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# INFLUENCING ENVIRONMENTAL CONDUCT INTERNATIONALLY: AN EXAMINATION OF OPTIONS

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**Influencing Environmental Conduct Internationally (Birchall Northey Review)** 1

**Introduction**

The 1992 Rio Conference on Environment and Development sought to place the global ecosystem alongside the "global village" in communications and the "global marketplace" in business. The post-Rio world has not seen the global ecosystem in these terms: while the global village and the global marketplace are regarded as positive developments, an affirmation of human technological ingenuity, the global ecosystem is regarded as a problem, a source of human limits. In this divergence, we have the source of the challenge to achieve sustainable development.

In recent years, the international community has identified a number of approaches to meeting this challenge. Some of these approaches involve traditional legal tools like legislation and regulation. The vast majority are not legal, in the sense of being enforceable in a court of law; instead, they work through consensus and cooperation. While government is the driving force for use of the traditional tools, business and non-governmental organizations are providing much of the leadership for the new options.

This paper is about the options actively being pursued in the international community. It starts with an examination of traditional approach - unilateral state action on international matters. Absent new international institutions, enforceable law is confined to the powers of individual countries and what they may do "extraterritorially" without creating controversy. The narrowness of the traditional approach leads naturally to consideration of other options. These options include use of financial incentives to improve public and private sector conduct, such as linking development assistance and export finance to environmental assessment. More recent innovations include international conventions that involve the business community in improving technologies (i.e., ozone depleting substances) and improving linkages between developed and developing countries (i.e., environmental offsets for air emissions). A further option that merits attention is the development of sectoral codes of conduct whereby, for example, the OECD has created guidelines for multinational enterprises.

It may be noted that virtually all of the more recent innovations have clear regard for the issue of competitiveness. This reflects the many recent studies which have examined competitiveness in relation to environmental regulation. In this age of the global marketplace, any initiative involving the private sector must be framed to take competitiveness into account.

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## PART I: UNILATERAL STATE ACTION TO INFLUENCE ENVIRONMENTAL CONDUCT INTERNATIONALLY

As discussed above, there is no sovereign body or adjudicator to decide upon international matters. Traditionally, states were not concerned with this absence as it left them with exclusive authority to deal unilaterally with matters within their boundaries. In more recent times, states have sought to push the domain of unilateral action outside their boundaries to meet modern concerns like the environment. This paper examines two types of unilateral state action that are designed to influence environmental conduct internationally: the 'carrot' and the 'stick'. The stick is unilateral state legislation with international application. The carrot is providing financial incentives to influence international conduct.

### A. APPLYING BINDING STANDARDS TO ENVIRONMENTAL CONDUCT INTERNATIONALLY

#### 1. Legality of Extraterritorial Legislation

In the past, international law applied strict limits on the ability of states to legislate extraterritorially. These limits were based on respect for both the sovereignty of states and the equality of states.

The respect for sovereignty was tied to the independent nature of states. It meant that each state had exclusive jurisdiction over its territory and the persons living in its territory. This principle of state sovereignty arose at a time when trade and travel were largely confined within a state's boundaries. Consequently, state sovereignty and jurisdiction corresponded directly to state territories and populations.

Corresponding to this right of each state to exercise jurisdiction over its territory and permanent population was the duty of each state to refrain from exercising jurisdiction over activities outside of its territory. This duty was based on the principle of the equality of states. Historically then, the international community was made up of a collection of sovereign states, each having exclusive jurisdiction over its territory and permanent population. The limits of each state's jurisdiction was in direct correlation to its physical territory.

In today's age of global communications and transportation, the principle of territorial jurisdiction no longer exists as a strict rule. States now recognize that there are certain circumstances in which both national and international interests are best served by allowing states to exercise jurisdiction outside of their territory.[1] For example, in certain situations, the

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[1] Maier, Harold, "Jurisdictional Rules in Customary International Law", in Meessen, Karl M. (ed.), *Extraterritorial Jurisdiction in Theory and Practice*, (London: Kluwer Law International Ltd, 1996), pp. 64-65.

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international community will recognize the right of a state to regulate the activities of its nationals abroad, or regulate foreign activities which pose a threat to its security.

Five principles now justify state extraterritorial actions:

> ***Territorial Principle***: The ability of a state to exercise jurisdiction over activities within its physical borders (although no longer the exclusive basis for the exercise of jurisdiction) is still the starting point at international law. Over time, the territorial principle has evolved to include not only activities conducted within a state's borders but also foreign activities which have "effects" within the state. This has come to be known as the "effects doctrine" and was first invoked by the United States in its anti-trust legislation to limit anti-competitive practices (i.e. price-fixing, cartel formation, etc.) in foreign countries with effects in the U.S. Now, most industrialized countries follow the U.S. approach.
>
> ***Nationality Principle***: This principle recognizes that states may have a right to exercise jurisdiction over the activities of their nationals abroad. An example would be a state taxing the extraterritorial income of its nationals.
>
> ***Security Principle***: This principle recognizes that governments may exercise jurisdiction over any person anywhere which affects state security. For example, the Canadian Government might seek to bring to trial (in Canada) a German citizen involved in the counterfeiting of Canadian currency in the basement of his home in Berlin.
>
> ***Passive Personality***: This principle refers to the nationality of the victim. For example, if an American citizen was murdered by a Dutch citizen anywhere in the world, the United States might argue that they should have jurisdiction over the criminal trial on the basis of the nationality of the victim.
>
> ***Universality Principle***: This principle supports governments around the world who take jurisdiction over the acts of non-nationals abroad that are universally condemned (e.g. genocide, piracy).

The ability of a state to link its extraterritorial actions to one of these principles does not necessarily make the extraterritorial action lawful. The territorial principle is, as stated above, still the starting point at international law. When a state relies upon one of the non-territorial jurisdictional principles to justify its extraterritorial actions, what often results is a conflict of jurisdiction. Thus, the oft-used phrase "extraterritoriality" is perhaps better explained by the

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term "jurisdictional conflict".

## 2. Analysis of a Jurisdictional Conflict

No hard and fast international law rules apply to jurisdictional conflicts. Rather, the legality and feasibility of exercising extraterritorial jurisdiction depends on a variety of factors and the particular circumstances of each case. The following summarizes some of the basic issues on determining whether applying environmental standards abroad is contrary to international law.

### (a) Relationship Between Jurisdictional Principles

Some international law experts take the view that jurisdictional principles follow a hierarchy, with the territorial principle taking precedence over the others, and perhaps the nationality principle being the second most-accepted principle by the international community.

By this view, the territoriality principle would be paramount in all instances. However, particular examples of jurisdictional conflict do not reflect such strong standing to this principle. For example, Study (1) [in the box below] saw the United States give way to the European

**Box 1**

**The *Soviet Gas Pipeline* case**

Through regulations passed in June of 1982, the U.S. Department of Commerce sought to prohibit the export of oil and gas equipment and technical data for use in the construction of a gas pipeline from the former Soviet Union to western Europe. The Regulations prohibited not only the direct export of such equipment and data from the United States, but also required persons "subject to the jurisdiction of the United States" to obtain re-export permits from the United States Office for Export Administration. Thus, the export controls were extended to the foreign subsidiaries of American multinational enterprises by reason of their ownership or control. The European Commission stated that the United States Regulations went beyond what was acceptable under international law on two grounds: (i) the Regulations violated the territorial principle of jurisdiction since they purported to regulate the activities of companies in the European Community that were not under the territorial jurisdiction of the United States; and (ii) there was no support for the Regulations based on the nationality principle since the Regulations sought to impose American nationality on companies contrary to the nationality of their incorporation and registered office.[2] The Regulations attracted widespread protest in Europe, with certain European States enacting "blocking statutes" requiring the subsidiaries to fulfill the terms of their contract. In November 1982, the United States rescinded its Regulations.

Community's territoriality argument. However, the case does not simply stand for the principle that territorial jurisdiction excludes all other exercises of jurisdiction. A number of other factors (including the intrusiveness of the American measures, the lack of a substantial connection to the

[2] These being the tests of corporate nationality accepted at international law: see *Barcelona Traction* case, ICJ Reports (1970).

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activity, the nature of the regulations, etc.) all worked to discourage the United States from maintaining its extraterritorial regulation.

The difficulty with applying a hierarchical conception of jurisdictional principles is that all jurisdictional conflicts involving the territory of one state would be resolved in favour of the territorial state. Yet the territorial principle is no longer exclusive; it is presumed to apply, but can be overcome in specific circumstances.

Thus, the more appropriate international law analysis involves undertaking a "balance of interests" type of analysis to consider the relevant factors in each case. In any balancing exercise, the "interests" at issue are those of each of the two states involved in the jurisdictional conflict, and the interests of the international community as regards such an exercise of jurisdiction. Thus, these conflicts involve national and international interests. The goal of any balancing exercise is to determine which side has a more substantial interest or connection with the activity sought to be regulated, and whether international interests would be served by permitting extraterritorial jurisdiction.

For example, were Canada to apply environmental standards to Canadian companies operating abroad, this would likely create a conflict between 'nationality' and 'territoriality'. The Canadian Government would be applying standards to foreign operations on the ground that the operator was Canadian[3], while the state in which such operations were being carried out would claiming that it had exclusive jurisdiction to apply its environmental standards since the operations were being carried out in its territory. Moving beyond these basic terms, the following factors would be relevant to determining the legality of any future standards:

- the level of intrusiveness of the Canadian environmental law in the foreign jurisdiction;
- the type of environmental law which is being applied;
- whether the law is in direct conflict with, or supplements, a law of the territorial state;
- the rationale for applying the environmental law abroad;
- whether an international minimum standard exists and must be complied with; and,
- the strength of the "nationality" connection.

***Level of Intrusiveness:*** Certain environmental laws will be viewed by states as very intrusive into the affairs of a foreign state. Often what makes an extraterritorial standard intrusive is how the standard gets enforced. For example, if a Canadian law sought to require its companies to obtain Canadian air and water emission permits for its overseas plants (rather than abide by

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[3] Whether or not a foreign operation is in fact "Canadian" may be a tricky question. The nationality of a corporation for the purposes of applying binding standards extraterritorially is discussed below.

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lower local standards), this would be considered as relatively intrusive since the local state might view its less stringent environmental standards as legitimate. However, certain environmental laws requiring environmental studies/assessments or environmental reporting obligations are not necessarily intrusive into another state's territory.

***Type of Environmental Law***: In certain sectors of activity, extraterritorial jurisdiction is more widely accepted. For instance, the exercise of extraterritorial jurisdiction in the field of anti-trust matters is commonplace.[4] The same could be said about tax jurisdiction, although the exercise of extraterritorial jurisdiction is usually carried out in accordance with a myriad of bilateral tax treaties. Certain "sub-sectors" of environmental law also appear to have some extra-territorial legitimacy - most notably, extraterritorial fisheries regulation. A recent example involved Canada extending its fisheries jurisdiction outside its territory [see box 2 below].

**Box 2**
**The *Estai* case**

In May 1994 and March 1995, the Canadian Government amended its *Coastal Fisheries Protection Act* and Coastal Fisheries Protection Regulations, respectively, to ban Portuguese and Spanish vessels from fishing for Greenland halibut (turbot) in international waters adjacent to Canadian waters (in an area under the quasi-regulatory authority of the parties to the North Atlantic Fisheries Convention (NAFC)). Six days after the passage of the Regulations, Canadian patrol ships boarded and seized a Spanish fishing vessel (the "*Estai*") in international waters. The European Union alleged that Canada's actions amounted to piracy because the *Estai* was in international waters. Canada argued that its extraterritorial actions were necessary to protect the dwindling stocks of turbot in Canadian waters. Because Greenland halibut straddles the boundary between Canadian and international waters, Canada sought to justify its exercise of extraterritorial jurisdiction on the basis of the "effects doctrine". In April 1995, Canadian and European Union negotiators concluded an agreement which established stricter enforcement measures for fishing within the NAFC Regulatory Area. Later that year, an international agreement (Agreement for the Implementation of the Provisions of the United Nations Convention of the Law of the Sea of 10 December 1982 Relating to the Conservation and Management of Straddling Fish Stocks and Highly Migratory Fish Stocks) was concluded which allowed for a more rigorous quota system and the boarding of foreign flag vessels in international waters upon suspicion of illegal fishing activity.

In addition to fisheries, some states also require environmental studies or assessments to be carried out as part of their bilateral overseas development assistance. The Canadian government might get some comfort out of these examples in exercising jurisdiction over its nationals abroad

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[4] Since the middle of this century, the United States has relied on the "effects" doctrine to apply its anti-trust laws abroad (i.e. prevention of cartel formation and price-fixing that raised the prices of goods imported into the United States). At the time when such measures were first used, they attracted widespread condemnation. However, most developed states now apply their anti-trust laws abroad for the same reasons. Not only are more states exercising such extraterritorial jurisdiction, but as the international community moves towards a more global, free-trading economic system, the interests of the international community are also said to be furthered by actions (extraterritorial or otherwise) to prohibit anti-competitive practices.

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in these particular fields.

***Conflicting or Supplementing Nature of Law***: Compliance by Canadian operations abroad with Canadian environmental laws will not normally result in Canadian operations being forced to breach a foreign law. This point was made fairly recently by a Japanese Court in a recent case [see Box 3 below].

**Box 3**

**The *Hokkaido* case**

In April 1992, the Sapporo High Court delivered a judgment which stated that a Japanese fisheries law (the Hokkaido Rule for Ocean Fisheries Adjustment) applied to the activities of Japanese fishers in any waters (i.e. not only the high seas but also the exclusive economic zone (EEZ) and territorial seas of other states). The President of a Japanese fishing and fish products corporation was charged with engaging in basket-fishing for crab in contravention of the Hokkaido Rule. The fishing activities at issue were all carried out in the territorial waters of the EEZ of the former Soviet Union, but adjacent to Japanese fishery zones. The Court stated:

> "[T]o prohibit a certain conduct by one's own nationals in such as the territorial sea of a foreign state does not in itself violate the State's sovereignty."

Certain foreign states might be persuaded that more stringent Canadian environmental standards supplement local requirements and do not conflict with them. In other cases, there may be no local standards at all, in which case it could be argued that no conflict exists.

***Rationale for Applying the Law Abroad***: A state may have a variety of reasons for wanting to apply its environmental laws abroad. For example, a state may seek extraterritorial legislation to prevent pollution inside its boundaries, the boundaries of neighbouring states or the global commons. The strongest example is when the environmental effects have the potential to spread back to the territory of the state seeking to exercise jurisdiction. For example, it does not seem so controversial to permit the United States to require American operations in Mexico's border region to abide by American environmental laws to minimize transboundary pollution which causes environmental impacts in south Texas. Equally, environmental effects on the global commons may authorize extraterritorial jurisdiction.

***Compliance With An International Minimum Standard***: To some extent, the application of Canadian environmental laws to Canadian companies operating abroad will depend upon whether certain international standards exist in the particular field being regulated, and whether the host state's environmental measures are in compliance with these international standards. As the body of substantive international environmental law grows, states will establish or alter their existing domestic environmental laws to bring them into conformity with international norms. Where a state does not have domestic environmental measures in conformity with international environmental law at a given time, it could be argued that Canada could legitimately seek to

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enforce the minimum required under international law,[5] if not its own standards.

***Strength of "Nationality" Connection***: The legality of an extraterritorial environmental standard may also depend upon the strength of the "nationality" connection. For example, where a Canadian company is a Crown corporation or otherwise acting on behalf of the Canadian Government, responsibility for breaches of international law on foreign territory can be attributed to the Canadian government. Consequently, the case for applying Canadian environmental standards to such corporations or activities is strengthened.

In considering the 'nationality' interest for extraterritorial environmental standards, the following distinctions will be relevant:

(i) whether the overseas operation is a foreign-incorporated subsidiary or merely a branch of a Canadian company;
(ii) whether the corporation is Canadian-controlled or otherwise in majority control of the board of directors ); or
(Iii) whether the operation has Canadian officers and directors who could be made subject to Canadian law based on their personal citizenship.[6]

To date, only the United States appears to have sought to enact and apply extraterritorial legislation to *foreign subsidiaries* of American companies on the basis of nationality, or ownership and control. The most notable example is the *Freuheuf* case [see Box 6 below].

**Box 6**

**The *Freuheuf* case**

In the 1960s, a dispute arose over provisions of the United States' *Trading with the Enemy Act* which sought to restrict trade with China. Fruehauf France SA was two-thirds owned and controlled by its American parent, Fruehauf International. The French subsidiary entered into a contract with another French company (Berliet) to supply trailers to be exported (along with Berliet's tractor units) to China. The US Treasury Department ordered the American parent to stop the sale, and this order was passed on to its French subsidiary. Berliet threatened to sue the French subsidiary and the three French directors of Fruehauf France SA (who were in a minority on the board of directors) applied to the French courts claiming abuse of rights by the American directors (whose decision was motivated by the fear of personal liability under American law). The Paris Court of Appeal agreed with the French directors and appointed a temporary administrator to oversee the performance of the contract. The US Treasury Department subsequently accepted the view of the Paris Court of Appeal and withdrew its order.

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[5] On this point also see the section on "International Conventions" below.

[6] Muchlinski, P.T., *Multinational Enterprises and the Law*, (Oxford: Blackwell Publishers Ltd., 1996), p. 124.

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Notwithstanding the *Freuheuf* case, the nationality of a foreign-incorporated subsidiary of a Canadian company may not be decisive. For instance, a court might recognize Canadian extraterritorial environmental legislation applying to a foreign subsidiary of a Canadian company if the company is simply manufacturing goods for Canadian consumption and doing so abroad in order to avoid Canadian environmental laws.

### (c) Conclusion

The legitimacy of Canada applying binding environmental standards abroad will depend upon the circumstances of each case. Where there is a conflict, the state with the territorial claim will start from the stronger position.[7] However, under certain circumstances, the international community may be tolerant, or even supportive, of applying binding environmental standards abroad.

## B. FINANCIAL INCENTIVES TO INFLUENCE ENVIRONMENTAL CONDUCT INTERNATIONALLY

Back in the 1960s, the United States was the first country to consider financial incentives as a major option for meeting environmental concerns. In 1969, the Nixon administration approved the *National Environmental Policy Act* (NEPA) to require an environmental impact statement prior to carrying out any 'major federal action' that would significantly affect the quality of the human environment. From the outset, major federal actions included financial assistance. In the early years, this approach focused on financial assistance for domestic activities. However, as a result of litigation and extensive congressional review, the Carter administration approved a special order to apply to all U.S. agencies operating internationally, including the U.S. Agency for International Development (USAID) and the Export-Import Bank (EXIM Bank).

The Carter approach was crafted with very careful regard to the issues of extraterritoriality and competitiveness. Both issues were subject to extensive congressional discussion with different committees producing conflicting recommendations. At the end of the day, the extraterritoriality issue was settled by ensuring that the Carter order applied to funding decisions by U.S. government officials, not to the projects that may receive funding. In other words, the U.S. did not apply its law to projects in other countries; it applied solely to U.S. decisions

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[7] This is confirmed by one of the key principles of international environmental law (Principle 21 of the Stockholm Convention/Principle 2 of the Rio Declaration) which states that: "States have, in accordance with the Charter of the United Nations and the principles of international law, the sovereign right to exploit their own resources pursuant to their own environmental policies, and the responsibility to ensure that their activities within their jurisdiction or control do not cause damage to the environment of other States or of areas beyond the limits of national jurisdiction."

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whether to provide any funding for such projects. To further limit the extraterritoriality issue, the Carter order made express provision to permit use of the environmental processes of other countries or international bodies as a substitute for U.S. requirements. Additionally, the Carter order made provision to exempt any decision from this order on the basis of foreign policy sensitivity. Consistent with these considerations, USAID developed a regulation which has been in place since 1978 without any noticeable domestic or international controversy.

Applying U.S. environmental assessment requirements to EXIM Bank raised additional concerns related to competitiveness. In particular, Congress was particularly concerned about applying standards to EXIM Bank that were not applied to similar organizations in other developed countries. These concerns were perhaps the main reason for the Carter order. After a lengthy debate and the initiation of legal proceedings (which did not go forward to any decision), Carter devised an order which relaxed some of the American domestic requirements for U.S. decision makers dealing with international matters. Under this approach, EXIM Bank agreed to establish environmental procedures for its export finance decisions. These were put in place in 1981 by regulation. More recently, EXIM Bank appears to have amended its procedures to establish a board of directors policy that requires environmental assessment before making funding commitments.

The NEPA approach has strongly influenced international development assistance and export financing. For example, virtually every developed country in the OECD has a policy of requiring some form of environmental assessment prior to making any significant development assistance decisions. Equally, the international development banks such as the World Bank have taken major steps over the past decade to carry out environmental assessments of funding decisions and reform internal procedures to bring environmental considerations forward at the earliest stages of decision-making.

Canada has also followed the U.S. lead in linking financial incentives to international activities. From 1974 to 1989, the federal Environmental Assessment and Review Process (EARP) provided a cabinet directive to all government departments providing financial assistance to any projects or other initiatives. In 1989, the cabinet directive was ruled legally binding through its embodiment in the *Environmental Assessment and Review Process Guidelines Order* (EARPGO). This ruling resulted in extensive litigation and ultimately led to the creation of the *Canadian Environmental Assessment Act* (CEAA) which was proclaimed in force in January 1995. The approach of CEAA has strong resemblance to the U.S. NEPA as it applies to federal decision-making, not to projects themselves. For federal funding decisions on projects outside Canada, the CEAA approach should minimize the issue of extraterritoriality.

A second related issue with CEAA funding incentives is their effect on competitiveness. To date, CEAA has not applied a blanket approach to Canadian decisions on international matters. In particular, the Export Development Corporation, which is a Canadian Crown corporation

equivalent to the EXIM Bank, has not been required to develop any environmental procedures.

As companies are finding greater interest in exploring markets in developing countries, the use of state financing to promote environmental assessment has ever greater significance. Thus, the U.S. NEPA has created an international consensus about the value of using government funding to ensure environmental assessment is carried out for development assistance. Equally, NEPA has also created an example of how governments may link more sensitive export finance funding to environmental assessment. Export finance requirements are likely to receive more attention in the coming years as the U.S. is actively seeking international consensus with other developed countries through the OECD.

## PART II: BILATERAL AND MULTILATERAL STATE ACTIONS TO INFLUENCE ENVIRONMENTAL CONDUCT INTERNATIONALLY

### 1. Bilateral Investment Treaties

BITs are agreements concluded between developed and developing countries to encourage companies from developed countries to invest in developing countries. BITs provide foreign companies with protection from state nationalization, and equal treatment vis-a-vis domestic companies. BITs emerged in the late 1970s after a number of less developed countries nationalized foreign company operations. Thus, BITs were pursued by developed countries seeking a stable investment environment for their companies operating abroad. The BIT were meant to address the uncertainties found in customary international law relating to transnational investment.[8]

Normally, a BIT will contain a most-favoured-nation ("MFN") clause, guaranteeing foreign companies at least as favourable treatment as any other foreign company. Some BITs will also include a national treatment clause, guaranteeing foreign companies at least as favourable treatment as domestic companies.

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[8] These include, *inter alia*: (a) whether a company has standing in international law to bring a claim against a host state for breach of an investment agreement; (b) whether the concept of permanent sovereignty over natural resources can form the legal basis for terminating an investment agreement entered into by a state with an company; (c) the basis for determining the quantum of compensation for assets which have been expropriated, nationalized or subjected to other means of property deprivation; (d) whether states have a right to offer diplomatic protection to investments made by their nationals in foreign states; and, (e) how disputes should be settled in relation to foreign company operations (i.e. local courts or international arbitration).

Typically, a BIT does not contain environmental standards. This is because the agreement is intended to create a level playing field. Nevertheless, it would appear to be open to Canada to conclude a BIT which (notwithstanding the MFN or national treatment clause) set out a minimum environmental standard for Canadian company operations in the host state. The policy considerations behind taking such an approach are whether a BIT including this provision would make Canadian foreign investment more attractive to the host country and whether it would limit Canadian companies from going abroad due to decreased profitability.

**2. Joint Implementation**

The United Nations Framework Convention on Climate Change introduced the concept of joint implementation (JI) as a way for states to reduce greenhouse gas emissions in a cost-effective manner. In its simplest form, a JI arrangement is one in which two or more states agree to jointly meet their environmental protection objectives in the most economically efficient manner. JI arrangements can take a variety of forms and operate to address a variety of different pollution problems.[9] For example, a JI project could involve the transfer of cleaner production technology to reduce greenhouse gas emissions or a reforestation or afforestation project to act as a greenhouse gas sink. JI arrangements can also vary according to the public/private mix of the project. At one extreme, a state could take the lead in seeking out and entering into JI arrangements. In such cases, the role of the private sector is limited to that of a technology supplier, or project consultant or contractor. At the other extreme, a state could take a hands-off approach, limiting their involvement to participating in the establishment of JI criteria. Equally, JI projects can be simple bilateral arrangements among two states or complex multilateral permit-trading schemes involving many private sector parties in a number of countries. This might work as follows: an energy-efficient state (State A) would enter into a JI arrangement with an energy-inefficient state (State B) whereby State A would provide some of its more efficient pollution control technology to State B in exchange for an emissions reduction "credit" equivalent to the amount of carbon reduced by the new technology. State A could apply this credit against its Climate Change Convention reduction requirements.[10]

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[9] For example, under the European Union's Protocol to the 1979 Convention on Long-Range Transboundary Air Pollution on Further Reduction of Sulphur Emissions, signed in Oslo on June 14, 1994, the signatory states to the Protocol to jointly meet their sulphur emission reduction targets with other signatory states.

[10] In the absence of any firm reduction requirements in the Climate Change Convention, the Parties to the Climate Change Convention decided at the first Conference of the Parties held in Berlin in April 1995, to establish a JI pilot phase to allow states to experiment with JI until the year 2000. Under the pilot phase, no credits will accrue to any state engaging in a JI project, but it is hoped that the experience and information acquired during the pilot phase will allow the Climate Change Convention to more accurately evaluate how much of a role JI can play in carbon emission reductions.

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The primary rationale for entering into a JI arrangement is cost effective environmental protection. However, other advantages which might flow from entering into a JI arrangement may vary significantly depending upon the specific JI arrangement entered into, and the nature of the entities entering into the JI arrangement.

For states entering into a JI arrangement, other advantages which might flow from JI include:[11]

- Re investor states (i.e., states transferring the technology or undertaking reforestation or afforestation projects abroad)

  In the case of a JI project involving technology transfer, the investor state can promote trade linkages with other states and assist investor state companies in establishing business relationships with like companies in foreign jurisdictions.

- Re host states (i.e., states receiving technology or hosting reforestation or afforestation projects abroad)

  In the case of a JI project involving technology transfer, the host state's benefits will be environmental (refitting local industry with cleaner technology), technological (the host state may be able to establish a "green technology" industry, especially where the host state and investor state are involved in co-development of technology for the JI project), economic (the host state is attracting foreign investment) and political (trade tensions may be reduced regarding products of the host state which have been turned away by states with more stringent environmental protection regimes).

Private sector companies may see other advantages to developing a JI arrangement:[12]

- Corporate Image: Engaging in JI projects which improve environmental conditions abroad may enhance the corporate image of the company from the investor state.

- Shaping Government Policy: Investor and host companies (i.e. companies of the host state) entering into JI arrangements may seek to demonstrate to their respective governments that a flexible regulatory regime involving JI (where companies are left to decide for themselves how best to meet certain standards) works better than specific

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[11] King, Richard J., "The Law and Practice of Joint Implementation" (1997), 6(1) *Review of European Community and International Environmental Law* 62 at 64.

[12] *Ibid.*

production process regulations.

- Business Relationships: Investor and host companies entering into JI arrangements will make business contacts with like companies in other jurisdictions.

- Experience with JI: Investor and host companies entering into JI arrangements under the Climate Change Convention pilot phase will gain valuable experience should a formal JI system be established under this Convention (or under other treaties).

### 3. Multilateral Codes of Conduct

Multinational codes of conduct were initiated to protect the economies of developing countries from dramatic actions of foreign company head offices, particularly when such actions were directed at the economic policies of developing country governments.

Most codes of conduct are classified as "guidelines" and are expressly stated to be "non-binding" or "voluntary."[13] Thus, these codes of conduct are not multilateral conventions which automatically become law as between the signatories.

There are perhaps four general codes worth noting: (i) the OECD Guidelines for Multinational Enterprises; (ii) the United Nations Draft Code of Conduct on Transnational Corporations; (iii) the International Labour Organization's ("ILO") Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy; and (iv) the World Bank Report to the Development Committee and Guidelines on the Treatment of Foreign Direct Investment. None of these contain detailed environmental standards. With respect to multilateral companies, the OECD Guidelines and the ILO Tripartite Declaration are similar, stating that:

> "Enterprises should take fully into account established general policy objectives of the Member countries in which they operate." (OECD)
>
> "Multinational enterprises should take fully into account established general policy objectives of the countries in which they operate." (ILO)

The United Nations Draft Code was never completed, as agreement could not be reached on its

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[13] For example, the OECD Guidelines for Multinational Enterprises - concluded among the OECD member States - expressly state that their observance is "voluntary and not legally enforceable." See Annex to the Declaration of June 21st, 1976 by Governments of OECD Member Countries on International Investment and Multinational Enterprises.

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provisions. Although no specific environmental provisions were included, its provisions are more detailed than those of the other codes. Its provisions on jurisdiction were particularly controversial and never reached final form in the Draft Code. Had the Draft Code ever been completed and adopted by the United Nations General Assembly, it would have carried more normative weight than any of the other codes, depending upon voting at the Assembly.

These codes of conduct and instruments of international organizations do not become part of the corpus of international law at their creation. However, they are multilateral declarations of international policy (often at the Ministerial level) and thus have more legal significance than simple unilateral acts of extraterritoriality. Over time, these codes (or more likely, certain provisions within these codes) have the ability to take on a normative character.

## PART III: RECOMMENDATIONS

**[Note to Draft: We will include this section once we have had an opportunity to discuss the recommendations with you.]**