

THE KYOTO PROTOCOL REVISITED

A RESPONSIBLE AND DYNAMIC ALTERNATIVE FOR CANADA

A strategy prepared by the
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THE NEED TO REVISIT THE KYOTO PROTOCOL

The enhancement of the environment in Canada and the world and the attainment of improved standards of living for Canadians and global citizens are cornerstones of the mandate of the Canadian Council of Chief Executives.

The Council's serious reservations about the Kyoto Protocol derive from a deeply held conviction that the Protocol as presently constituted will do little to achieve urgently needed global environmental enhancement, and that it will undermine Canada's ability to meet its social and economic priorities.

This paper outlines the reasons for our reservations about the Kyoto Protocol and our response to the federal government's recent discussion paper, *Canada's Contribution to Addressing Climate Change*. More importantly, our paper explains why Canadians can achieve far more both nationally and globally by adopting a responsible and dynamic alternative to the Kyoto Protocol.

OUR CONCERNS ABOUT THE KYOTO PROTOCOL

Five years after negotiation of the Protocol, it has become clear that it represents an unachievable target for Canada, for the following reasons:

-The size of the challenge is insurmountable. While Canada's commitment would require a reduction in emissions from the 1990 baseline, the country's total emissions have in fact continued to grow, fueled by economic growth, higher exports and increases in population. Indeed the gap between the target and the federal government's own forecast of emissions on a business-as-usual basis is some 240 million tonnes of CO₂ equivalent annually. Achieving the target would require a 30 percent decrease in emissions in a very short time (six to ten years) and would present an insurmountable challenge for a country with an energy-intensive economy, a cold climate, large transportation distances and a population that continues to grow through immigration. With no breakthrough technologies on

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the horizon that have an early, broad-based applicability, this essentially represents a limit on the size of the Canadian economy.

-The Protocol flies in the face of continental realities and Canada's competitiveness globally. Canada's most important economic partner has declared the Kyoto Protocol "fatally flawed" and has chosen to follow a uniquely American response to the global climate change challenge. Should Canada ratify the Kyoto Protocol and follow a course widely divergent from that of the United States, the costs to Canadians would be far more severe than Canada might have anticipated when it signed the Protocol. Given the extent of Canada's dependence on energy-intensive exports and of its integration with the United States economy, ratification would have an immediate and significant impact on its competitive position relative to the United States and on its ability to attract investment and to maintain and create jobs in enterprises serving continental and global markets. On a broader basis, Canada would be the only country in its hemisphere to accept emission limits. As well, Canadian firms would be placed at a disadvantage relative to competitors in Asia, Eastern Europe and the oil-producing nations of OPEC, none of which would face the same constraints.

-The Protocol is ineffective as a global strategy. At the same time that the Protocol would impose significant costs, it will do very little to slow the global build-up of greenhouse gases. With the withdrawal of the United States, and the lack of any reduction obligations on the part of developing countries, the Protocol would cover at best one-third of current global emissions.

-Canada's contribution to global reductions is not fully recognized. Some of Canada's exports to the United States of hydroelectricity and natural gas have the potential to replace more GHG-intensive fuels in that country, and yet under the structure of the Protocol there is no credit for Canada's contribution to lowering global emissions. This is unacceptable.

-The scale and timing of the Kyoto Protocol commitment would require significant changes in consumer behaviour. More than 80 percent of the greenhouse gas emissions associated with fossil fuels

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come from the end-use consumption of energy. Yet the nature of the challenge still has not been properly explained to Canadians nor have they been informed of how they would be affected. Other countries, for example, have demonstrated a variety of strategies for reducing emissions from transportation. These include fuel taxes, road tolls and alternate-day driving restrictions. Whatever path Canada chooses, chopping overall emissions by 30 percent is sure to disrupt significantly the day-to-day lives of Canadians in many ways as well as increasing the cost of goods and services.

-Investment, credit ratings and the currency will be hit hard. Canadian companies already are coping with the challenges of an economic downturn, a relatively small capital market and global overcapacity in key industries such as steel, petrochemicals, oil, automobiles and forest products. Any commitment to emission targets that creates uncertainty about the ability of Canadian-based companies to grow will have an immediate impact on investor perceptions of risk. A signal that Canada has consciously limited its growth prospects will persuade both foreign and domestic companies to shift planned capital investments to other countries and risks a further outflow of head offices from Canada. Credit ratings will suffer and the cost of capital for Canadian enterprises will rise. These factors could trigger a damaging decline in the value of the Canadian dollar.

-Adherence to the Protocol will undermine key social priorities. Largely due to immigration, Canada is one of the few industrialized countries whose population is growing. Because the Kyoto Protocol target is expressed as a cap on total rather than per capita emissions, Canada might be forced to reduce flows of immigration in order to meet its commitment. Pursuit of the Kyoto objective would also restrict further development of Canada's substantial energy and resource endowment, thereby constraining economic opportunities for aboriginal peoples and for those in economically disadvantaged regions of the country. Canada's energy sector is the largest single source of new capital investment, a significant contributor to export earnings and a major source of tax revenue.

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-A focus on costly cuts to emissions in the short term could divert resources from more effective approaches that would have greater long-term impact. Real progress must be global and can only be made over several decades through the adoption of new generations of technology and the development of widely available and cost-effective forms of low or non-carbon energy.

We acknowledge that governments and businesses alike make decisions every day based on imperfect information. But in considering how far to go in imposing real costs on businesses, consumers and taxpayers, Canada must take into account the degree of uncertainty that still surrounds the science of climate change. As Professor Richard Lindzen of the Massachusetts Institute of Technology, one of the world's foremost climate change authorities, puts it: "We are not in a position to confidently attribute past climate change to CO₂ or to forecast what the climate will be in the future.... We simply do not know what relation, if any, exists between global climate changes and water vapour, clouds, storms, hurricanes and other factors."

On the other hand, there is broad scientific consensus that the Kyoto Protocol will have very limited impact on the global growth of greenhouse gas emissions. This leads to another question, the extent to which limited resources should be allocated to emissions reduction rather than to measures to mitigate and adapt to the impacts of climate change.

The above factors all suggest a fundamental re-examination of Canada's approach to the issue of global climate change. The recent federal discussion paper, entitled *Canada's Contribution to Addressing Climate Change*, despite its noble intentions does little to change this assessment. Most of the options it lays out do not even meet the government's own criteria for an acceptable plan. Nor are these options consistent with the recently released federal Innovation Strategy. To achieve a more prosperous and environmentally sustainable future for Canadians, it is essential to get all the federal policy signals moving in the same direction.

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The federal discussion paper falls short on a number of fronts:

-It tries to downplay the real size of the challenge imposed by the Kyoto Protocol target - an unprecedented 30 percent reduction in emissions in less than 10 years. This is done in part by means of a number of questionable assumptions, including the size of reductions to be achieved through existing government measures, and the federal government's claim for up to 70 megatonnes of credits for Canada's "clean energy exports".

-The discussion paper suggests a long list of possible "targeted measures" by governments. It recognizes that even such costly measures cannot by themselves ensure achievement of the Kyoto Protocol target. While government policy can create a framework and provide incentives, emissions will not be reduced until Canadian consumers, businesses and institutions actually make the necessary investments. The discussion paper provides neither an estimate of how many people and companies would respond to its targeted measures, nor of the total public and private investment required.

-The paper lays out a bevy of potential spending programs and tax increases that would undo much of the progress that has been made in restoring fiscal balance in Canada.

-The various schemes of emissions trading contemplated all would raise costs for Canadian firms beyond those of their major competitors and penalize even highly efficient enterprises.

What then should Canada's approach be to this challenging issue, both domestically and globally? Canada need not take a back seat to any country when it comes to protecting the environment. Last year, for instance, Canada was ranked fourth globally on the World Economic Forum's Environmental Sustainability Index. Our country has a responsibility to show leadership on the climate change issue. We want to ensure that this role is fulfilled on the basis of real goals and lasting accomplishments, not vague goals and paper achievements. In light of

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the many problems with the Kyoto Protocol, Canada's approach to the climate change issue must reflect maximum prudence and common sense. *This is not, however, an excuse for inaction.*

The Canadian Council of Chief Executives (formerly the Business Council on National Issues) was the first national business organization to endorse vigorous industry action aimed at curtailing greenhouse gas emissions and promoting energy efficiency as an essential element of company and country competitiveness. *The Council's commitment to national and global environmental goals goes well beyond the issue of global climate change. We believe that the promotion of clean air, clean water and sustainability must be key components of Canada's economic, social and developmental agenda. This requires casting off the shackles of the Kyoto Protocol in favour of a broader, more innovative and demonstrably more constructive agenda that will bring benefits to Canadians and to citizens around the world.*

We do not pretend to have all the answers at this stage, nor do we wish to preempt what must become a frank and inclusive national discussion. What we offer here is simply a framework of principles and action items that we hope will be seen as a constructive contribution to the shaping of a positive climate change strategy for Canadians.

A MADE-IN-CANADA CLIMATE CHANGE STRATEGY

Objective: *A strategy that combines responsible action to address greenhouse gas emissions with policies that enhance the country's quality of life and economic competitiveness as well as its ability to play a leadership role in devising a longer-term global solution to the risk of serious climate change.*

The development of a made-in-Canada strategy on climate change should be guided by the following principles:

-Public engagement. The first step must be meaningful engagement of the Canadian public. Before proceeding further,

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Canada needs to establish a solid consensus on what is appropriate and achievable for Canada, what performance targets the country should set for itself, what policy choices and behavioural changes will be needed to meet those targets, what costs the public is prepared to pay and how progress will be monitored.

-Balance and equity. Canada's strategy must be balanced and equitable. Whatever targets for action we adopt as a country, no sector or region should bear an undue share of the burden.

-Short- and long-term action. An effective strategy must both include prudent and cost-effective action in the near term and contribute to lasting solutions over the longer term. For instance, Canadian-led fuel cell technology offers great promise, but cannot possibly contribute meaningfully to reducing Canadian emissions within the Kyoto Protocol timeframe.

-Overall societal benefits. Rather than a strategy focused solely on greenhouse gases, Canada must fashion an approach that maximizes environmental, health and social benefits domestically, and that contributes to broader economic and environmental progress internationally. In particular, domestic policies should focus on improving important indicators of quality of life such as air quality in urban regions.

-North American integration. Continental economic integration and shared environmental space require a coherent approach to reducing emissions on a North American basis. Canada can play a leadership role among its continental partners in forging a more innovative and sensible North American response.

-Economic competitiveness and growth. Global leadership in any field flows from economic strength. To ensure that Canadian governments and enterprises maintain their capacity to develop and deploy innovative emission-reducing technologies, it is essential to foster a sustainable business environment that encourages economic growth and leads to more jobs, rising personal incomes and a stronger tax base.

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-Global champions. The strategy must strengthen Canada as a base for innovative and competitive global champions that can create economic advantage at home while also developing technologies and practices that contribute to global environmental solutions.

Canadian action to deal with climate change must be broadly based, engage governments, industry and citizens in meaningful actions and ensure maximum benefit for each dollar expended. The most important elements of a Canadian action plan are:

1. Public involvement and education. Meaningful progress in understanding and managing the risks of climate change is not possible without broadly based public support and a willingness to act. Such a strategy requires:

- A common understanding of the issue of climate change and the potential effectiveness of alternative approaches;
- A meaningful public debate about the most effective policies, what the necessary measures will cost and who will pay the price;
- A longer-term and much expanded public education campaign on responsible citizen action, similar to the one that built broad support for the fight against government deficits in the 1990s;
- Development of indicators to measure citizen engagement and progress on issues of environmental sustainability;
- A committed business community that can contribute through employee information and support of public education and action programs.

2. Strategic investment in the development and adoption of energy-efficient technologies. In order to change behaviour and reduce emissions of greenhouse gases, governments will have to devote a much larger share of their resources to environmental purposes. These resources should be targeted to areas where Canada has a particular advantage and partnered with industry wherever possible. Governments could:

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- Increase public investment in research in potential breakthrough technologies in a wide range of energy sources, which offer the potential to dramatically reduce global greenhouse gas emissions;
- Increase the share of renewable energy and lower emitting technologies by offering tax credits or other incentives;
- Offer an accelerated capital cost allowance for business investment in advanced technologies and emissions-reducing machinery and equipment;
- Support further development of fuel cell technologies and the refueling infrastructure;
- Provide additional incentives and innovative financing for energy retrofits of buildings;
- Adopt a national building code with strong energy efficiency criteria;
- Expand energy audit programs for houses, commercial buildings and public facilities;
- Set new energy efficiency standards for appliances;
- Enhance support for research and development in clean coal and hydrogen technologies;
- Reduce the fiscal and regulatory barriers to greater use of co-generation in industrial plants;
- Intensify research into and demonstration of carbon dioxide capture and storage; and
- Expand Canada's world-leading efforts in carbon sequestration through measures such as tax incentives for reforestation; improved Crown forest land management; restoration of marginal land with tree-planting, shelter belts and green spaces; and tax incentives and education to improve agricultural practices with respect to carbon retention in soils.

3. A stronger commitment by industry. While energy use by consumers has continued to grow rapidly, Canadian industry has

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made very significant progress in improving energy efficiency, enhancing both its competitiveness and its ability to contribute to lasting technology-based solutions. Emissions from the mining and manufacturing industries overall already have been stabilized at 1990 levels, despite production increases of 35 percent, which represents an improvement in emissions intensity of 1.4 percent annually. As well, technology improvements in the oilsands industry are expected to yield a 45 percent decline in GHG emissions per barrel of oil from 1990 levels. Industry-government partnerships in programs such as the Canadian Industry Program for Energy Conservation (CIPEC) and the Voluntary Challenge and Registry (VCR) have resulted in enhanced performance and reporting of emissions. Nonetheless, businesses need to remain focused on investigating new technologies and other opportunities to continue to reduce emissions per unit of output.

-Agreements entered into between government and industry sectors can set appropriate performance goals and monitor performance. In order to encourage the growth of globally competitive firms, these goals should focus on lowering the emissions intensity of production. In addition, such agreements would need to recognize the rate of capital stock turnover and technology development, as well as the nature of the resource base and production processes in different sectors.

-Companies should make energy efficiency a standard benchmark of corporate competitiveness.

-Companies should strengthen their focus on continuous improvement in product and process design, recycling and management of materials through their lifecycle, and examine opportunities to lower the carbon intensity of their operations.

-Smaller and medium sized enterprises lag significantly in the development and adoption of innovative technologies. Larger companies therefore have an opportunity to demonstrate leadership within the private sector by encouraging adherence to voluntary codes and sharing best practices and information programs on energy management.

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4. A Canadian program on science and adaptation. Canada should advocate internationally and carry out domestically a balanced approach of research, mitigation and adaptation. The Kyoto Protocol will make no significant difference to the global growth of greenhouse gas emissions, especially as long as the United States remains outside. A responsible strategy, therefore, must include measures to prepare for the potential impacts of climate change.

-Canada can contribute to improving the world's scientific understanding of the climate system and the extent of human influence on the climate.

-Canadian research priorities should include the potential impact on the Arctic, the Great Lakes and fragile ecosystems, as well as effects on agriculture, forestry and resource development.

-Canada can also participate in the global effort to develop strategies for managing and adapting to the longer-term risks of climate change, particularly for vulnerable regions and people in developing countries.

-Canadian industry should contribute resources and expertise to this research effort.

5. Inter-governmental collaboration in transportation and urban design. The transportation sector in particular is a large and growing source of emissions and must be a focus of any effective strategy to reduce Canadian emissions:

-Federal, provincial and municipal governments must coordinate policies to enhance transportation systems and urban design, reduce traffic congestion and improve air quality in the country's most heavily populated regions.

-Significant additional investment in urban and inter-city public transit will require federal as well as provincial and municipal participation.

-Vehicle fuel efficiency standards should remain harmonized on a North American basis as they continue to evolve.

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6. Action at the community level. There are a number of opportunities to integrate climate change actions with local efforts to revitalize communities. Among other things, municipal governments could:

- Set targets for reductions in per capita GHG emissions;
- Enhance land-use planning;
- Investigate community energy planning and green power purchasing, with an aim to ensure such purchases optimize results for taxpayer dollars;
- Accelerate the capture of landfill gas for use in electricity;
- Improve management of municipal solid waste, including diversion from landfill;
- Improve municipal water and sewage infrastructure.

7. A fiscal and business environment that encourages energy-efficient growth.

-Far-reaching measures to reduce emissions inevitably will constrain the growth of Canada's energy-intensive economy. These measures therefore must be offset by determined efforts to improve Canada's tax and regulatory regimes and ensure robust business investment and job creation.

-The potentially substantial new public investments in areas such as research, renewable energy and public transit will require difficult choices among fiscal alternatives. However, an effective *made-in-Canada* climate change strategy should not add to the overall share of government in the economy. Higher spending on environmental measures may reduce the ability of governments to address growing needs in other areas such as health care and education. The test of their commitment to addressing climate change lies in the trade-offs that must be made between competing priorities.

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-Incentives to stimulate new investment must be carefully designed to ensure efficient attainment of program objectives and effective use of public resources.

8. Canadian leadership internationally. A *made-in-Canada* approach would also demonstrate leadership in developing a truly global strategy for managing climate change.

-While continuously improving its own emissions performance, Canada's international development strategy should focus on helping developing countries to increase economic growth while becoming more efficient in energy use, so that they can be part of the global effort to reduce emissions over the long term. Bringing major emitters such as China and India and the key energy-exporting members of OPEC into the global effort to reduce emissions would do far more for the global climate than any measures Canada could hope to make within its own borders.

-Reducing emissions will have an impact only over the very long term. Investment in alternative priorities such as the alleviation of poverty, provision of clean water and improvement of health care would have a much greater impact in meeting the broader goal of improving the quality of life of the world's poorest people. Meeting these objectives could advance the world to a position of greater economic strength from which it would be better able to address global issues such as climate change.

-Canada should address climate change issues as an essential element in its strategy for managing North American integration. Economic integration imposes some real constraints on Canadian policy choices, but also offers important opportunities and points of leverage. In particular, energy security remains a priority for the United States within the context of increased integration with Canada and Mexico. This provides an opening for Canadian leadership within North America that could lead to a more comprehensive, innovative and sensible response on climate change through a coherent continental approach.

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Canada can play a leadership role in managing the transition to a more sustainable future both at home and abroad, but only if we have a “made-in-Canada” strategy that has broad public support and reinforces the creative energies of our governments, our enterprises and our citizens.