

The Federal Regulatory Framework for Greenhouse Gases and other air emissions: a “rewarmed” issue?

In accordance with its announcement in its Notice of Intent published on October 21, 2006¹, the federal government, on April 26, published the regulatory framework it favours for greenhouse gases emissions and other air pollutants.

The “Regulatory Framework for Air Emissions”, despite its title, is not a restrictive regulation. For the time being, it is only a document that outlines draft sectorial regulations, the first of which is scheduled for republication in spring 2008, unless an election puts it off to an even later date!

The federal government’s regulatory framework seeks to identify short, medium and long-term reduction targets for industrial atmospheric emissions, establish regulatory and non-regulatory actions in relation to transportation, consumer and commercial products, and determine a regulatory framework for improvement of indoor air quality.

This newsletter closely examines each of these measures.

A. The regulatory framework for industrial atmospheric emissions

Industrial atmospheric emissions include greenhouse gases (GHG) and air pollutants such as nitrogen oxides (NO_x), sulphur oxides (SO_x), volatile organic compounds (VOC), particulate matter (PM), benzene and mercury. The industrial sectors concerned are electricity generation by combustion, oil and gas, the forest industry (including pulp and paper and wood products), smelting and refining, including aluminum, alumina and base metal smelting, iron and steel, iron ore pelletizing, potash, part of the mining sector, and cement, lime and chemical production, including fertilizers. In these key sectors, the regulations should translate into emission reductions adding up to 60 megatonnes (Mt) by 2020, relative to their level in 2006.

By H  l  ne Lauzon



Here is the initial framework the federal government proposes for reduction of greenhouse gases emissions.

Greenhouse gases

In the short term, the government is pursuing the objective of stopping the growth of greenhouse gases between 2010 and 2020. In the medium term, it would reduce them by 20% or 150 Mt by 2020 and, in the long term, it would lower them up to 70% by 2050. To achieve these goals, it proposes to implement reduction “targets”, starting in 2010, initially established in terms of intensity, and not in absolute terms. Emission intensity is the GHG cap set for each unit of production. Thus, the targets established in

terms of emission intensity are linked to production, while a reduction in absolute terms constitutes a total reduction of emissions. The base year to establish these reduction targets, in terms of emission intensity, becomes 2006, and not 2003, as the Notice of Intent had indicated. A notice then will be issued under section 71 of the *Canadian Environmental Protection Act*² (hereinafter “CEPA”) to gather 2006 data that will be used to establish emission reduction targets.

Emission reduction targets

Different targets would be established depending on whether they concern an existing facility or a new facility, that is, a facility for which the first year of operation is 2004 or later.

For existing facilities, a target would be established based on an improvement of 6% per year from 2007 to 2010 or 18% in 2010 relative to the emission intensity level that existed in 2006. Subsequently, from 2010 to 2015, the target would be an emission intensity reduction of 2% per year, thus resulting in a 26% reduction in GHG emission intensity by 2015.

New facilities would benefit from a three-year grace period and, commencing in the fourth year, the targets would be based on the clean fuel standards while seeking an improvement of 2% per subsequent year up to 2020.

¹ Notice of intent to develop and implement regulations and other measures to reduce greenhouse gas emissions, (2006) 140 Gaz. Can. 13350, page 3357.

² S.C. 1999, c. 33.



Compliance mechanisms

The government proposes various measures that will allow the companies affected by the regulations to comply with their reduction obligations. These measures are also called “compliance mechanisms”.

Apart from the emission reduction attributable to various abatement actions, such as deployment of technology or energy efficiency measures, it would be possible for a company to comply with part of its GHG emission reduction obligations by contributing to a technology fund, which would make it possible to fund investments in technologies and infrastructure likely to result in rapid GHG emission reductions. The contributions would be established at a rate of \$15 per tonne of carbon dioxide equivalent for the years 2010 to 2012 and \$20 per tonne for 2013. Subsequently, the contribution rate would increase each year according to the growth of nominal GDP. However, contributions to the Fund would be capped, starting in 2010, at 70% of the total reductions. This percentage would diminish gradually up to 2018, when companies would not longer be authorized to contribute to this Fund³. Through the technology Fund, it would also be possible, for the period from 2010 to 2017, to finance research and develop projects up to a limit of 5 Mt per year, or obtain credits for investments in special projects. We should note that provincial funds in compliance with the federal Fund could be recognized as equivalent.

A company could also achieve its emission reduction objectives by resorting to the emissions trading system, that is, by acquiring credits through a free market, such as a stock exchange. It could also resort to the national offset credit system following (verified) emission reductions occurring outside the regulated activities. It could also obtain “Kyoto units” through the Kyoto Protocol’s Clean Development Mechanism, by carrying out a project in a developing country. In this last case, however, a cap of 10% of the total target would be set. The government is also

considering, for the first time, the possibility of establishing links with other emissions trading systems, such as the *Western Regional Climate Action Initiative* and the *Regional Greenhouse Gas Initiative* in the United States, or with other systems eventually put in place, without excluding the Mexican and European markets in the longer term.

Several companies will be delighted to learn that the government intends to recognize the “early actions” taken between 1992 and 2006, but up to a limit of 15 Mt of carbon dioxide equivalent for the entire industry, including a maximum of 5 Mt per year.

Let us now look at the government approach regarding atmospheric pollutants.

Atmospheric pollutants

The government objective for air pollutants is to set emission reduction targets in relation to the 2006 base year. These measures would result in a 55% reduction of air pollution emissions present in the environment due to smog and acid rain. National caps and sector-specific caps will be established.

Emission reduction targets

For the national caps, the emission reduction targets envisioned are 40% for nitrogen oxides, or a cap of 600 kilotonnes (kt), 55% for sulphur oxides, or a cap of 840 kt, 45% for VOC, or a cap of 360 kt, and 20% for PM, or a cap of 160 kt.

The sector-specific caps should be validated by June 2007.

We should add that other limits could be imposed for mercury emissions from electricity generation and base metal smelting. The same could be true for benzene emissions from natural gas production and processing, refineries and the iron and steel industry.

Compliance mechanisms

As in the case of GHG emissions, the government proposes various measures enabling companies to comply with their emission reduction obligations. Apart from the possibility of reducing emissions by their own means, companies can trade nitrogen oxide and sulphur oxide emissions, subject to restrictions on the use of tradable credits if the company is located in a region where air quality does not meet the national objectives or if it contributes to air pollution in regions downstream. We should add that the government is considering the establishment, with the United States, of a cross-border trading system for nitrogen oxide and sulphur oxide emissions.

Due to the fact that some provinces have already regulated or are considering regulation of GHG emissions and air pollutants, the federal government’s regulatory framework confers very great autonomy on the provinces through the equivalency agreement mechanism discussed below.

Administrative framework

Equivalency agreements

Pursuant to section 10 of CEPA, the Minister may enter into an equivalency agreement with a province, a territory or an aboriginal government if this government can prove that there are provisions in force which attain or exceed an equivalent environmental protection level prescribed by the federal regulations in force and that these provisions include rights similar to those prescribed by sections 17 to 20 of CEPA, namely the right of citizens to demand an investigation of offences under the legislation.

³ The emission cap would be 65% in 2011, 60% in 2012, 55% in 2013, 50% in 2014, 40% in 2015, 10% in 2016 and 2017 and 0 in 2018.

If an equivalency agreement is made, enforcement of the federal regulations may be suspended in the signatory province or territory, so that the equivalent provincial regulation would apply.

Penalties

Subject to the penalties that may be found in CEPA against the violation of a legal obligation, the federal government's regulatory framework does not provide for any specific penalty for violation of the industrial air emission reduction targets.

Follow-up and evaluation

The government framework provides for a five-year review of the regulations to evaluate the progress accomplished towards attainment of the medium-term and long-term emission reduction objectives.

In conclusion, let's look at the regulatory non-regulatory actions the government proposes for transportation sources, commercial and consumer products, as well as the regulatory framework desired for improvement of indoor air quality.

B. Specific action for transportation sources, commercial and consumer products and indoor air quality

Concerning road transportation, the government wishes to adopt energy efficiency standards, beginning with the 2011 model year, when the Memorandum of Understanding with the auto industry expires in 2010⁴. For automobiles and light trucks, the government is pursuing the concept of a Clean Auto Pact based on North American environmental regulatory standards.

The rail sector would benefit from a voluntary approach from 2006 to 2010, but would be subject to restrictive standards beginning in 2011.

As regards the aviation sector, the government, for the time being, seems to want to honour the 2005 agreement, under which the industry undertook to reduce its GHG emissions by 24% in relation to its 1990 emissions by the 2012 deadline.

In the case of commercial and consumer products, the government intends, by 2012, to phase out the use of incandescent light bulbs, impose higher performance standards for all lighting products, energy performance standards for dishwashers, refrigerators, dehumidifiers, air conditioners, commercial washing machines and commercial boilers, and VOC reduction standards by reducing the amount of solvents used in commercial and consumer products.

Concerned about the health effects of indoor air quality, the government intends to develop draft regulations to improve indoor air quality and draw up a priority list of indoor contaminants that require government action.

Conclusion

Paradoxically, even though this regulatory framework is not yet a duly decreed regulation, so to speak, companies have no other choice but to comply with it promptly and begin reducing their GHG emissions if they want to reach their objectives of 18% in 2010. This has caused some raised eyebrows among people who express doubts about the adoption of the regulations before the next election and the reelection of the government in power.

In terms of environment protection, we may deplore the fact that targets will not be set in absolute terms from 2010. We do not know if "targets" will be considered as legal obligations or only broad goals without any penal consequences.

It is appropriate to ask what impact the Technology Fund will have on the free market for emission credits, since the contribution rate paid into the Fund would be set at \$15, and then at \$20, per tonne of carbon dioxide equivalent. The Fund could have the effect of limiting the free market to projects with a value of less than \$15 per tonne. In terms of environmental protection, there is reason to ask whether it will limit real GHG emission reductions by allowing technological investments to replace concrete reductions.

The government's intention to recognize the early actions taken between 1992 and 2006 makes us wonder how the government will credit these actions if the year base is 2006.

We can question the scope of the offset credits: Do they apply exclusively to the regulated companies? Due to the existence of the Fund, will they be limited to projects valued at less than \$15 per tonne?

There is also reason to rejoice at the recognition of the Kyoto Protocol's Clean Development Mechanism, even though it is capped at 10% of the total target. In this case as well, the concrete effect of the Technology Fund might be to favour only CDMs valued at less than \$15 per tonne of carbon dioxide equivalent. It is deplorable that the national registry required under

⁴ According to this Memorandum, the auto industry undertook to reduce its GHG emissions by 5,3 Mt by the 2010 deadline in relation with its 1990 emissions.

You can contact any of the following members of the Climatic Changes Law group in relation with this bulletin.

the Kyoto Protocol does not exist for Canadian companies and that there is no recognition of the Kyoto Protocol's Joint Implementation Mechanism, but at least the government reserves the possibility of monitoring market trends and eventually allowing trading with other American or European emission trading systems.

The latitude allowed to the provinces, territories and aboriginal government has the merit of avoiding overlaps by allowing application of the provincial or territorial regulations through equivalency agreements, to the exclusion of the federal regulations. However, what will be the applicable criteria to determine if the provincial regulation attains or exceeds and equivalent environment protection level prescribed by the federal regulation in force?

As of today, future transaction should report any applicable emission reduction targets, any project to reduce GHG emissions, any non compliance GHG issues, as well as any emission trading project.

All successive governments have acknowledged the importance of the issue of climate change, but none of them has shown an unequivocal intention to move from talk to action. It seems that this question of GHG emission regulation, now put off to 2008, increasingly is a "rewarmed issue" for the House of Commons and the government, as it has been for years, with everyone afraid of burning their fingers.



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