

North American Climate Change Regulation and Economic Integration



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Will there be an integrated North American carbon regime?



- Probably not. Countries need to adjust their own programs to appease domestic constituencies and will not agree to give up sovereignty over their own climate policies.
- The United States will set its climate policy unilaterally, and Canada will likely create a system comparable to that of the US.
- There might be some allowance trading between the United States and Canada. Mexico will probably be linked to the North American regime through offsets, not allowances.

US Regulation: What Is on the Table?

• **House of Representatives**

- Waxman-Markey: American Clean Energy and Security Act (ACESA), H.R. 2454. Has passed the House.

• **Senate**

- Kerry-Boxer: Clean Energy Jobs and American Power Act (CEJAPA), S. 1733. Passed the Environment and Public Works Committee, but has since stalled.
- Cantwell-Collins: Carbon Limits and Energy for America's Renewal (CLEAR) Act. Originally received little attention in the Senate, but Kerry-Graham-Lieberman bill will reportedly use some ideas from this bill.
- Kerry-Graham-Lieberman: Forthcoming.
- Bingaman: American Clean Energy Leadership Act (ACELA). Passed the Energy and Natural Resources Committee.

US Federal Regulation: Implications for North American Cooperation and Trade

• **Competitiveness provisions**

- Rebates for trade-intensive, energy-intensive industries: Begin in 2012 in Waxman-Markey.
 - ✦ Issued on a product-output basis; cover 100 percent of costs.
 - ✦ Does this create perverse incentives?
- International reserve allowance program: Could begin in 2020 depending on international efforts to reduce emissions.
 - ✦ Imposed against imports from countries that fail to take comparable action on climate change.
 - ✦ Have already provoked international outrage.

US Federal Regulation: Implications for North American Cooperation and Trade



- In order for US firms to use allowances from foreign countries, the foreign country must have a national or international carbon trading regime that imposes mandatory absolute greenhouse gas emissions limits on one or more sectors and is at least as stringent as that of the United States.
 - Canada will comply only if it adopts absolute rather than intensity-based targets.

US Federal Regulation: Implications for North American Cooperation and Trade



- **Renewable energy**
 - It is still unclear whether electricity exported across borders can count as eligible renewable energy under Waxman-Markey's renewable portfolio standard.
 - Hydroelectricity exported from Canada to the US will subtract from a utility's generation baseline, making it easier for utilities to meet the renewable portfolio standard.

US Regulation: Implications for North American Cooperation and Trade

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- If Congress does not act, the EPA is obligated to step in and regulate.
- Proposed EPA rule will require large facilities to adopt the best available GHG emissions reduction technology when their facilities are constructed or upgraded.
 - Would cover about 400 new facilities and modifications per year.
- Sectors with a high degree of intra-industry trade between the United States and Canada that are likely to be required to obtain permits under the program include paper, petrochemicals, basic organic and inorganic chemicals, plastics, resins, iron, and steel.

State and Regional Initiatives: Implications for North American Cooperation and Trade

- **Regional cap-and-trade programs:**
 - RGGI: In place now. Members: Connecticut, Delaware, Maine, Maryland, Massachusetts, New Hampshire, New Jersey, New York, Rhode Island, Vermont.
 - WCI: Scheduled to begin auctions in 2012. Members: British Columbia, Manitoba, Quebec, Ontario, Arizona, California, Montana, New Mexico, Oregon, Utah, Washington.
- **There is uncertainty surrounding the future of existing state-provincial cap-and-trade compacts.**
 - Under current US cap-and-trade legislation, state cap-and-trade programs will be preempted.
 - It is yet unclear how the disbanding of the multi-jurisdictional carbon trading systems will affect carbon markets in participating Canadian provinces.

State and Regional Initiatives: Implications for North American Cooperation and Trade



• Renewable Portfolio Standards

- To date, 30 states have enacted a patchwork of different renewable portfolio standards, all containing different targets, timelines, and definitions of renewable energy. Ontario, New Brunswick, and Nova Scotia also have renewable standards.
- Definitions of renewable energy could be a point of contention going forward, particularly where large hydro is concerned.
- Many states allow renewable energy credits (RECs) to be traded cross-border, but the tracking systems that certify and manage these credits are highly regionalized and uncoordinated, posing a *de facto* barrier to REC trade.

State and Regional Initiatives: Implications for North American Cooperation and Trade



• Low-Carbon Fuels Standards

- Developed by California; others including Ontario, British Columbia, and the RGGI region have indicated an intention to adopt the standard.
- Requires fuel distributors to reduce the carbon intensity of fuels by 10 percent between 2010 and 2020.
- Oil sands production generates 15-20% more GHG emissions on a well-to-wheel basis than conventional oil, putting it at a disadvantage under the standard.
- Canadian oil sands crude will find other markets in the Gulf Coast and Asia, but widespread adoption of the standard – particularly in the Midwest - would deal a blow to the industry.
- Is the standard WTO/NAFTA legal?

A New NAFTA “Overlay” for Energy and Climate Change



- **Use the Commission for Environmental Cooperation (CEC) as a clearinghouse for climate change-related data..**
 - Expansion of database on North American emissions.
 - Reporting on new climate initiatives and regulations in each country.
 - Clearinghouse for monitoring, reporting, and verification (MRV) of carbon credits issued under national or regional carbon regimes.

A New NAFTA “Overlay” for Energy and Climate Change



- **Standardize definitions of renewable energy and coordinate renewable energy policies.**
 - Both Canada and the United States should agree on how imported electricity – particularly hydro - should be credited and certified under renewable portfolio standards. Border states and provinces should continue to work toward zero-carbon energy generation through existing regional institutions.

A New NAFTA “Overlay” for Energy and Climate Change

- **Adopt a NAFTA peace clause.**
 - “Carbon protectionism” in the near term is likely to be emulated or provoke retaliation in other countries.
 - A framework needs to be developed under the WTO to handle competitiveness concerns that are not addressed through international climate negotiations.
 - A temporary “peace clause” suspending border measures for a limited time should be incorporated into climate legislation in order to encourage WTO negotiating efforts.
 - Liberalization of environmental goods and services should be given higher priority in the Doha negotiations.

A New NAFTA “Overlay” for Energy and Climate Change

- **Establish a “safe harbor” to shield climate change taxes and regulations from claims under the indirect takings provisions of NAFTA Chapter 11.**
 - Chapter 11 requires governments to provide compensation to investors for measures that are “tantamount to expropriation.”
 - To date, Chapter 11 cases have assumed a limited scope for environmental laws’ constituting expropriation – but climate change laws will have unprecedented economic effects.
 - If not clarified, Chapter 11 could provoke regulatory chill and adversely affect trade and investment flows in the region.