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Workshop

International Institutions for Sustainability

Background and Expert Questions

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1 Project Background

The workshop “International Institutions for Sustainability” is part of a DIW research project on “Sustainability and Economics“, which is funded by the BMBF (German Federal Ministry of Education and Research). This survey project consists of several workshops on economic and related sciences approaches to sustainable development and a questionnaire on “Economics and Sustainable Development”. The first three workshops are “Intergenerational Justice and Sustainability” (15th & 16th May), “International Institutions for Sustainability” (12th & 13th June), and “Measuring Sustainability” (3rd & 4th July).

The project is motivated by the observation of a scientific divide in economics. One indicator of this divide is the fact that the concept of sustainable development is still being ignored by many mainstream neoclassical economists. As an alternative line of research the merger-movement of “Ecological Economics” has formed. It investigates various aspects of sustainability and consists of many different scientific approaches, joined by their frontiers with mainstream neoclassical economics. Also, in general, the theoretical and methodological contribution of economics to sustainable development (SD) seems to need further elaboration. The survey project thus aims to identify both, pressing research needs and promising lines of economic research. It also aims to identify concepts that may bridge the gap between economic approaches (e.g. evolutionary economics) and provide a multi-dimensional mindset to overcome the current constellation of “schools of thought”. The project is based on an integrative concept, which we have labelled “Sustainability Economics” (SE). The key features of the Sustainability Economics concept are:

- a) A comprehensive approach encompassing the ecological, economic and social dimensions of sustainability,
- b) the development of economic methods and concepts that deal with problems of sustainability,
- c) a strengthening of policy-orientated economic approaches for sustainability,
- d) an integration of sustainability concepts of general economics (such as sustainable finance) into the environmental economics SD debate,
- e) and an identification of “bridges” between different economic “schools of thoughts” by means of studying integration and disintegration processes in general science and exploring venues of interdisciplinary approaches.

2 Research Issues

The issues we highlight in this short paper should be regarded as starting points for two workshop sessions on "International Institutions for Sustainability" and for the discussion of the role of economics in sustainability research. In our first session, we focus on the global distributional conflicts between developing and developed economies, taking as an example the topics of trade and environment policies. The second session deals with selected issues of global governance.

2.1 Trade and Environment Issues: How to Overcome North-South Conflicts?

The first session will deal with the links between trade and environment issues and the role that institutions could play to overcome the underlying distributional conflicts. It will cover aspects of separation and integration of different policy areas up to the proposal of a single international institution, World Environment Organisation (WEO).

Both, environmental and trade policy issues have distributional dimensions on their own. Global conflicts can be observed e.g. over global pollution issues, over the sharing of environmental risks, or over the access to natural resources. Many developing countries argue that more global environmental protection could reduce their development potential– a prominent example is the allocation of emission rights under the Kyoto Protocol. Also, developing countries fear that environmental commitments in international environmental agreements would reduce their options for economic specialisation. Many of these countries heavily depend on resource-intensive exports, not least to pay for foreign debt. Since the Rio Summit in 1992 the concept of Ecological Debt has been coined – mainly by NGOs – in order to express the unequal distribution of environmental burden between North and South. According to this concept, a debt is built up by industrialised countries, first, because they purchase raw materials at prices which do not internalise global or national externalities and second, because they consume a disproportionately high share of global resources without compensating less developed countries (Martinez Alier 2003).

The liberalisation of trade is regarded by most nations as an important driving force for economic development. Again, there are asymmetries between developing and developed countries. Industrial countries tend to protect their markets (e.g. against imports of agricultural products, textiles and other resource-intensive goods), while asking developing countries to

liberalise. Negotiations on the latest WTO-liberalisation round, in Doha 2002, were successful only because it was labelled as a "development round" with special trade concessions for poor countries. It seems, that the distribution of the gains from trade between North and South is crucially dependent on the industrial countries' willingness to accept the structural changes free trade brings about at the national level.

The negotiations and agreements on international environmental protection and on free trade determine parts of the overall global institutional framework that contributes to sustainable development paths. Since the early 1990s the links between world-wide trade liberalisation and environmental quality as well as environmental policy, both at the national and international level, have been subject to fierce public debate and thorough analyses in mainstream economics (see Nordström/Vaughan 1999 for an overview). Following the 1992 Rio Summit, negotiations on global environmental issues have increased significantly. In parallel, the WTO was founded in 1995, replacing the General Agreement on Tariffs and Trade (GATT), and upgrading the international institutional setting for free trade as well as its enforcement. The current framework for negotiating environment and trade issues includes on the one hand, a global environmental policy regime - which in turn consists of a number of different Multilateral Environmental Agreements (MEAs), regional and bilateral agreements as well as the United Nations Environment Programme (UNEP) – and, on the other hand, the WTO.

Integration Versus Separation of Policy Areas

A crucial question for the future of institutional management and negotiations on trade and environment is whether there should be more integration or strict separation of these policy areas. Observing the current international negotiations and trade-and-environment conflicts, it is evident, that the WTO has a powerful dispute settlement mechanism which dominates all Multilateral Environmental Agreements (MEAs), because the latter lack a single global institutional body as well as sanction mechanisms. This leads to a ranking between the WTO and MEAs (except for the Cartagena Protocol (2000) in which signatories recognise that trade and environment should be mutually supportive). Without fundamental reforms the WTO will remain the dominant institution to settle disputes over trade and environment issues. This is even more important as for many developing countries the issues of trade, economic development and environmental policy are interrelated to a degree that

seems to make separate solutions impossible. Nevertheless, these countries reject attempts made by some industrial countries (e.g. the EU) to integrate to a larger degree environmental issues into WTO rules, not least because they suspect that international green policy instruments applied to traded goods – such as ecological labels or national standards on production methods – are simply disguised trade protection by industrialised countries.

Issue Linkage

Linking these issues in international negotiations seems appealing. It might help to overcome many trade and environment disputes in a framework of voluntary assent. Game theory is a powerful tool to study institutional arrangements among independent negotiators. Game theoretic models demonstrate that linking of issues in negotiations is a strategic choice which enables negotiators to enlarge their payoff space. Under specific assumptions countries would agree to co-operate on linked policies, while without linkage the dominant strategy, e.g. given the incentive structures in global environmental policy, would be non-cooperation (Finus 2001). A prominent example of a successful linkage between environment and trade issues is the Montreal Protocol (1989) on the depletion of the ozone layer. Two caveats, however, must be made. First, the Montreal Protocol trade sanctions were never actually used and second, substitutes for the pollutant CFC were readily available.

World Environment Organisation

The debate on international institutions for the management of trade and environment issues focuses on the dominant role of the WTO, the increasing number of separate MEAs and the lack of a single, powerful global environmental institution. This has led to new institutional proposals for the creation of a World Environment Organisation (WEO). Lodefalk/Whalley (2002) list 17 proposals made by individual authors (mainly economists and political scientists) as well as international organisations. For example Whalley/Zissimos (2002) argue that a WEO could provide a bargaining framework for trades and exchanges of commitments on various environmental issues such as biodiversity protection in return for cash, policy change and other considerations. They expect the WEO to finally evolve to a “global power broker” with other currently existing institutions realigning their activities. A WEO, according to these authors, could provide a less restrictive bargaining framework than the WTO currently does, not least as there should be no membership obligations. Instead, a WEO should concentrate on internalisation deals between countries.

Walley/Zissimos, however, acknowledge that a crucial issue with respect to developing countries is, whether such an institutional approach would increase or decrease their bargaining power compared to the current international regime (Biermann 2002).

Expert Questions

North-South Conflicts and Trade and Environment:

- **Do the economic and political links between trade and environment provide solutions for distributional conflicts or should there be strict separation in negotiating and managing these fields internationally?**
- **How can the institutional needs of developing countries in these fields be identified and included in institutional analyses?**
- **How can developing countries gain from international agreements (e.g. sharing rules, management of resources, mechanism design, technology transfer)?**
- **Would a World Environment Organisation help overcome North-South environmental conflicts??**
- **What could the analyses of links between trade and environment imply for other sustainability issues (e.g. social standards, technology transfer)?**
- **What role does economic research play in this debate and how could economic insights be implemented in policy-making?**

Research Agenda:

- **How would you define your contribution in this field of research?**
- **Which other contributions seem promising to you?**
- **Which topics would you suggest to discuss in a deeper and more specialised way after this workshop?**

2.2 A Regime for Global Sustainable Development Governance

The discussion of international regimes for sustainable development governance has become increasingly interdisciplinary, bringing together economics, political sciences and international law in the analysis of global governance issues. For this workshop the discussion needs to be focussed. Thus, this session will first address the current international institutional order – broadening the discussion in Session 1. The most pressing issue seems to be how the existing institutions (in a narrow definition, i.e. international organisations) could interact and co-operate effectively and how non-governmental stakeholders should be integrated in these processes. Taking a broader perspectives on the definition of institutions (e.g. as norms and practices), the second issue is the identification of new institutional concepts and tools for global sustainable governance. Last but not least, the political economic explanation of institutional failure will be addressed.

International Institutional Order

The current international organisations which dominate the institutional order are the United Nations Organisation and the Bretton Woods organisations (WTO, IMF, Worldbank). They have been subject to criticism and reform proposals and still lack behind in integrating and supporting the global development approach announced in Rio in 1992. Instead, especially the international organisations of the Bretton Woods system (IMF, Worldbank, WTO) still manifest North-South structures (e.g. stemming from colonial times) and have not been able to fully consider the social and ecological dimensions of sustainability in their practices. The United Nations Organisations and Programmes could not fill this “institutional gap”. On the contrary, the UNEP's role has weakened over the years, mainly because of lacking financial resources, but also because it has been promoting a large number of multilateral environmental agreements (MEAs), which handle specific global issues (climate, biodiversity, etc.) in their individual Secretariats. This makes coordination and co-operation of international environmental policy difficult.

Both, the integration of all sustainability dimensions in existing organisations or a new design of international institutions for sustainability would be a complex task. In addition, there is a clear ranking by national policy makers between the goals addressed by international institutions: institutions with economic goals (Bretton Woods, business and banking

systems) are being regarded as relatively more important than MEAs or, for example commitments on development aid or labour standards. Not least, current international organisations lack democratic mechanisms and are dominated by the most powerful economies, esp. the US (e.g. Moltke 2002, Gupta 2002, Deutscher Bundestag 2002).

National governments are the most important actors at the international level since international law and international rules are applied along the venues of national institutions. However, there is also an increasing number of non-governmental actors. The rise of non-governmental interest groups (coined as Civil Society) has led, both nationally and internationally, to the question how non-state stakeholders could be integrated in international policy processes (von Moltke 2002). To name just one example, NGOs have had a vital role in the debate over regulation of international investment (the failure of the Multilateral Investment Agreement (MAI) is a prominent example). NGOs have become an important actor at the international level, representing particular interest groups across national borders and putting pressure on governments and international negotiators to include environmental and social aspects in their negotiations.

Identification of Institutional Concepts and Tools

Institutions comprise not only national or international organisations. Institutions can be defined as norms and practices which build the basis for individual preferences and private as well as public organisations. Examples are legal concepts (e.g. property right, international customary law) and frameworks, national and international markets or traditional cultural rules. One important issue in the global governance debate is the process of increasing international business relations. Flexibility and mobility of private firms left national governments with fewer options to enforce their national economic and social rules to foreign direct investors, and the lack of global rules for international investment hampers also global environmental and social standards. The list of new institutional concepts and tools for a global regime for sustainable development is growing. It includes: new approaches to rule-making, incentive structures, participation, control and enforcement mechanisms, and tools like codes of conducts, public-private partnerships, international standards, assessment and rating agencies or indices (e.g. Loehman/Tusak 1998, Moltke 2002, Swanson 1999, 2002). A key issue is whether and how these new ideas could help to reach an international governance framework.

Explaining Institutional Failure

It seems most important for the discussion of global governance concepts to analyse and explain the underlying structures and incentive problems of international policy making. From a mainstream economic perspective, the incentive problems of international policy making and international institutions are at the core of explaining institutional failures (including market failure and policy failure). Negotiating and implementing international regimes face free-riding problems, ambiguous property rights, time inconsistency and contract enforcement problems (e.g. Swanson 2001, Whalley/Zissimos 2002). These problems determine whether countries and other stakeholders, first, are willing to engage in negotiations, and second, are willing to hold on to the commitments made. The analysis of transaction costs helps identifying the incentive aspects of alternative institutions (see e.g. Hurwicz 1998 for an overview on game theoretic and other microeconomic approaches). Hurwicz argues that there is room for creativity regarding the design of mechanisms to deal with the drawbacks of currently known policies, yet second-best solutions are unavoidable.

Political economy (PE) analyses deliver a number of explanations why markets do not allocate resources efficiently or why policy makers do not follow first-best economic policy options. Explanations are derived for the behaviour of voters, politicians, bureaucrats and interest groups. The neo-classical approach assumes that private instead of social benefit is being optimised by the actors. Point of departure is the homo economicus, who maximises his utility and acts in a rational and market-oriented manner (Fritsch et al. 1999). So far, the PE approach has mainly been used to address national policy-making. New approaches (beyond homo oeconomicus and beyond the national level) seem promising. The dominant neo-classical PE approach, for instance, does not include social, psychological, cultural and other aspects of human behaviour (e.g. learning) as determinants of institutional arrangements and their functioning. Ostrom (1998) has included such features in the analysis of environmental problems. She suggests an Institutional Analysis and Development approach, including rules, physical and material conditions, community attributes and incentives for individuals. Her main findings are, that neither market nor state institutions alone are sufficient to cope with the diversity of environmental problems. Successful institutional design has to take into account the interaction of rules with physical and biological attributes (Ostrom 1998, p. 84). Söderbaum (2000) questions the traditional assumption of rationality and optimising behaviour as being useful only for a subset of decision-making situations. Instead, he takes a

broader approach and defines a homo politicus (Political Economic Person) who cares also about her habits, lifestyles, history and irreversibilities.

Expert Questions

Global Sustainable Development Governance:

- **What are the global institutional needs for sustainable governance? How could the various global institutions governing specific policy topics interact and cooperate effectively and how should non-governmental stakeholders be integrated into these processes?**
- **How can the global development approach announced in Rio in 1992 be backed by a concise and appropriate international institutional order?**
- **What role should private and public actors play in an international institutional regime for sustainable development governance?**
- **How does economic research approach new institutional arrangements and tools (e.g. public/private partnerships, voluntary agreements)?**
- **What are the ecological economic approaches to international institutional design and management?**
- **What can political economic analysis contribute to the understanding of institutional constellations beyond national borders?**
- **How could economic insights made applicable in international policy and law?**

Research Agenda:

- **How would you define your contribution in this field of research?**
- **Which other contributions seem promising to you?**
- **Which topics would you suggest to discuss in a deeper and more specialised way after this workshop?**

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