policy/economy/apec/2012/pdfs/aelm_annex_c_en.pdf)

<sup>13</sup> See: <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2017/july/ustr-releases-nafta-negotiating>



This could counterbalance some of the other USTR objectives relating to industrial goods, “good regulatory practices,” sanitary and phytosanitary measures (SPS) and technical barriers to trade (TBT). These objectives, by contrast, potentially reduce governments’ space to protect the environment and public health in that they aim at promoting “greater regulatory compatibility,” reducing burdens “associated with unnecessary differences in regulation,” requiring for measures to be “evidence-based” and “science-based,” or “avoiding unnecessary redundancies,” etc. (p. 4). These formulations could be understood to go well beyond what is required in the WTO agreements. In this respect, discussions about the new NAFTA should be careful not to undermine legitimate health and environmental protection measures that NAFTA parties wish to adopt based on their own acceptance of risk.



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### Head Office

111 Lombard Avenue, Suite 325  
Winnipeg, Manitoba  
Canada R3B 0T4

**Tel:** +1 (204) 958-7700

**Fax:** +1 (204) 958-7710

**Website:** [www.iisd.org](http://www.iisd.org)

**Twitter:** [@IISD\\_news](https://twitter.com/IISD_news)



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