Global Justice Now submission to the International Trade Committee inquiry on

Trade and the environment

February 2022

Introduction

1. Global Justice Now welcomes the opportunity to make a submission to the International Trade Committee in their inquiry on trade and the environment. Global Justice Now is a democratic social justice organisation working to create a more just and equal world.
2. Key points in this submission are:
   a. Currently there is little explicit alignment between the UK's trade and environmental policies, but the default effect tends to be for trade to override environmental policies. This needs to be reversed. We need to transform trade deals to be climate friendly.
   b. A carbon border adjustment mechanism could potentially make sense as one component of a much wider package for a climate transition, primarily made up of enabling and supportive measures. On its own however it is a punitive measure and there are serious concerns from a development perspective.
   c. We are seeing an increase in the use of ISDS by fossil fuel companies over climate related policies, and some countries have acknowledged that the risk from ISDS has prevented them from being more ambitious in their climate policy. ISDS clauses are incompatible with climate action and the UK should:
      i. not include ISDS clauses in new trade agreements
      ii. exit the Energy Charter Treaty
      iii. remove ISDS clauses from existing agreements.
   d. There is an opportunity for the UK to investigate strategic waiver of trade restrictions around technology transfer and intellectual property in order to springboard a green technological revolution globally. At the same time it is important to ensure that rhetoric around green trade is not used to impose forced opening of markets for trade and services in ways that undermine local economies and development, particularly in developing countries.

Alignment of trade agenda and environmental policies

3. Currently there does not seem to be much explicit coordination and alignment between the UK's trade agenda and the UK's environmental policies and its commitment to climate, biodiversity and other international goals. However the default effect tends to be for trade to override environmental policies. This needs to be reversed.
4. The UK's trade agenda is currently following a model and pattern of trade rules derived from earlier agreements – each new agreement tends to reuse much that was in earlier texts. These earlier texts were not designed with climate change and environmental objectives in mind – and indeed some of their provisions have been contributing factors in creating the climate crisis and environmental problems that we face.
5. There are therefore many areas of tension, some of them quite deeply embedded in the rules of the agreement. Where there is conflict between trade agreements and multilateral environmental agreements, including the climate treaty, experience shows that at present the trade rules usually win out. This is because trade rules have real, binding sanctions, whereas environmental agreements do not, but sadly also due to the continuing tendency for greater political weight and will to be given to narrow economic considerations rather than wider environmental and societal concerns.

6. Instead, our trade agenda needs to help us achieve our climate, environmental and social goals. It should be a tool for achieving them and not an end in itself.

7. Trade rules should comply with multilateral environmental agreements, climate goals, and environmental standards, as well as human rights and labour standards. This should be written in to the trade agreements themselves, and it should also be clear that if there is a conflict between, for instance, a trade agreement and a climate agreement, that trade rules are subordinate. This does not mean that the trade deal should have any role in defining the scope of these other areas of international law; simply that the rules should make reference to the various treaties and define that these prevail over trade rules.

8. The following points outline some of the areas of concern with the current pattern of trade rules:

   a. *Process and production methods:* limiting the ability to distinguish goods and services by the carbon impact of the way they were made or other sustainability criteria – for instance so that higher tariffs could be set on carbon intensive production.

   b. *Deregulatory pressure*: for the step change we need to tackle the climate crisis, we need strong, clear regulations setting boundaries and a common basis for engagement and strategically steering our economy and society into new directions. Many trade rules, by contrast will have a broad deregulatory effect, through the inclusion of necessity tests on regulations, through regulatory coherence processes, through giving preference to voluntary self-regulation, through pressure on standards and through enabling ISDS challenges.

   c. *Spread of climate technologies*: we need rapid adoption of climate technologies across the whole world – renewable energy, clean transport, building technologies, low carbon manufacturing, etc. Trade rules however often place limitations on the extent to which governments can take action to ensure technology transfer. Trade rules also often enforce inappropriate levels of intellectual property rules.

   d. *Levelling up*: in seeking to manage the climate transition, the government may wish to ensure that communities feel the benefit of green growth – that jobs lost in one sector are replaced by decent jobs in another, that currently deprived areas might be able to take advantage of growth sectors. Trade rules however often place limitations on governments ability to target using domestic content requirements or to give preference to domestic producers.

   e. *Investor state dispute settlement (see more below)*: all of the above are reinforced by ISDS clauses which enable foreign corporations to challenge the government on the basis of trade rules, including those affecting climate.

9. As the UK develops its independent trade policy in a time of climate crisis, we should be seeking to transform trade deals to be climate friendly, rather than further reinforcing the status quo and tying us into rules that hamper climate action.

Carbon border adjustment mechanisms

10. Carbon border adjustment mechanisms (CBAMs) are a complex issue. They may initially seem welcome from a climate perspective, but serious concerns have been raised from a development perspective by developing countries, and the evidence for the climate benefits is so far lacking.

11. The basic idea of a carbon border adjustment mechanism is to levy a charge on imports based upon their carbon level. The corollary is the assumption that there are already domestic carbon measures in place to do the same, and thus that an ‘adjustment’ on imports at the border is intended to level the playing field. The most concrete proposal for such a levy so far is that of the EU, although the idea has also been floated in various ways in discussions by the US, Japan and Canada.

12. The EU's CBAM proposal focuses on five sectors: cement, electricity, steel, aluminium and fertilisers. It is intended to be start in 2026 and be phased in up to 2035 and would be linked to the carbon price in the EU's Emissions Trading Scheme (ETC). There are exemptions for countries with equivalent carbon pricing schemes, but no automatic exemption for least developed countries (LDCs).

13. The most affected countries by these proposals are likely to include Turkey (cement, steel), Switzerland (electricity), Russia (electricity, steel, aluminium, fertilizers) and Norway (electricity, aluminium) when judged by the proportion of the EU's imports. The proposal is also likely to have an impact on several developing countries such as Mozambique, for whom the exports to the EU are of economic significance even though they do not make up a large proportion of the EU's own imports.

14. The most commonly cited arguments for CBAMs are:

    avoiding 'carbon leakage' where industry moves to other regions of the world with weaker environmental and climate standards

    maintaining competitiveness of domestic industry

    encouraging climate action in other countries

15. Carbon leakage however has often been a intentional strategy in recent decades, in which carbon emissions have been 'offshored' to developing countries, often by corporations still ultimately based in developed countries. This offshored production is driven by consumption in rich countries. A study has shown that while a CBAM might have some effect on leakage, overall it is only likely to cut 0.1% of global carbon emissions, at the cost of development impacts. It also seems likely that the cost of the tax will get passed down to the weakest players in the supply chain – often either consumers, workers or small-scale producers.

16. As a means of encouraging climate action, a CBAM is a punitive measure. It is extremely unfair that rich developed countries should seek to unilaterally impose punitive measures while simultaneously refusing to provide enabling measures and support. In particular, developed countries are failing to live up to their commitments on climate finance. They refuse to provide adequate funding for a climate transition away from carbon but then seek to impose penalties on countries that have not been able to make that transition yet.

17. A CBAM could make sense as one component of a much wider package for a climate transition, primarily made up of enabling and supportive measures. This could include:

    adequate climate finance for developing countries

    stronger climate mitigation measures at home

    technical assistance, capacity building, and expertise sharing programmes on mitigation, adaptation, loss and damage, response measures

    real and effective technology transfer programmes to help retrofit and jumpstart innovation

    a 'climate waiver' on trade rules and a 'peace clause' on WTO dispute settlement over cases involving climate related measures

    debt cancellation, freeing up resources to undertake climate action

    reform of international tax regimes

18. In such a context, a CBAM could have a role, but should include:

    exemptions for developing and least developed countries

    ring fencing revenues to be used for climate related measures – additional to current forms of climate finance

Investor state dispute settlement clauses

19. Investor state dispute settlement clauses in trade and investment agreements allow foreign corporations to sue governments outside of the national legal system. It takes the arbitration model common for commercial disputes, but applies it to a public policy setting, including

over climate goals and environmental policy. The amounts involved can often be far higher than would be the case in national courts.

20. Just in the past couple of years we have seen four energy companies launch investor state dispute settlement (ISDS) cases against governments over climate related policies:
Ascent Resources (UK registered) is suing Slovenia over fracking (June 2020)
RWE is suing the Netherlands over coal phase out (Feb 2021)
Uniper is also suing the Netherlands over coal phase out (April 2021)
TC Energy is suing the US over cancellation of the tar sands Keystone pipeline (Dec 2021)

21. These join previous cases of similar nature:
Lone Pine is suing Canada over a moratorium on fracking (2013)
Rockhopper is suing Italy over a ban on offshore oil drilling close to the coast (2017)

22. The speed at which these cases are arising is increasing. Industry analysts themselves predict that increased climate ambition of national emissions plans with reference to the Paris climate agreement will drive a rise in ISDS cases.[1]

23. The concept of stranded assets in relation to the climate energy transition refers to fossil fuel reserves and infrastructure that will need to be left in the ground and decommissioned if we are to have any chance of meeting climate targets. These assets have therefore lost some or all of their value and need to be written off. Mark Carney, then governor of the Bank of England, highlighted the risks in 2015.

24. ISDS cases however, provide a route for fossil fuel companies to try their luck at recouping some of those losses. An example is seen in the RWE and Uniper cases, where coal power stations are being phased out in the Netherlands by 2030. These plants were built when the science was already clear, so the companies should have been well aware of the risks they were taking. Nonetheless the Dutch government was offering compensation for the phaseout (€512m for RWE and €351m for Uniper). However this was not considered adequate by the companies and they are suing for €1.4bn and €1bn respectively under the Energy Charter Treaty. The Energy Charter Treaty is an investment agreement on the energy sector between over fifty countries, which includes ISDS.

25. Sometimes merely the threat of the existence of ISDS is enough for fossil fuel companies to get more money - it is not always even necessary for a case to be brought. As part of the German coal phaseout, two energy companies were awarded compensation that independent think tanks assess to be up to twelve times higher than would be normal. The German government has faced ISDS cases in the past and is thus very aware of the potential for such cases, and at the time Uniper was already threatening a case against the Netherlands. The German government got the energy companies (RWE again and LEAG) to sign a contract agreeing not to use the Energy Charter Treaty. The German Federal Ministry of Economics has acknowledged that the agreement to waive the use of ISDS played a 'role' in the high level of compensation.[2]

26. ISDS cases will therefore drive up the costs to governments and the public purse of the climate transition that is necessary to address the climate crisis. A recent editorial in the Financial Times and Bloomberg columnists have criticised this. As the FT piece says:

> "These governments — and their taxpayers — are thus being asked to bear all the risk associated with assets rendered less valuable or worthless by necessary climate action.

[1] Berkeley Research Group quoted by AFP, "Governments risk 'trillions' in fossil fuel climate litigation", France24, 11 Nov 2021, https://www.france24.com/en/live-news/20211112-governments-risk-trillions-in-fossil-fuel-climate-litigation

[2] "Wie Schiedsgerichte Europas Klimaziele bedrohen", *BuzzFeed News* 23 Feb 2021, https://www.buzzfeed.de/recherchen/energiecharta-vertrag-schiedsgerichte-europa-klimaziele-90214917.html in German. The relevant sentence is: ""Die Qualität und der Umfang des Rechtsbehelfsverzichts haben bei der Entschädigungsdiskussion sicherlich eine Rolle gespielt, sie waren jedoch nicht allein maßgeblich.", or translated "The quality and scope of the legal waiver certainly played a role in the compensation discussion, but they were not the only deciding factors."

> The prospect of "bailing out" fossil fuel projects risks disincentivising the steps needed now, from both markets and government, to secure swift decarbonisation."[3]

27. As the FT quote highlights, the danger is not just in the increased cost, it is also in the risk that in order to avoid those costs, governments do less, act more slowly or do not take action at all – a chilling effect. We are already too slow and too late in taking climate action. The world cannot afford more barriers that cause delay.

28. Recently governments have explicitly acknowledged that the threat of ISDS has prevented them from being more ambitious in their climate policy. New Zealand's climate change minister said the country did not join the Beyond Oil and Gas Initiative launched at COP26 because by doing so it "would have run afoul of investor-state settlements", and the Danish government set a climate target of 2050 rather than earlier in order to avoid "incredibly expensive" payments on stranded assets through ISDS.[4]

29. This is a chilling effect on the governments of developed countries. It is very likely that such chilling effect will be even stronger on the governments of developing countries, for whom even just the legal costs of fighting ISDS cases is a much higher proportion of limited government budgets, let alone the risk of losing a case and facing a requirement to pay billions.

30. ISDS clauses are incompatible with climate action and are a risk for the entire world. The UK should not include them in new trade agreements, should exit the Energy Charter Treaty and should remove such clauses from existing agreements.

Opportunities for 'green' goods and services exports

31. As noted above, we need rapid adoption of climate technologies across the whole world – renewable energy, clean transport, building technologies, low carbon manufacturing. Current trade rules however often place limitations on the extent to which governments can take action to ensure technology transfer. At present trade rules also often enforce inappropriate levels of intellectual property rules.

32. The economies of many developing countries have been trapped fossil fuel dependency. They are now being asked to transition to clean technologies, but may have to pay a exorbitant amounts to patent owners, mostly in rich countries, in order to do so. Recent announcements of climate finance to help countries transition may end up just lining the coffers of such corporations, while the climate transition is slowed.

33. Trade rules on intellectual property may also hamper innovation that is vital here in the UK as well as elsewhere in the world, by enabling companies to surround their products with patent 'thickets'. These are intended to stifle competition and maintain monopoly positions in markets and do nothing to support innovation.

34. There is an opportunity for the UK to investigate strategic waiver of trade restrictions around technology transfer and intellectual property in order to springboard a green technological revolution globally.

35. At the same time it is important to ensure that rhetoric around green trade is not used to impose forced opening of markets for trade and services in ways that undermine local economies and development, particularly in developing countries.

For more information, please contact Jean Blaylock.

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[3] Editorial board, "Governments should not foot the bill for stranded assets" *Financial Times*, 21 Feb 2022 https://www.ft.com/content/6e480f92-894a-494e-90ee-c60d20ce22f9

[4] Elizabeth Meager, "Cop26 targets pushed back under threat of being sued" *Capital Monitor* 14 Jan 2022, https://capitalmonitor.ai/institution/government/cop26-ambitions-at-risk-from-energy-charter-treaty-lawsuits/