

---

January 1998

## The Impact of Globalization on Sovereignty and the Environment

Stuart Smith

Follow this and additional works at: <https://scholarlycommons.law.case.edu/cuslj>

 Part of the [Transnational Law Commons](#)

---

### Recommended Citation

Stuart Smith, *The Impact of Globalization on Sovereignty and the Environment*, 24 Can.-U.S. L.J. 263 (1998)

Available at: <https://scholarlycommons.law.case.edu/cuslj/vol24/iss/37>

This Speech is brought to you for free and open access by the Student Journals at Case Western Reserve University School of Law Scholarly Commons. It has been accepted for inclusion in Canada-United States Law Journal by an authorized administrator of Case Western Reserve University School of Law Scholarly Commons.

## THE IMPACT OF GLOBALIZATION ON SOVEREIGNTY AND THE ENVIRONMENT

*Stuart Smith*\*

The discussion of globalization and its effect on sovereignty in the environment is one that is very close to the National Round Table of the Environment and the Economy, which I chair. The National Round Table consists of about two dozen people appointed by the Prime Minister, drawn from industry and non-governmental organizations with a sprinkling of academics and first nation representatives, and so on. What we try to do is arrive at a consensus where possible. But, more often, we arrive at a clear statement of what it is we are not agreeing about, and that is still pretty important.

At first, I wondered if that was the way to go, but when I saw the organization spending most of its time trying to reach a consensus but ending up wordsmithing to paper over cracks, I thought it was better to say ahead of time that we are going to agree on precisely the nature of our disagreement. The effect of that was to bring people a whole lot closer together than they otherwise would have been. A lot of disagreement is not really on the point; it is about the perceived motivation on the other side, and it is about distrust. Once you are able to leave aside the issue of distrust and perceived motivation and deal with the substance itself, it is very interesting how much closer you can arrive in the search for a consensus.

In any case, we have been working on a number of issues, and just last week we brought to a close a unique Canadian experience. We invited a random sample of people who received the Order of Canada, which is an honorary recognition in our country, to spend six days immersed in the topic of climate change. We brought in all the experts on all sides of the issue, skeptics and believers alike, and answered all their questions. They controlled the process, and we chaired it. And now they are going to issue a declaration to their fellow Canadians on what they believe their fellow Canadians would wish to do if all of them had that chance for a total immersion in the topic. This is the first time anybody has used the Order of Canada like that. It could be quite interesting. Anyway, I just wanted to tell you a little bit about the Round Table so you knew what I was doing nowadays, and to give you some

---

\* Stuart Smith is Chairman of the Board of Ensyn Technologies, Inc., based in Ottawa, Ontario. He holds an M.D. from McGill University.

idea why I am so bold as to say something on the topic of globalization and the environment.

From my point of view, the key factor in globalization is education. I believe that what happened was that education in low-wage areas permitted the movement of the means of production to areas where there is a good skill-to-wage ratio and a sufficient amount of management ability. Had it not been for the widespread availability of education, I do not think we would have seen the revolution that has marked the last couple of decades of this century. We would not have seen markets open the way that they have. Local infrastructure improvement, of course, is also important, but that has tended to parallel advances in education.

Everybody speaks of technology. You keep hearing that technology is the reason for globalization, but I do not believe that to be the case. Technology has had a few impacts, however. For one thing, it has impacted the movement of the production methods which I just described as moving to where the skills, relative to wages, were plentiful. Technology has become more mobile and more footloose. It has become more automated and easier to move. Communication technologies, which we hear about all the time, naturally allow easier financial movement and better management control at a distance. That is clearly a place where technology has had a role. In a peculiar way, the confidence of the former members of what used to be called the Atlantic monopoly has allowed markets to be opened. We became confident that we could find niches for ourselves in the higher value-added areas, most of which were technological, though some had nothing much to do with technology.

I would like to point out that globalization was also stimulated to some extent by large government borrowings. You may ask, how is that the case? As you well know, the Western nations had to borrow money from outside their own countries to finance government deficits. The Japanese, for example, were very willing to buy large amounts of that debt, and, for that matter, to do a lot of portfolio investment and even create factories in other parts of the world, including the United States. They were largely interested in keeping U.S. markets open because the rapidly developing countries of Asia depended entirely on having open markets into which they could sell. One of the reasons why we went along with it and allowed our markets to be opened was the fact that we needed that money to finance some of our various adventures at home.

In any event, we now have globalization of trade and investment moving ahead, and there is simply no end in sight. The market system has clearly swept aside everything before it. There are benefits to that. The most important benefit is higher average global prosperity. That is particularly true in the

newly industrializing countries, despite the recent economic upheaval in five of those nations in East and Southeast Asia. There is no question that the movement to the market economy throughout the world and the globalization of markets has led to the greatest good for the greatest number. The advanced countries have now been able to receive cheaper goods, and they have also had pressures to keep wages down. Of course, if you are a wage earner, that is not very good news. On the other hand, the fact that we have been able to have sustained growth without wage pressures has probably allowed us to miss what would otherwise have been a scheduled downturn in our economy.

We have had a period of almost unparalleled growth without an expected downturn and that has to be chalked up to the fact that we have not had any inflationary pressures. That, in turn, is due to the availability of cheaper goods and the pressure on our own companies and on our own workers to recognize their competitive situation with lower paid, attractive areas in other parts of the world. Now let us get a little closer to the topic that I am supposed to be dealing with, and that is the effect of sovereignty, particularly on the environment.

As you have heard from several other speakers, the real power of nation-states has been greatly diminished. In a sense, governments have been reduced to the position of what I call "bond salesmen," and to some extent, "real estate salesmen." They need to please investors, whose supply of loyalty is pretty close to zero. If you have to make sure that people are confident enough to buy your debt instruments on the international market, you do not have a heck of a lot of clout. You are suddenly put in the position of a supplicant going to somebody else and hoping they will buy what you have to sell.

This is where we have been. There has been a turnaround recently because, in both Canada and the United States, as well as in most countries in Western Europe, we have been getting on top of these deficits. The need to go out and borrow year after year may be a thing of the past. For a while, we were put in a position where our control over our own policies was pretty minimal, perhaps more so in Canada than in a powerful country like the United States. But, I think both our countries found themselves under some serious constraints due to having to play in the international financial market.

An interesting side-effect of globalization on weaker nation-states is that governments are obliged to enter larger blocks and to compete with one another to attract industry and investment. The weakness of central governments has also allowed nationalist sentiments in certain places like Scotland, Quebec, the Balkans, and others to flourish. The people ask themselves, if my central government is not able to control things and give me the kind of society I want, and if I have to join a larger block anyway, why do I have to

go through the central government that is not of my particular nationality and that I have never liked anyway? There is a significant increase in that type of nationalist sentiment within nation-states. In Britain, they are trying to deal with it by giving Scotland and Wales a certain devolution of power. We have a federal system in Canada that was supposed to deal with the matter, and I am confident that, in the long run, it will. But for the moment, as you know, we are going through some difficult times.

The most important consequence of all of this, the one that is really looming over the planet, is the fact that supranational government organizations cannot yet match the power of supranational firms. There simply is nothing on the horizon that indicates that we will be able to meet that challenge. Let me talk about that specifically with respect to standards and behavior dealing with the environment. But, everything I say for the environment could deal with anything else that is an externality from the point of view of the market system.

The market system regards the environment, ethics, labor practices, working conditions, and human rights as "externalities." There is no monetary value attached to those things. Consequently, the unparalleled growth and the now unopposed victory of the market system, (one which I applaud, by the way), has put in front of us a huge challenge of how to deal with these externalities.

Such externalities were previously dealt with, if at all, by individual governments who could set standards for human rights, for working conditions, for environmental protection, and so on. This has become very difficult, since companies are easily able to leap over any particular rule that a given country applies and use the threat, or the actual performance of taking their business elsewhere. The globalization of markets makes that fairly easy because these companies do not have to lose the market from which they are escaping or from which they are threatening to escape. The positive side of all this has been an upward pressure on these standards in countries that need to export to the industrialized world. So with respect to environment and working conditions, and, to a lesser extent, human rights and business ethics, these developing countries are trying to meet higher standards than they have met in the past; they are worried about being shut out of markets due to such factors as poor environmental performance.

On the positive side, there has been a rush into things like the International Standards Organization's (ISO) new ISO 14,000, a set of voluntary standards which are frankly much more popular in places in Southeast Asia than they are here. That is because it is seen as a ticket of entry into our market if companies in Southeast Asia can demonstrate that they have been given a stamp of approval by the ISO. Frankly, the one market they are wor-

ried about is the United States, which is probably the only country left that has the individual power – if they ever decide to use it – to really affect the future of individual companies by protecting markets based on environmental issues.

The negative side, of course, is the downward pressure on standards in the industrialized countries. We have to compete with these lower-wage countries where the regulations may not be very strong. Or, if they are there, they may not be enforced or taken very seriously.

The other thing to remember is that, in these other countries, businesses do not operate under the same conditions of peer and community pressure that they do in our own countries. If you ask me, the main reason that businesses will do what is right environmentally is that business people want to be respected by their fellow business people, by their communities, by their families, and by their neighbors. That sense of community and peer respect is very hard to transfer to a distant country in a different part of the world. It just does not stretch that far, at least in today's stage of human development. With what are we left? We are left with treaties that try to encourage countries to set and share standards to protect the environment. The United Nations Environment Program (UNEP), for example, has been promoting a treaty with regard to the movement of hazardous substances. What they are trying to do is to make it plain that, when you send a hazardous substance to a Third World country, you have to at least identify it. Even then, there is plenty of opposition to it. But it looks as though it is going to move ahead.

The Kyoto Convention<sup>1</sup> was an example of the world trying to put together an agreement on greenhouse gas emissions. As you know, it certainly is very far from a *fait accompli* at this point. The matter has not been ratified yet by any of the major governments, and, in the United States, it may not even come up for ratification for some time.

The most successful international treaty, I would argue, has been the Montreal Protocol to protect the ozone layer.<sup>2</sup> But, then again, it is a pretty defined, discrete area in which people are expected to act, with only a few manufacturers of the offending substance. It is nothing like the complex matter the greenhouse gases represent as a challenge to our societies. So we try with treaties, but there is only one body that has the power and influence to put teeth in any of these treaties, and that is the World Trade Organization (WTO).

---

<sup>1</sup> United Nations Framework Convention on Climate Change, Dec. 10, 1997, 37 I.L.M. 22 (1998).

<sup>2</sup> Montreal Protocol on Substances That Deplete the Ozone Layer, Sept. 16, 1987, 26 I.L.M. 1541 (1987).

The WTO, up until this point, has had no appetite for any such restrictions. They have viewed their job as getting rid of barriers to trade, and they have ruled accordingly in every single case that has come before them. For those of us concerned about such externalities as the environment, we are getting a little bit discouraged because we would like to see a slightly more even-handed approach on the part of the WTO. They have made their point that they are not going to brook any excuses for blocking off markets to trade and for using discriminatory measures. I do believe that there are a couple of babies that have gone out with some of the bath water, and that the WTO does have to start to take these other matters more seriously.

The WTO made a recent decision about bovine hormones.<sup>3</sup> I do not know if you have been following that. It is an esoteric issue. This was an issue where Europeans had put up completely unjustifiable trade barriers, allegedly on the basis of health, to imports of Canadian and American beef. The Europeans were totally wrong on that issue, as far as I am concerned. The dispute resolution mechanism ruled the same way. At the same time, they did say that, if you want to make a case before the WTO on health, there are certain things you have to do. That is the first time they have actually come out and shown people a way that they could make a case before the WTO. Admittedly, it is based on health, not on the environment. But, at least it is a start. It is better than just simply saying, if you are closing your market, you are wrong, do not bother us. I see that as the first move. We should keep an eye on that. We need clear environmental rules and people will have to bring more environment cases before the WTO before we can settle all this.

I am hoping that, with the movement to market-based mechanisms for encouraging environmental protection, the WTO will either be forced to take a stand on those measures, or a new body will have to be set up that will handle them. Let us speak for a moment about the most important market-based mechanism, tradable emissions permits. President Clinton has put before the world community the idea that we should deal with greenhouse gases not by working against the market, but by getting the market to work with us. He proposes setting a value on being clean, setting a value on reducing emissions, and then allowing companies and countries to trade among themselves. Those values, in the form of permits, will have a tradable value on an exchange.

We think that is a terrifically important concept. It will be discussed in Buenos Aires late this fall. In order to set that up globally, there will have to be a central mechanism to control the accounting and the exchange of those permits. That central mechanism could well grow ultimately, in my way of

---

<sup>3</sup> *E.C. - Measures Concerning Meat and Meat Products (Hormones)*, WT/DS48/AB/R (Jan. 16, 1998).

thinking, into the kind of international body that might be able to apply serious sanctions with respect to environmental performance. The WTO may ignore that, but I would not be surprised to see an eventual merging of those two bodies. The sanctions that would then be applied to people who do not play by the rules of the permit trading game would be trade sanctions agreed upon and enforced by the WTO. That is the best hope we have in the near future of arriving at a solution to this problem. We can think globally, but at the moment, we can only act locally. If you want to deal with the environment, you have got to think globally, and you have got to act globally.

People recognize the victory of market forces and are trying now to work with them, rather than against them. We have consumer boycotts. We have an effort being made to introduce tradable permits, which work for greenhouse gases and could work in many other areas as well. We have eco-efficiency indicators. We at the Round Table are doing some of that. The notion is that companies will be able to report to their consumers, to their suppliers, to their shareholders, and to their boards of directors on their environmental performance.

We are trying to develop standardized indicators that are very robust and will hold up from industry to industry. These will indicate such things as what percentage of the material that comes into a plant goes out as waste and how much goes out as product. That is an indicator which companies could ultimately report on their balance sheet. Similarly, the amount of energy consumed per unit of production is another such indicator that can find its way onto balance sheets. Ten large companies in the United States and Canada are now testing the feasibility of these indicators. We are working with the World Business Council on Sustainable Development to some extent on that.

There have been several studies recently, including one in the *Harvard Business Review*, which have compared the better performing companies environmentally with the poorer performing companies within a given sector, be it the chemical sector, petroleum sector, and certain other sectors.<sup>4</sup> It has been found that the so-called clean companies have outperformed the so-called dirty companies by a factor between 2.25% and 4.0% annually. So, that is at least 2.25 basis points a year of outperformance by the clean companies. This is not necessarily because they are saving a whole lot of money by being clean, although they may be; it is probably because the kind of management people who worry about these things, who anticipate the future with respect to the need to be environmentally conscious, also do other things right. They probably give more consideration to human resources, customer needs, market position, and so on.

---

<sup>4</sup> Dun Grifford, Jr., *The Value of Going Green*, HARV. BUS. REV., Sept. 1997, at 11.

There is a general belief out there now that clean performance enhances shareholder value, even if only as a marker for good management. A lot of mutual funds now take advantage of that. So again, the idea is to work with the market to encourage people to be environmentally responsible rather than trying to work against the market by imposing fines or sanctions.

In summary, the globalization of markets has certainly had an impact on the ability of nation-states to control externalities including environmental performance. What we see now is a movement to market-based instruments like tradable permits, consumer pressures, and investor pressures seeking shareholder value. These are taking the place of what used to be a command-and-control attempt to deal with these issues. In the long run, I still hope we will have a world organization that can apply sanctions on behalf of such issues as the environment and human rights. We are not there yet, but perhaps by moving toward tradable permits to the greenhouse gas issues, we are taking a step closer. We should open a dialogue with the WTO and encourage it to slightly dilute its general approach which has been in favor of opening markets at all costs. Markets have won. Thank goodness for that. Now, we have got to deal with the consequences of that victory.