THE SOLITARY ATTEMPT: INTERNATIONAL TRADE LAW AND THE INSULATION OF DOMESTIC GREENHOUSE GAS TRADING SCHEMES FROM FOREIGN EMISSIONS CREDIT MARKETS

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This Comment examines the influence of international trade agreements on the implementation of a hypothetical, domestically-scaled cap-and-trade scheme to facilitate greenhouse gas emissions reductions in the United States. Several areas of intersection are examined, including the contemplation of the credits as commodities for trade and the construction of measures designed to offset any competitive disadvantage such a system might put on domestic companies. The Comment concludes that a domestically-scaled cap-and-trade scheme, while an important step in mitigating global climate change, is vulnerable to challenges under existing international trade agreements. Such challenges, if successful, may in turn drive the convergence of policy goals and mechanisms on an international scale, thereby undercutting the United States' ability to pursue regulatory goals distinct from the rest of the world. In order to best protect domestic interests, the nation should augment the development of domestic policies with the active negotiation of international emissions reduction goals and agreements on the treatment of emissions credits under international trade regimes.

INTRODUCTION

December of 2007 saw the thirteenth Conference of the Parties[1] under the United Nations Framework Convention on

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1. United Nations Climate Change Conference, *United Nations Climate Change Convention in Bali* (2007), http://unfccc.int/meetings/cop_13/items/4049.php (last visited Sept. 10, 2008).

Climate Change ("UNFCCC").[2] Held in Bali, the topics of discussion were many, but none so contentious as what to do next; that is, how to catalyze—and how to structure—a world-wide climate change response post-Kyoto. As the Conference came to a close during the final formal plenary, the United States made an objection, providing another in a long string of obstructions to the consensus-making efforts under the UNFCCC.[3] In response, Papua New Guinea's Kevin Conrad stood and charged the obstinate giant, " 'I would ask the United States, we ask for your leadership. But if for some reason you're not willing to lead, leave it to the rest of us. Please get out of the way.' "[4]

The remark met loud applause from the collection of representatives and observers that had spent the prior two weeks diligently working out a roadmap for future collaborative efforts.[5] The remark earned Mr. Conrad the title of "the mouse that roared in Bali,"[6] and became symbolic of a growing impatience with the United States' reticence regarding global climate change initiatives. However, the mouse that roared may not be without teeth.

As a prolific by-product of production, the general consensus is that policies addressing greenhouse gas emissions reductions should leverage market forces toward the achievement of their environmental policy goals.[7] Of course, the markets of the world are integrated by complicated international trade regimes under treaties such as the North American Free Trade

2. United Nations Conference on Environment and Development: Framework Convention on Climate Change, May 9, 1992, 1771 U.N.T.S. 108, *reprinted in* 31 I.L.M. 849 (1992) [hereinafter UNFCCC].

3. Andrew C. Revkin, *Issuing a Bold Challenge to the U.S. Over Climate*, N.Y. TIMES, Jan. 22, 2008, at F.2. It should be noted that Conrad's challenge followed on the heels of the one issued by the U.N. Secretary General, which called for "the United States and China to play 'a more constructive role' " in the development of a world-wide strategy to mitigate climate change effects through the reduction of greenhouse gas emissions. Elisabeth Rosenthal, *U.N. Chief Seeks More Leadership on Climate Change*, N.Y. TIMES, Nov. 18, 2007, at 1.3.

4. *See* Revkin, *supra* note 3.

5. *Id.*

6. *See, e.g.,* Videotape: The Mouse that Roared in Bali (N.Y. TIMES 2008), http://video.on.nytimes.com/?fr_story=8b8fe34e60b27654b7f8cd4b31008fe348a41b86 (last visited Sept. 10, 2008).

7. On this general point, see Carol M. Rose, *Rethinking Environmental Controls: Management Strategies for Common Resources,* 1991 DUKE L.J. 1, 14–24 (1991), which argues that market forces and property law regimes are more favorable to command and control legislation when the objects of regulation are pervasive.

Agreement ("NAFTA"),[8] and the General Agreement on Tariffs and Trade ("GATT"),[9] or other provisions formulated under the auspices of the World Trade Organization ("WTO").[10] If the United States does not take a leadership role in the negotiation of global reduction goals and the development of climate change policy tools, and chooses instead to act on a national scale first, it may find its efforts vulnerable to challenges under international trade law. These challenges may, in turn, push domestic efforts toward conformity with international climate change responses, whether the nation agrees to those terms or not.[11]

There are several leverage points through which international trade regimes might influence domestic cap-and-trade systems, some more plausible—that is, presenting more colorable international legal claims—than others:

[1] Tenets of international trade law, specifically national treatment and most-favored nation principles, may require the inter-market transfer and recognition of emissions allowance credits.

[2] National treatment and most-favored nation principles may require that foreign investors and financial service providers be allowed to participate in the domestic cap-and-trade system.

[3] The principles of trade liberalization may disallow the imposition of trade barriers aimed at reducing the burden imposed upon domestic producers vis-à-vis importers of foreign goods that may not be as stringently regulated, if regulated at all.

[4] Even if such measures are exempted from the requirements of free trade agreements, the principle of common but differentiated responsibilities may limit the *extent* to which the United States is allowed to close the competitive gap through parallel measures: international trade regimes may prohibit the United States

8. North American Free Trade Agreement, U.S.-Can.-Mex., Dec. 17, 1992, 32 I.L.M. 289 (1993) [hereinafter NAFTA] (NAFTA Preamble and Parts 1-III); *Id.* at 605 (NAFTA Parts IV-VII).

9. *See* General Agreement on Tariffs and Trade of 1947, Oct. 30, 1947, 55 U.N.T.S. 187 [hereinafter GATT 1947].

10. *See, e.g.*, Final Act Embodying the Results of the Uruguay Round of Trade Negotiations, Apr. 15, 1994, 33 I.L.M. 1125 (1994) and following agreements [hereinafter WTO Agreements], *available at* http://www.wto.org/english/docs_e/legal_e/final_e.htm.

11. *See infra* Parts III and IV.

from putting imported goods on equal footing with domestic goods when it comes to internalizing the costs of their carbon footprint.

[5] Finally, there is some concern that the allocation of emission allowances may in effect subsidize the operation of certain recipients, which would in turn be actionable under international trade law by importers or importing countries that perceive themselves to be disadvantaged by the measures.[12]

Dispute resolution at all of these intersections between international trade law and domestic cap-and-trade measures has the potential to drive the convergence of distinct cap-and-trade regimes. For example, a reviewing body might strike down restrictions on participation in the markets, urge the cross-market transfer of emissions allowances, or call for the uniform application of the principle of common-but-differentiated responsibilities under the UNFCCC. Such holdings would drive the integration of regulatory efforts that had, up to that time, been conceived as distinct regimes. Of the enumerated issues above, only the first, third, and fourth issues are considered in any detail in this Comment. The second and fifth concerns have been thoroughly addressed by other authors.[13]

This Comment divides the discussion into several parts. As an initial matter, it provides two brief background sections: one on the United States' experience with cap-and-trade mechanisms as contextualized by international efforts to address global climate change (Part II), and another on the relevant international trade law which, through its requirements and dispute resolution mechanisms, may have something to say about a domestically-scaled cap-and-trade program (Part

12. Since this fifth aspect is not discussed further, the skeletal argument is this: the development and distribution of emissions allowances constitutes a substantial transfer of salable resources from the government to certain industries. If a company ends up as a net-seller of these allowances and if those sales reach a certain level there is a colorable claim that the government has just subsidized certain industrial activities, which in turn would implicate the imposition of countervailing duty measures as a remedy to offset the subsidy granted to a foreign competitor.

13. *See*, *e.g.*, Marisa Martin, *Trade Law Implications of Restricting Participation in the European Union Emissions Trading Scheme*, 19 GEO. INT'L ENVTL. L. REV. 437, 444–46 (2007) (discussing restrictions of foreign service providers from the European Union Emissions Trading Scheme); Annie Petsonk, *The Kyoto Protocol and the WTO: Integrating Greenhouse Gas Emissions Allowance Trading into the Global Marketplace*, 10 DUKE ENVTL L. & POL'Y F. 185, 204–14 (2000) (discussing various arguments as to whether allocation of emissions credits constitutes an actionable subsidy under the WTO regime).

III). These Parts will help locate the issues in the field of international law and foreshadow later discussions, but do not present any analysis specifically concerning the concerns identified above. Part IV examines possible efforts to protect domestic producers from competitive disadvantages arising relative to their unregulated foreign competitors. Part V considers whether emissions credits themselves deserve national and most-favored-nation treatment. Of special concern here is whether NAFTA provisions complicate the analysis of other authors based solely on WTO requirements and precedent. Providing a salient example for the consideration of these issues throughout the Comment is America's Climate Security Act of 2007, also known as the Lieberman-Warner Bill, which is currently before Congress for consideration.[14] The Bill would establish an economy-wide cap-and-trade program to facilitate the United States' reduction of greenhouse gas emissions, and it includes several provisions which explicitly contemplate such a system's interaction with foreign trade.[15]

In Part VI, this Comment concludes that a nationally-scaled cap-and-trade system, though a critical step in addressing the global concern of climate change, may be vulnerable to challenges levied under international trade regimes. While there are better and worse ways of structuring such a domestic system in order to insulate it from attack, the most protective measures are likely to be the pursuit of parallel international agreements that would establish through treaty how emissions credits should be treated by the various free trade agreements and set agreed-upon emissions reduction goals for the nations of the world. In concrete terms the Lieberman-Warner Bill does a reasonable job of protecting itself from attack under international trade agreements, but it is not "bulletproof."[16] Section 6003(b)(1) of the Bill sets out the policy that the United States "work proactively under the United Nations Framework Convention on Climate Change and, in other appropriate forums, to establish binding agreements committing all major

14. *See* S. 2191, 110th Cong. (2007), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_bills&docid=f:s2191is.txt.pdf. A summary of the bill is available from the Library of Congress' website at www.thomas.gov.

15. *See, e.g.*, S. 2191 § 2501 ("Use of International Allowances or Credits"); §§ 6001–07 (collectively referred to as "Title VI—Global Effort to Reduce Greenhouse Gas Emissions").

16. Darren Samuelsohn, *Baucus Seeks Assurances on Global Warming Bill's WTO Prospects*, ENV'T & ENERGY DAILY, Feb. 15, 2008 (on file with author).

greenhouse gas-emitting nations to contribute equitably to the reduction of global greenhouse gas emissions."[17] This statement of policy should be understood not merely as an aspirational goal, but as a critical component to the successful implementation of such a scheme.

II. THE UNITED STATES AND GREENHOUSE GAS CAP-AND-TRADE SCHEMES: INTERNATIONAL LAW AND POLICY CONCERNS

The international regulatory complex surrounding greenhouse gas emissions is an impressive patchwork of regulatory regimes.[18] Most prominent in this landscape is the move toward cap-and-trade systems to reduce emissions.[19] The European Union ("EU") consolidated its efforts to comply with its various Kyoto-set obligations under the European Union Emissions Trading Scheme ("EU ETS").[20] The EU ETS is itself comprised of the elemental regimes of its many member nations, and its ranks may be expanded in the not-too-distant future to include Canada and Japan.[21] Additionally, several regional cap-and-trade programs are under development within the United States.[22]

Commentators and critics have written volumes assessing this regulatory complex and its many components. Some argue that this kind of multi-layered regulatory complex is just what the doctor ordered, analogizing to the system of cooperative federalism structured under the Clean Air Act and the Clean Water Act whereby the states are responsible for coming up with and enforcing regulations that meet federally determined goals regarding environmental protection.[23] Most, however,

17. S. 2191 § 6003(b)(1).

18. *See generally* Erik B. Bluemel, *Unraveling the Global Warming Regime Complex: Competitive Entropy in the Regulation of the Global Public Good*, 155 U. PA. L. REV. 1981 (2007).

19. *See, e.g.*, Shan Carter et al., *On the Issues: Climate Change*, N.Y. Times, http://elections.nytimes.com/2008/president/issues/climate.html (last visited Oct. 17, 2008) (indicated that both presidential candidates in 2008 supported a mandatory cap-and-trade system to reduce greenhouse gas emissions).

20. *See* Council Directive 2003/87/EC,2003 O.J. (L 275) 32 (EU) ("Establishing a Scheme for Greenhouse Gas Emission Allowance Trading Within the Community and Amending Council Directive 96/61/EC").

21. *See* Martin, *supra* note 13, at 446.

22. Principal among these are the Regional Greenhouse Gas Initiative in the Northeast, http://www.rggi.org/, and the Western Climate Initiative in the western United States, http://www.westernclimateinitiative.org/.

23. *See* Bluemel, *supra* note 18, at 2030 (citing Tamara L. Joseph, *The Debate*

are skeptical of anything less than a harmonized, international affront on the problem of global climate change. For example, Erik Bluemel recently argued that the nested nature of the EU ETS in fact creates an agar for inefficiency and a network of incentives for non-compliance, both of which frustrate the system's environmental policy goals.[24] Under his analysis, adding more distinct regulatory schemes to the international greenhouse gas regulatory process could only make things worse.[25] Many others have approached the problem of global emissions reduction through a traditional commons analysis inspired by Hardin's *The Tragedy of the Commons*.[26] For the most part, these writers conclude that sub-global (and thus certainly subnational) attempts at regulating a global commons are either destined for failure or doomed to languish in inadequacy.[27]

Over Environmental Standards in the European Community: A Race to the Top Rather Than a Race to the Bottom?, 6 N.Y.U. ENVTL. L.J. 161 (1997); Richard L. Revesz, *Rehabilitating Interstate Competition: Rethinking the "Race-to-the-Bottom" Rationale for Federal Environmental Regulation*, 67 N.Y.U. L. REV. 1210 (1992)).

24. *See* Bluemel, *supra* note 18, at 2018 ("While the EU ETS seeks to harmonize its policies with those of the Kyoto Protocol, it has neither fully synchronized its liability rules with the Protocol nor ensured that standard procedural requirements are applied within its member countries.").

25. *See id*. at 2032 ("Different liability rules, procedures, and enforcement mechanisms across elemental regimes . . . create opportunities for accidental and intentional noncompliance that are not present in a harmonized global regime.").

26. Garrett Hardin, *The Tragedy of the Commons*, SCIENCE, Dec. 13, 1968, at 1243.

27. *See, e.g.*, Daniel C. Esty, *Toward Optimal Environmental Governance*, 74 N.Y.U. L. REV. 1495, 1498 (1999) (warning that a "theory of optimal environmental governance must . . . seek to minimize . . . structural (or jurisdictional) mismatches between the scale of an issue and the regulator's jurisdiction"); Laura Kosloff & Mark Trexler, *State Climate Change Initiatives: Think Locally, Act Globally*, 18 NAT. RES. & ENV'T, Winter 2004, at 46, 48 (admitting that state and local climate change initiatives are "a good thing" but questioning their efficacy and role in effecting substantive change); Robert N. Stavins, *Policy Instruments for Climate Change: How Can National Governments Address a Global Problem?*, 1997 U. CHI. LEGAL F. 293, 323 (1997) (concluding that, since unilateral regulatory actions "will invariably be highly inefficient, any domestic program requires an effective international agreement, if not a set of international greenhouse policy instruments"). *See also* Kirsten H. Engel & Scott R. Saleska, *Subglobal Regulation of the Global Commons: The Case of Climate Change*, 32 ECOLOGY L.Q. 183, 192 (2005) ("Legal scholars, applying the logic of the tragedy of the commons to global environmental problems such as climate change argue, consistent with the matching principle, that unilateral regulation by subglobal governments is irrational.").

A few authors have put forward interesting arguments to justify the activities of relatively small jurisdictions attempting to influence a global issue. *See, e.g.*, J.R. DeShazo & Jody Freeman, *Timing and Form of Federal Regulation: The Case of Climate Change*, 155 U. PA. L. REV. 1499, 1500 (2007) (arguing "that

Amidst these concerns over a splintered global response to global climate change, the United States has balked at regulating greenhouse gas emissions at all, largely due to the ever-present worry that imposing greenhouse gas emissions restrictions on the national economy may give our trade partners in the developing world—especially China and India—a competitive edge.[28] The United States has been reluctant to align itself with international efforts at reducing greenhouse gas emissions and has resisted integrating its regulatory prerogatives with those structured by other regimes. Upon Australia's recent ratification of the Kyoto Protocol, the United States donned a dubious notoriety as the sole industrialized nation not to have aligned itself with the treaty.[29] What's more, the United States joined the consensus at the final formal plenary of the UNFCCC held in Bali, Indonesia only after "[a] swell of boos and jeers" subsided at its objection to some last-minute language.[30]

However, the wheels of policy formulation have begun to turn in the United States. The publication of the Fourth Assessment Report: Climate Change 2007 by the Intergovernmental Panel on Climate Change[31] marked for many the de-

states can be important catalysts of a federal policy response by stimulating both pro-regulatory and anti-regulatory forces to appeal to the federal government for relief sooner rather than later"); Kevin Doran, *U.S. Sub-Federal Climate Change Initiatives: An Irrational Means to a Rational End?*, 26 VA. ENVTL. L.J. 189 (2007), *available at* http://ssrn.com/abstract=1019896; Kirsten H. Engel, *Mitigating Global Climate Change in the United States: A Regional Approach*, 14 N.Y.U. ENVTL. L.J. 54, 56 (2005) (noting that, "[c]onsidered by themselves, most of the state or local initiatives currently being contemplated are unlikely to have a big effect upon global climate change, although they could contribute importantly to moving forward the overall politics of greenhouse gas regulation" and going on to consider the relative effectiveness of small jurisdictions coordinating their efforts to cover larger sectors of the economy).

28. *See, e.g.,* Byrd-Hagel Resolution, S. Res. 98, 105th Cong. (1997).

29. *See* The Associated Press, *Kyoto Ratification First Act of New Leader*, N.Y. TIMES, Dec. 4, 2007, at A.8 (reporting that the newly elected Australian Prime Minister "immediately signed documents to ratify the Kyoto Protocol on climate change. The action reversed a decade of Australian environmental policy, left the United States standing alone among industrialized nations in its refusal to ratify the treaty, and brought prolonged applause at a United Nations climate change conference in Bali, Indonesia.").

30. Revkin, *supra* note 3.

31. Of the many sections to this long publication, the "Summary for Policymakers" made the most impressive impact on the discussion. Intergovernmental Panel on Climate Change, IPCC Fourth Assessment Report: Climate Change 2007, [hereinafter IPCC], http://www.ipcc.ch/ipccreports/assessments-reports.htm (follow "Working Group I Report, 'The Physical Science Basis' " hyperlink, then follow the "Summary for Policymakers" hyperlink).

finitive end to what seemed the painfully protracted debate regarding climate change science and whether the planet is indeed warming or its climate systems shifting. The question of just what to do about it now squarely faces policy makers. Of the many prospects, including carbon taxes or command-and-control regulation of greenhouse gasses under the Clean Air Act, the cap-and-trade system has quickly become the most talked-about option, if only for its pro-market aesthetic.[32]

Cap-and-trade programs targeting emissions reductions are not new to the United States. In 1990, Congress appended Title IV to the Clean Air Act, adding two cap-and-trade programs for the reduction of nitrogen oxides and sulfur dioxide, two pollutants tied to the creation of acid rain.[33]

Given the United States' historical reluctance to join international efforts to reduce greenhouse gases ("GHG"), and considering the nation's relatively extensive (and arguably successful) history with the implementation of cap-and-trade pollution reduction measures, it seems likely that the United States will try to insulate its scheme from other similar ones around the world.[34] While the question of whether or not it *should* insulate itself has been taken up by several authors as noted earlier, there is a very real question as to whether or not it even *can* in light of international trade agreements such as NAFTA,[35] GATT,[36] or WTO agreements.[37]

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32. It is fundamental to understanding international legal issues surrounding the development of emissions trading regimes to know the basics of how cap-and-trade systems work. For a brilliant introduction to how a cap-and-trade system works and many of the fundamental challenges to such a regulatory system, see Holmes Hummel's slide show "An Introduction to Cap-and-Trade Climate Policy," posting of David Roberts to Gristmill Blog, http://gristmill.grist.org/story/2007/12/6/05958/4475 (last visited Sept. 14, 2008), which discusses the topic by analogizing to the game of musical chairs.

33. Clean Air Act §§ 401–416, 42 U.S.C.A. §§ 7651–7651o (2003 & West Supp. 2008). The United States Environmental Protection Agency ("EPA") recently promulgated two more rules involving cap-and-trade systems for emissions reductions, the Clean Air Interstate Rule ("CAIR"), 72 Fed. Reg. 62338 (Nov. 2, 2007) (to be codified at 40 C.F.R. pt. 52), and the Clean Air Mercury Rule ("CAMR"), 72 Fed. Reg. 59190 (Oct. 19, 2007) (to be codified at selected parts of 40 C.F.R. pts. 51, 60, 72, 78, 96, and 97). However, the march of the cap-and-trade mechanism across the legal landscape of pollution control law was stifled somewhat when both of these rules were thrown out after judicial review. *See North Carolina v. EPA*, No. 05-1244 (D.C. Cir., July 11, 2008) (vacating CAIR); *New Jersey v. EPA*, No. 05-1097 (D.C. Cir. Feb. 8, 2008) (vacating CAMR).

34. *See*, *e.g.*, Lieberman-Warner Bill, S. 2191, 110th Cong. §§ 2501–02 (2007) (imposing limits on the use of foreign credits to cover domestic emissions reduction obligations).

35. NAFTA, *supra* note 8.

Domestic carbon cap-and-trade systems may be influenced by international trade agreements in several ways that command attention. First, as urged by the very lexicon with which these emissions trading systems are described, there is the concern of just how the trade of emissions credits will be couched within international trade requirements. Because the fundamental goal of trade liberalization is to reduce trade barriers between marketplaces, those bodies hearing complaints under international trade treaties may look poorly upon emissions trading systems that seek to insulate themselves from outside participation. Marisa Martin recently illustrated, in the context of the EU ETS, that restricting foreign brokerage firms from participating in the trade of emissions credits may violate the General Agreement on Trade in Services.[38] In addition, there is the possibility that the emissions credits themselves might be treated as tradable commodities that are cognizable by the trade liberalization treaties. While several authors that have thought about this issue have concluded that emissions credits would not be considered "products" under the GATT,[39] Canada's recent proposal to implement a cap-and-trade scheme tied to the EU ETS adds a new dimension to the situation.[40] NAFTA's provisions are arguably broader in their consideration, and may require integration of Canadian and U.S. systems if they were erected in parallel. This, in turn, may open a back door for the transfer of credits between the European system and anything implemented domestically in the United States. Such transfers, if not accounted for in the development of the scheme, could well frustrate the market's stability and the environmental policy goals of the various systems.

Further, and perhaps the most prominent concern sounded in the debate over the construction of a carbon cap-and-trade system, some view the imposition of such regulatory schemes as effecting a tax on the covered industries.[41] Essentially, the

36. GATT 1947, *supra* note 9.

37. *See*, *e.g.*, WTO Agreements, *supra* note 10.

38. Martin, *supra* note 13, at 439 ("[T]he E.C. Directive restricting carbon trading is inconsistent with the E.C.'s commitment to liberalize its financial services under the GATS. . . . [B]y banning *U.S.* participation in the E.U. ETS, the European Community is acting contrary to Articles II (most-favored nation), XVII (national treatment), and XVI (market access) of the GATS.") (emphasis added).

39. *Id.* at 446–47.

40. *See* discussion *infra*, Part V.

41. *See* discussion *infra*, Part IV.

argument goes, making covered industries pay to emit certain toxins into the air will raise the cost of production of domestic goods. That is, after all, the whole idea: to make industry polluters internalize the cost of climate shifting production practices. But this sparks worries surrounding the loss of competitive edge against foreign companies that are not burdened by such costs. Companies making their home in countries that either have less stringent greenhouse gas emissions controls or have yet to enact any emissions restrictions whatsoever would then have an advantage over U.S. producers.

III. A CONTEXTUALIZED INTERNATIONAL TRADE LAW BACKGROUNDER

This Comment now turns to what NAFTA and the WTO require of their contracting parties, and the rights and obligations they frame in connecting domestic environmental regulation to international trade. Though, admittedly, the "devil is in the details," a broad-strokes review of the NAFTA and WTO trade agreement regimes and their interpretive histories will nonetheless help tease out some of the complexities that arise when regional or domestic cap-and-trade schemes are imposed under extant free trade obligations.[42] What follows is a high-altitude review of the structure of free trade under the provisions of NAFTA and the WTO regime that attempts to note those provisions that are potentially important in later analysis. After that, this Comment briefly reviews the international law principle of common but differentiated responsibilities in the context of global efforts to mitigate and adapt to the effects of climate change.

A. The Treaty Provisions Governing Free Trade

Several tenets of trade liberalization operate similarly under the two regimes. Perhaps most importantly here, both NAFTA and the WTO Agreements require "national treatment" of imported goods.[43] Essentially, this means that no nation is

42. Cataloging the nuances of the connection between these free trade agreements and domestic environmental laws is not only beyond the scope of this Comment, but is the subject of quite a few thick volumes of legal analysis and instruction. The point here is merely to sketch out the international trade framework in order to overlay it with the novel contemporary issue of domestic greenhouse gas cap-and-trade schemes.

43. Indeed, NAFTA incorporates by reference the GATT's national treatment

allowed to discriminate between its own products and those from abroad; parties to these agreements must treat imported goods identically to like goods that are produced domestically. Under NAFTA, the requirement is asserted in a number of ways but none more important than in the investment framing it is given in Chapter 11: "Each Party shall accord to investors [and investments of investors] of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors [or to investments of its own investors]."[44] However, these terms are broadly defined, covering, *inter alia*, any "enterprise," loan to, or equity security of an enterprise, and "real estate or other property, *tangible or intangible*."[45]

The WTO provisions related to national treatment of imported goods are not quite so all-encompassing on their face as those of NAFTA. Under Article III of the GATT 1994, taxes and regulations shall not be imposed "so as to afford protection to domestic production."[46] This language is limited to goods or commodities as they have been traditionally understood. Even the Agreement on Trade-Related Investment Measures only covers "goods."[47] However, Article XVII of a parallel agrement, the General Agreement on Trade in Services ("GATS"),[48] extends national treatment requirements to services.

The NAFTA and WTO trade regimes also impose "most-favored nation treatment" obligations. Where national treatment ensures members will not discriminate between their

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principles and all its interpretive notes. NAFTA, *supra* note 8, art. 301(1). *See also id.*, art. 1102 ("National Treatment"); GATT 1947, *supra* note 9, art. III ("National Treatment on Internal Taxation and Regulation").

44. NAFTA, *supra* note 8, arts. 1102–03. There are provisions tailoring the national treatment requirement to nearly every topic addressed under NAFTA—Government Procurement, *id.*, art. 1003, Cross-Border Trade in Services, *id.*, art. 1202, Financial Services, *id.*, art. 1405, Intellectual Property, *id.*, art. 1703—but for the most part, these employ many of the same words in the description of the principle as the Chapter 11 formulation for investments, and none are quite so impressive in scope.

45. *Id.,* art. 1139 (emphasis added); *see also* S.D. Myers, Inc. v. Canada, 40 I.L.M. 1408, 1431–32 (NAFTA Arb. Trib. 2000) (interpreting investment broadly to include expectations of income or profit); discussion *infra* Part V (concerning Canada and the establishment of an emissions trading scheme in order to comply with that country's Kyoto obligations).

46. GATT 1947, *supra* note 9, art. III(1).

47. *See* WTO Agreements, *supra* note 10, Annex IA, art. 1 (Agreement on Trade-Related Investment Measures).

48. General Agreement on Trade in Services, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1B, Legal Instruments—Results of the Uruguay Round, 1869 U.N.T.S. 183, 33 I.L.M. 1125 (1994) [hereinafter GATS].

own products and those from abroad, the most-favored nation treatment principle requires that members not discriminate between the products of other parties as well.[49] The NAFTA provisions mirror those regarding national treatment, again employing the investors and investment lexicon.[50] The WTO provisions provide simply that there be no margin of preference granted to those duties imposed on the imports of one country vis-à-vis any other importer of like goods or services.[51]

Despite some similarities in allowable exceptions to the imposition of trade measures, the two trade regimes diverge considerably in the field.[52] For the purposes of the WTO agreements, permissible exceptions to the earlier-mentioned general principles concerning the imposition of trade barriers are captured in Article XX of the GATT. Of particular concern here are those exceptions relating to environmental protection. Specifically,

> nothing in [the GATT] shall be construed to prevent the adoption or enforcement by any contracting party of measures:
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> . . . .
>
> (*b*) necessary to protect human, animal or plant life or health;
>
> . . . .
>
> (*g*) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption.[53]

As prefaced by Article XX's chapeau, provisions covered by these exceptions cannot "constitute a means of arbitrary or unjustifiable discrimination" between importing countries.[54]

These exceptions and their surrounding jurisprudence are important under NAFTA since Article XX and its interpretive notes are incorporated by reference into NAFTA Article

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49. *See* NAFTA, *supra* note 8, art. 1103.

50. *See id*. As with the national treatment requirement, there are several scattered sections describing the most-favored-nation principle in context sensitive terms. I have focused here on the broadest language to ease the analysis and shorten this review.

51. GATT 1947, *supra* note 9, art. I; GATS, *supra* note 48, art. II.

52. This divergence is discussed below in Part III.B with regard to the interpretive history of the two treaty regimes.

53. GATT 1947, *supra* note 9, art. XX.

54. *Id*.

2101(1).[55] NAFTA also has exception language couched within provisions that discuss the rights and obligations of Parties to develop and implement sanitary and phytosanitary ("SPS") measures[56] and standards-related measures.[57] For the most part, the rights and obligations with regard to each type of standard closely track one another.[58] The Parties are to use international standards to guide the setting of SPS and standards related measures[59] and, to the extent practicable, are to "pursue equivalence" of those measures.[60] However, the Parties are directed to "make compatible their respective standards-related measures" "[w]ithout reducing the level of safety or of protection of human, animal or plant life or health, the environment or consumers."[61] Importantly, NAFTA countries are allowed to employ measures more stringent than any existing international standard[62] so long as they are founded upon rigorous scientific investigation,[63] do not discriminate between domestic and foreign products,[64] do not create unnecessary obstacles to trade,[65] and are not established to disguise trade restrictions by casting them in an environmental lexicon, just as required by the Article XX chapeau.[66]

Both NAFTA and the GATT/WTO provide mechanisms for dispute resolution that may be engaged by nations perceiving themselves penalized by the imposition of trade barriers.[67] As

55. NAFTA, *supra* note 8, art. 2101(1).

56. *Id.*, arts. 709–23. SPS measures are used to safeguard against risks to "human, animal, or plant life or health" from pests, diseases, or food-born contaminants. *Id.*, arts. 712(1), 724.

57. *Id.*, arts. 901–15. The scope of these technical standards is far broader than SPS measures as they cover all human health, welfare, and environmental measures that might act as inadvertent barriers to trade. *See id.*, arts. 904, 915.

58. *Compare* NAFTA, *supra* note 8, arts. 904–05, *with* arts. 712–13.

59. *Id*. arts. 713, 905.

60. *See id*. arts. 714, 906.

61. *Id*. art. 906(2).

62. *Id*. art. 905(3).

63. *See* NAFTA, *supra* note 8, arts. 712(3), 907(1)(a); *see also* Panel Report, *EC Measures Concerning Meat and Meat Products (Hormones) – Complaint by the United States*, WT/DS26/R/USA (Aug. 18, 1997) (reviewing European Union measures inhibiting the importation of meat products with certain hormones under the Agreement on the Application of Sanitary and Phytosanitary Measures and finding those measures inadequately justified by scientific risk assessment studies).

64. *See* NAFTA, *supra* note 8, arts. 712(4), 904(3).

65. *See id*. arts. 712(5)–(6), 904(4).

66. *See id*. arts. 712(6), 907(2)(b); GATT 1947, *supra* note 9, art. XX.

67. *See, e.g.,* NAFTA, *supra* note 8, ch. 11, § B (Settlement of Disputes between a Party and an Investor of Another Party), ch. 19 (Review and Dispute Settlement in Antidumping and Countervailing Duty Matters).

such, countries frustrated by the construction of a cap-and-trade program in the United States that burdens companies beyond the country's borders may engage these mechanisms in order to bring the United States' scheme more in line with international practices.

NAFTA sets up a host of dispute resolution mechanisms to be employed depending on the nature of the dispute.[68] However, disputes between NAFTA parties, with some exceptions, "regarding any matter arising under both this Agreement [NAFTA] and the *General Agreement on Tariffs and Trade*, any agreement negotiated thereunder, or any successor agreement (GATT), may be settled in either forum at the discretion of the complaining Party."[69] This choice of forum opportunity confers a significant advantage to the aggrieved party. For example, a party that perceives a penalty due to the establishment of a countervailing duty against its products may engage the dispute resolution process set forth in NAFTA Chapter 19, a process explicitly designed to be deferential to the countervailing duty laws of the defending party. On the other hand, the aggrieved party could pursue resolution of the dispute under the WTO regime, where panels would employ international trade law principles rather than interpret domestic countervailing duty laws.[70] Given the history of WTO consideration of measures erected for environmental protection discussed below, and NAFTA's greater concern for environmental protection, it is likely that any challenges to domestic environmental laws would be brought under the auspices of the WTO regime.[71] As such, WTO provisions and interpretation are primary in the following analysis.

B. Interpretive Histories Under the Free Trade Regimes

At the dawn of the NAFTA negotiations, the GATT arbitral panel handed down a decision in a dispute between the United States and Mexico over an embargo the former had imposed on

68. *See id.*

69. *Id.* art. 2005(1). *See also* David A. Gantz, *Dispute Settlement Under the NAFTA and the WTO: Choice of Forum Opportunities and Risks for the NAFTA Parties*, 14 AM. U. INT'L L. REV. 1025, 1034 (1998–1999).

70. *See* Gantz, *supra* note 69, at 1028.

71. The WTO Appellate Body's infamous rejection of every cross-border environmental regulation that it has been asked to review is illustrated in the cases discussed in the following section.

the import of yellowfin tuna and yellowfin tuna products.[72] According to the United States, tuna fishing practices, which employed "purse-seine" nets, effected an intolerable "taking" of dolphins under Section 101(a)(2) of the Marine Mammal Protection Act ("MMPA").[73] As such, products tainted by the use of such methods were subjected to an embargo.[74]

Mexico challenged the embargo under Article XI of the GATT, and the United States responded that its embargo should be allowed to stand under Article III, citing the Article XX exceptions.[75] The GATT Panel Report, commonly called *Tuna/Dolphin I*, favored Mexico.[76] The measures employed by the United States were impermissible under the tenets of liberalized trade and could not be justified by the exceptions of GATT 1947 Article XX(b) and (g).[77] The decision held that trade restrictions discriminating between "like physical products" based solely on the methods of their production are inconsistent with the provisions of the GATT: trade measures cannot make distinctions on processes or production methods alone.[78] The GATT arbitral panel later clarified that this process/product distinction does not only frame decisions between producing and consuming countries. In *Tuna/Dolphin II*, a related review of the MMPA brought by the European Economic Community and the Netherlands, the panel said that the process/product distinction is also to be applied to restrictions imposed on products channeled through "intermediary" countries—nations essentially acting as middlemen between producing and consuming countries.[79] This basic holding was reaffirmed in later decisions by the GATT arbitral panel.[80]

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72. CHRIS WOLD ET AL., TRADE AND THE ENVIRONMENT: LAW AND POLICY 205 (2005).

73. *Id.*

74. *Id.*

75. *Id.* at 205–06.

76. *See id.* at 205–08.

77. *See* PHILIPPE SANDS, PRINCIPLES OF INTERNATIONAL ENVIRONMENTAL LAW 955 (2d ed. 2003).

78. *See* Report of the Panel, *United States—Restrictions on Imports of Tuna*, DS21/R (Sept. 3, 1991) (unadopted), 30 I.L.M. 1594, 1616–1622 (1991) [hereinafter *Tuna/Dolphin I*].

79. Report of the Panel, *United States—Restrictions on Imports of Tuna*, DS29/R (June 16, 1994) (unadopted), 33 I.L.M. 839, 888–99 (1994) [hereinafter *Tuna/Dolphin II*]. *See also* WOLD ET AL., *supra* note 72, at 210–11.

80. *See* WOLD ET AL., *supra* note 72, at 213–14 (stating that the central holdings of *Tuna/Dolphin I* & *II* were "reinforce[d]" by the GATT Panel's later reports, including, *inter alia*, Report of the Panel, *United States – Taxes on Automobiles*, DS31/R (Oct. 11, 1994) (unadopted), 33 I.L.M. 1397 (1994)).

Proceeding as they did in the shadow of *Tuna/Dolphin I*, the NAFTA negotiations were haunted by the possibility that trade agreements could adversely affect the efficacy of even *domestic* environmental laws. Article 903 attempts to eliminate this concern by allowing a party to maintain a degree of protection greater than that afforded by the norms of the international community. Nevertheless, as discussed above, the choice of forum opportunity offsets any real protective benefit this provision attempts to establish.[81]

In 1996, the newly formed WTO Appellate Body was presented with its first dispute overtly concerned with environmental protection. The *Reformulated Gasoline* case involved a dispute between the United States and two South American countries, Brazil and Venezuela, who both complained that the newly promulgated "Gasoline Rule" of the United States impermissibly discriminated against foreign importers.[82] In considering the dispute, the Appellate Body illuminated several aspects concerning trade restrictions that seek justification under Article XX exceptions. First, it concluded that the GATT " 'is not to be read in clinical isolation from public international law,' " thereby allowing for principles of international law beyond the WTO to play a part in considering the availability of Article XX exceptions.[83] This means that principles such as sustainable development, the precautionary principle, and the principle of common but differentiated responsibilities may all affect whether an otherwise prohibited trade restriction should be allowed under Article XX.

Additionally, the Appellate Body noted several characteristics of the Article's chapeau, which places the "no arbitrary or unjustifiable discrimination" condition on regulations that would seek haven there.[84] Specifically, the Appellate Body

81. *See* NAFTA, *supra* note 8, arts. 903, 2005(1).

82. Panel Report, *United States—Standards for Reformulated and Conventional Gasoline*, WT/DS2/R (Jan. 29, 1996), 35 I.L.M. 274 (1996) [hereinafter *Reformulated Gasoline,* Panel Report]; Appellate Body Report, *United States – Standards for Reformulated and Conventional Gasoline,* WT/DS2/AB/R (Apr. 29, 1996), 35 I.L.M. 603 (1996) [hereinafter *Reformulated Gasoline*, Appellate Body Report].

83. SANDS, *supra* note 77, at 963 (quoting *Reformulated Gasoline*, Appellate Body Report, *supra* note 82, at 621). *See also* Appellate Body Report, *European Communities—Measures Concerning Meat and Meat Products (Hormones)*, ¶¶ 120–30, WT/DS26/AB/R, WT/DS48/AB/R (contemplating the European Communities' argument that the precautionary principle has become a part of the corpus of customary environmental law).

84. *See* SANDS, *supra* note 77, at 963–64.

pointed out, *inter alia*, that the chapeau was concerned more with the manner in which the disputed measure was implemented, that it underscored the ideas that the listed exceptions ought not be employed in ways that frustrate the goals of trade liberalization or abrogate legal obligations under the substantive rules of the GATT, and that the burden of proof to justify the measure under the chapeau lay with the party pushing its implementation (generally speaking, the party defending themselves before the Body).[85]

The *Shrimp/Turtle* cases marked the next evolution in defining the intersection of regulations aimed at environmental protection and international trade law under the WTO.[86] There, the dispute centered on the United States' import ban imposed on shrimp products harvested with technology that would inadvertently take sea turtles in the process.[87] The import ban paralleled regulations under the Endangered Species Act which required U.S. fleets to use so-called turtle excluder devices.[88]

Reviewing a challenge that the import ban violated the tenets of liberalized trade, the Appellate Body upheld the *Reformulated Gasoline* decision by insisting that there be a "substantial relationship" between the structure of the trade measure and the purported environmental policy goal.[89] Additionally, the measure must be applied evenhandedly among foreign and domestic products.[90] Measures that invoke the Article XX(g) exception to the protection of exhaustible resources must be implemented "in conjunction with restrictions on domestic production or consumption."[91] While the Appellate body concluded in this case, as it had in *Reformulated Gasoline*, that the disputed U.S. measures were indeed substantially related

85. *Id.* (citing *Reformulated Gasoline*, Appellate Body Report, *supra* note 82, at 626–29).

86. Appellate Body Report, *United States—Import Prohibition of Certain Shrimp and Shrimp Products – Recourse to Article 21.5 of the DSU by Malaysia*, WT/DS58/AB/RW (Oct. 22, 2001); Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R (Oct. 12, 1998) (*adopted* Nov. 6, 1998) [hereinafter *Shrimp/Turtle*].

87. ANUPAM GOYAL, THE WTO AND INTERNATIONAL ENVIRONMENTAL LAW 160 (2006).

88. *See id.*

89. *Id.* at 161.

90. *Id.*

91. *Id.* at 151 (citing Report of the Panel, *Canada—Measures Affecting Exports of Unprocessed Herring and Salmon*, ¶ 4.4, L/6268-35S/98 (Nov. 20, 1987) (*adopted* Mar. 22, 1988) (GATT)).

to the purported environmental policy goal, the measures were found wanting in other ways.[92] Specifically, the WTO Appellate Body stated unequivocally that there is an obligation on members to pursue " 'serious across-the-board negotiations' " with other members before imposing unilateral trade restrictions that targeted environmental protection.[93] It clarified, though, that these efforts need not necessarily be successfully concluded, the requirement of which would essentially grant veto power to other nations over the implementation of a country's policies.[94]

While far from a victory from the viewpoint of environmentalists, the *Shrimp/Turtle* decisions did provide some reasons to hope that international trade and environmental protection would not always be so deadlocked and working cross purposes, as had been feared in the wake of the *Tuna/Dolphin* dispute. Where the *Tuna/Dolphin* cases were suspicious of the extraterritorial nature of the United States' domestic regulations, the Appellate Body softened its consideration of this issue in *Shrimp/Turtle*, so long as the party imposing the restrictive measure took into consideration the context or prevailing conditions in those nations the measures would affect.[95] Perhaps more importantly, the Appellate Body explained that Article XX(g) should be read " 'in the light of contemporary concerns over the community of nations about the protection and conservation of the environment.' "[96]

In 2000, the WTO Appellate Body shed some light on the "like products" language of the national treatment requirements under the GATT in the *Asbestos Case*.[97] The dispute in the *Asbestos Case* concerned a French decree that effectively placed an import ban on products containing asbestos and the resulting different regulatory treatment of concrete containing chrysotile fibers and concrete reinforced with allegedly similar fibers such as cellulose or glass fibers.

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92. *See Shrimp/Turtle*, *supra* note 86, § 7.50–.60; *Reformulated Gasoline*, Appellate Body Report, *supra* note 82, § IV.

93. SANDS, *supra* note 77, at 972 (quoting Report of the Appellate Body, *United States—Import Prohibition on Certain Shrimp and Shrimp Products—Recourse to Article 21.5 of the DSU by Malaysia*, ¶ 123 [sic]).

94. *Id.*

95. *See id.* at 977 (also noting that the parties must engage in serious negotiation to secure a cooperative solution before resorting to unilateral action).

96. *Id.* at 967 (quoting *Shrimp/Turtle, supra* note 86, ¶ 129).

97. Appellate Body Report, *European Communities—Measures Affecting Asbestos and Asbestos-Containing Products*, WT/DS135/AB/R (Mar. 12, 2001) [hereinafter *Asbestos Case*, Appellate Body Report].

The Appellate Body concluded that " 'likeness' was a 'determination about the nature and extent of a competitive relationship between and among products,' and had to be made on a case-by-case basis."[98] It enumerated four inquiries related to the determination of "likeness" regarding (1) the "properties, nature and quality of the products," (2) the use to which the products are put, (3) consumer perception of the products, and (4) the international tariff classification of the products.[99] The Appellate Body overturned the Panel's decision, conceding the argument of the European Communities in favor of the trade restriction that the disparate health effects of the two kinds of fibers weighed on the "likeness" determination.[100] It thus indicated a willingness to include environmental and health effects into the "likeness" calculus.

Most recently, in the *Retreaded Tires* case, the WTO Appellate Body considered a Brazilian import restriction on retreaded tires from Europe.[101] Brazil urged that the tires posed several environmental and health risks including "the transmission of dengue, yellow fever and malaria through mosquitoes which use tyres as breeding grounds" and the "exposure . . . to toxic emissions cause[d] by tyre fires."[102]

The majority of the dispute concerned the so-called "necessity test." Recall that Article XX(b) excepts the imposition of trade measures "*necessary* to protect human, animal or plant life or health." In the *Retreaded Tires* case, the Appellate Body approached the "necessity test" through three considerations: (1) the contribution of the import ban to the achievement of its

98. SANDS, *supra* note 77, at 975 (quoting *Asbestos Case*, Appellate Body Report, *supra* note 97, ¶¶ 99, 101).

99. GOYAL, *supra* note 87, at 99 (citing Report of the Working Party, *Border Tax Adjustments*, ¶ 18, L/3464 (Dec. 2, 1970), GATT B.I.S.D. (18th Supp.) at 97 (1970)); Report of the Panel, *EEC—Measures on Animal Feed Proteins*, ¶ 4.2, L/4599 (Mar. 14, 1978), GATT B.I.S.D. (25th Supp.) at 49 (1978). *See also Asbestos Case*, Appellate Body Report, *supra* note 97, ¶ 101 (indicating that four criteria for analysis correspond to four categories of possibly shared product characteristics).

100. *See* SANDS, *supra* note 77, at 975.

101. *WTO Finds Brazil Illegally Blocked Used Tires from Europe*, INT'L HERALD TRIB., Dec. 3, 2007, *available at* http://www.iht.com/articles/ap/2007/12/03/business/EU-FIN-ECO-WTO-EU-Brazil-Tires.php.

102. Appellate Body Report, *Brazil—Measures Affecting Imports of Retreaded Tyres*, ¶ 119, WT/DS332/AB/R (Dec. 3, 2007) [hereinafter *Retreaded Tires*, Appellate Body Report] (quoting Panel Report, *Brazil—Measures Affecting Imports of Retreaded Tyres*, ¶¶ 7.109, 7.112, WT/DS332/R (June 12, 2007) [hereinafter *Retreaded Tires*, Panel Report]).

objective,[103] (2) the possible alternatives to the import ban,[104] and (3) the weighing and balancing of relevant factors.[105] In the process of its consideration, the Appellate Body reaffirmed that "it is within the authority of a WTO Member to set the public health or environmental objectives it seeks to achieve, as well as the level of protection that it wants to obtain, through the measure or the policy it chooses to adopt."[106] It went on to find that the import ban imposed by Brazil was necessary to affect its environmental policy goal, and so was provisionally justified under the Article. However, the Appellate Body concluded that the ban was impermissibly discriminatory under Article XX's chapeau after considering the method of implementation, specifically focusing on an exception to the import ban for neighboring countries as well as its effect on the volume of used tires imported into the country.[107]

In the end, though dotted with moments where the WTO regime seems capable of liberalizing its enforcement and contemplating the environmental consequences of free trade, the interpretive history fleshing out the intersection between the WTO regime and environmental protection has been a disappointment for environmentalists almost without exception.

The scope of NAFTA's national treatment requirements is the interpretive history most important for the purposes of this Comment. NAFTA Article 301 incorporates by reference the GATT principles of national treatment and all the interpretive notes, but other national treatment provisions expand the scope of the Treaty to things other than "products" narrowly construed. Specifically, Article 1102 includes "property, *tangible or intangible*."[108]

" 'Modern international practice relating to compensation and restitution clearly admits of a wide definition of property or of protectable interest.' "[109] This may include inquiries into "the 'actual' character of a right (as opposed to potential or

103. *Retreaded Tires*, Appellate Body Report, *supra* note 102, ¶¶ 134–55.

104. *See id*. ¶¶ 156–75.

105. *See id*. ¶¶ 176–83.

106. *Id*. ¶ 140 (citing *Reformulated Gasoline*, Appellate Body Report, *supra* note 82, ¶ 28; *Asbestos Case*, Appellate Body Report, *supra* note 97, ¶ 168).

107. *Retreaded Tires*, Appellate Body Report, *supra* note 102, ¶¶ 151–52.

108. NAFTA, *supra* note 8, art. 1102.

109. Céline Lévesque, *Distinguishing Expropriation and Regulation Under NAFTA Chapter 11: Making Explicit the Link to Property*, *in* THE FIRST DECADE OF NAFTA: THE FUTURE OF FREE TRADE IN NORTH AMERICA 293, 312 n.101 (KEVIN C. KENNEDY ed., 2004) (quoting BEN A. WORTLEY, EXPROPRIATION IN PUBLIC INTERNATIONAL LAW 8 (Arno Press 1977) (1959)).

aleatory) and its durability (as opposed to revocability)."[110] The broad scope "investment" which frames the regime's national treatment and most favored nation requirements has been interpreted just about as broadly as it will stretch.[111]

In *Pope & Talbot v. Canada*, the NAFTA Arbitral Tribunal contemplated a classical essential attributes definition of property considering the owners right to " 'use, enjoy and dispose of the property.' "[112] The tribunal there also considered how the disputed right related to an investment, including its effect on "the control of the investment, the direction of the day-to-day operations, and the lack of interference with management."[113] All of these concerns can be equally applied to carbon credits, and the broad interpretation of "property" does not hint at any reason that this would not be the case were the question brought before the Tribunal.[114]

C. The Principle of Common but Differentiated Responsibilities in the Context of Climate Change Mitigation Efforts

Principle 7 of the Rio Declaration, to which the United States is a party, is often cited as the foundational and even best expression of the notion that states have common but differentiated responsibilities concerning international environmental issues:

> In view of the different contributions to global environmental degradation, States have common but differentiated responsibilities. The developed countries acknowledge the responsibility that they bear in the international pursuit of sustainable development in view of the pressures their societies place on the global environment and of the technologies and financial resources they command.[115]

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110. Lévesque, *supra* note 109, at 312.

111. *See* S.D. Myers, Inc. v. Canada, Partial Award (Nov. 13, 2000), 40 I.L.M. 1408, 1432 (2001) (NAFTA Arb. Trib.) (interpreting investment broadly to include expectations of income or profit). *See also* WOLD ET. AL., *supra* note 72, at 731 (discussing and quoting *Pope & Talbot, Inc. v. Canada*, Interim Award (June 26, 2000), 40 I.L.M. 258 (2001) (NAFTA Arb. Trib.) [hereinafter *Pope & Talbot*]).

112. *See* Lévesque, *supra* note 109, at 313–14 (quoting *Pope & Talbot*, *supra* note 111).

113. Lévesque, *supra* note 109, at 314.

114. *See* discussion *infra* Part V.A–B.

115. Conference on Environment and Development, June 3–14, 1992, *Rio Declaration on Environment and Development*, Principle 7, U.N. Doc.

While the Rio Declaration provides insight into the principle of common but differentiated responsibilities ("CBDR"), the principle's charge lacks substance without application to a specific context or incident of environmental degradation.

The UNFCCC provides exactly that. In framing the world's approach in responding to the daunting issue of global climate change, parties to the treaty agreed to act to protect the climate system "on the basis of equity and in accordance with their common but differentiated responsibilities and respective capabilities."[116] The inclusion of the CBDR principle in the UNFCCC sheds light on just how various nations of the world are expected to perform relative to one another while reducing their greenhouse gas emissions. As one commenter explained:

> [T]he developed country Parties should take the lead in combating climate change and the adverse effects thereof.
>
> The Climate Convention recognizes that all countries are responsible for climate change and should endeavor to limit the pollution that causes it. However, following the CBDR principle, the treaty does not require developing countries to reduce their greenhouse gases. It instead requires the developed countries to take the "lead in modifying longer-term trends in anthropogenic emissions [of greenhouse gases] consistent with the objective of the Convention." Thus, there is a double standard built into the Climate Convention—a double standard that is meant to achieve the Convention's objective of reducing GHGs to manageable levels in ways that are both effective and fair.[117]

A/CONF.151/5/Rev.1 (June 13, 1992), *reprinted in* 31 I.L.M. 876 (1992) [hereinafter Rio Declaration].

116. UNFCCC, *supra* note 2, art. 3(1). *See also* Paul G. Harris, *Common but Differentiated Responsibility: The Kyoto Protocol and United States Policy*, 7 N.Y.U. ENVTL. L.J. 27, 35 (1999) ("The U.S. government has consistently supported common but differentiated responsibility in the context of climate change, despite contrary interpretations in most press reports." (citation omitted)).

117. Harris, *supra* note 116, at 31–32 (alteration in original) (citations omitted). *See also* Phillippe Sands, *The "Greening" of International Law: Emerging Principles and Rules*, 1 IND. J. GLOBAL LEGAL STUD. 293, 311 (1994) ("Under the terms of the 1992 Climate Change Convention, the principle of 'common but differentiated responsibilities' translates into 'specific commitments' on the mitigation of climate change only for developed country Parties and other developed Parties, and differentials in reporting requirements." (citation omitted)).

Article 24 prohibits parties from making reservations to the Climate Convention.[118] What's more, the United States did not submit an interpretive declaration with regard to the meaning of the principle's inclusion or the specific nature of the disparate responsibilities that it structures.

Despite its agreement, the United States has been hesitant to take the lead in reducing greenhouse gas emissions. A primary concern has been the effect binding emissions reduction obligations may have on the national economy, and the possibility that saddling domestic production with mandatory emissions reductions may place it at a disadvantage vis-à-vis developing countries such as China and India who are not burdened by the pressure to internalize the costs of emitted carbon in their production processes. These concerns coalesced into the Byrd-Hagel Resolution in 1997, where the United States Senate,

> because of the disparity of treatment between Annex I Parties[119] and Developing Countries and the level of required emission reductions, could result in serious harm to the United States economy, including significant job loss, trade disadvantages, increased energy and consumer costs, or any combination thereof . . .

resolved that the country should not sign on to any agreement that would "mandate new commitments to limit or reduce greenhouse gas emissions for the Annex I Parties, unless the protocol or other agreement also mandates new specific scheduled commitments to limit or reduce greenhouse gas emissions for Developing Country Parties within the same compliance period."[120] The Byrd-Hagel Resolution thus not only expressed the Senate's concern that binding emissions reductions mandates would put the countries' economy at a disadvantage, it also concluded that the United States should commit to emissions reductions only if developing countries were burdened by similar requirements. The resolution passed by a ninety-five to zero vote.[121]

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118. *See* UNFCCC, *supra* note 2, at art. 24.

119. Annex 1 parties are essentially the set of industrialized nations under the Kyoto Protocol.

120. Byrd-Hagel Resolution, S. Res. 98, 105th Cong. (1997).

121. Byrd-Hagel Resolution Summary & Status, http://www.thomas.gov/cgi-bin/bdquery/z?d105:s.res.00098 (last visited Sept. 18, 2008).

So it would seem that the United States would like the common but differentiated responsibilities of the world's countries to mean that all countries are obliged, at least to some degree, to reduce their greenhouse gas emissions. Indeed, the Senate debate leading up to the passing of the Byrd-Hagel Resolution indicates that most senators embraced the broad outline of the CBDR principle, so long as developing nations had mandatory reduction goals that were pursued alongside U.S. domestic efforts at national regulation.[122] But can wishing make it so? That is, to what extent can statements by the U.S. government influence the interpretation of the CBDR principle in the context of climate change mitigation?

In customary international law, it is often said that a country must consent to a principle in order to be bound by it.[123] Here, the Unites States' presence as a signatory of both the Rio Declaration and the Climate Convention undeniably illustrate the United States willingness to abide by the principle. The question now becomes one of how that principle should affect ground-level activities with respect to environmental policy.

The United States is quick to point out that the requirement that developed nations of the world lead the global community in mitigating global climate change is somewhat qualified in the language of the UNFCCC. Specifically, developing countries committed themselves to develop national climate change policies "with a view to minimizing adverse effects on the economy."[124] However, the list of principles under Article 3 of the UNFCCC includes language that dovetails with provisions governing international trade mentioned earlier:

> The Parties should cooperate to promote a supportive and open international economic system that would lead to sus-

122. *See* Harris, *supra* note 116, at 37–43 (recounting the Senate debate prior to the vote on Byrd-Hagel Resolution).

123. Though some proponents have argued to the contrary, an attempt to show the CBDR principle has risen to the level of customary international law is likely an unsuccessful one: the principle is relatively new to the international law scene, and differentiated responsibilities seem the exception rather than the rule in the international legal landscape. *See* Christopher D. Stone, *Common But Differentiated Responsibilities in International Law*, 98 AM. J. INT'L L. 276, 299–300 (2004) ("The practice of differentiating responsibilities has not, despite occasional claims by its proponents, been elevated to the status of a customary principle of international law. In general, the terms of customary international law and multilateral conventions apply universally. Lack of resources is no more a defense to transboundary pollution or trading in endangered species than it is to abusing ambassadors or practicing piracy.").

124. UNFCCC, *supra* note 2, art. 4(1)(f).

> tainable economic growth and development in all Parties, particularly developing country Parties, thus enabling them better to address the problems of climate change. *Measures taken to combat climate change, including unilateral ones, should not constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade*.[125]

The final sentence, italicized here, is strikingly similar to the language of the GATT Article XX chapeau. However, it is important to note that the language that confines the prohibition on discriminatory measures as between only those countries where like circumstances prevail has been dropped. Since the UNFCCC entered into force, language echoing these principles has appeared in the decisions of the Conferences of the Parties, annual gatherings of UNFCCC members at which the members discuss and evaluate implementation of the Convention.[126]

IV. ISSUES WITH CLOSING THE COMPETITION GAP: MARKET MANIPULATION UNDER INTERNATIONAL TRADE SCHEMES

It has long been the fear of policy makers in the United States that regulating greenhouse gas emissions would place U.S. industries at a disadvantage.[127] Specifically, the worry is that GHG regulations will raise the cost of energy production, which will in turn raise production costs across the national economy. Industries competing with companies that base their operations in a country yet to impose greenhouse gas regulations are suddenly saddled with a competitive disadvantage vis-à-vis their foreign counterparts. This worry has a name: it

125. UNFCCC, *supra* note 2, art. 3(5) (emphasis added).

126. The most recent example can be found in the Bali Action Plan, adopted by the thirteenth Conference of the Parties to the UNFCCC. The Plan outlines those steps the international community will take up until the fifteenth Conference of the Parties to be held in Copenhagen, Denmark, where it is hoped the Parties to the UNFCCC will be able to solidify plans for coordinating the world's greenhouse gas emissions reduction efforts post-2012. Of interest to the instant discussion is language that echoes the principle of common but differentiated responsibilities with respect to market-based future initiatives. The Parties agreed to consider "[v]arious approaches, including opportunities for using markets, to enhance the cost-effectiveness of, and to promote, mitigation actions, bearing in mind different circumstances of developed and developing countries." Conference of the Parties to the UNFCCC, Dec. 3–14, 2007, *Bali Action Plan*, § (1)(b)(v), U.N. Doc. FCCC/CP/2007/L.7/Rev.1 (Dec. 14, 2007).

127. *See, e.g.*, Byrd-Hagel Resolution, S. Res. 98, 105th Cong. (1997).

is China; it is India. As Senator Arlen Specter recently opined before the Senate Finance Committee:

> If new climate change legislation places U.S. manufacturers at a competitive disadvantage compared to producers in countries like China and India that have less rigorous standards, then such legislation may actually *worsen* our climate change problem—and could have devastating consequences for the U.S. economy and our manufacturing sector.[128]

However, the recent sea of change in U.S. politics, and the wave of GHG-regulating laws introduced before Congress,[129] bespeaks a readiness to pass global warming legislation in spite of these concerns. As such, any regulatory scheme may well attempt to offset the perceived burden on domestic production by imposing import duties on certain products from countries not regulating their greenhouse gas emissions, thus placing those products on equal footing in the U.S. market with domestically-manufactured products.

The first problem with this kind of offsetting scheme is one of valuation. The natural method of offsetting is the imposition of a fixed import tax on the products of concern. But how should this tax be determined if its purpose is to offset the burden imposed on domestic production which fluctuates with the emissions credit market? Policy-makers must face the practical problem of matching the tax on foreign goods to the relative disadvantage borne by domestic producers. At least when it comes to their scientific backing, environmentally justified taxes are subject to less scrutiny than restrictive regulations.[130] To that extent, a country may have some leeway in calculating

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128. *International Aspects of Carbon Cap-and-Trade Program: Hearing Before the S. Finance Comm.*, 110th Cong. (2008) [hereinafter *Hearing*] (statement of Sen. Arlen Spector) (emphasis in original), *available at* http://finance.senate.gov/hearings/testimony/2008test/021408astest.pdf (last visited Sept. 18, 2008).

129. *See* PEW CENTER ON GLOBAL CLIMATE CHANGE, ECONOMY-WIDE CAP-AND-TRADE PROPOSALS IN THE 110TH CONGRESS (2007), http://www.pewclimate.org/docUploads/110th%20Congress%20Economy-wide%20CapTrade%20Proposals%2011-2007.pdf (last visited Sept. 18, 2008) (comparing the seven economy-wide cap-and-trade schemes proposed as of Nov. 16, 2007).

130. Andrew Green & Tracey Epps, *The WTO, Science, and the Environment: Moving Towards Consistency*, 10(2) J. INT'L ECON. L. 285, 286 (2007) ("[T]he issue of scientific uncertainty is treated differently depending on the type of policy instrument used by the domestic government. When a government uses a regulatory measure (such as regulatory limits on automobile emissions), it is subject to more rigorous requirements than if the government chooses to use a tax.").

a carbon tax in order to match the burden on importers with that of domestic producers to internalize the cost of their greenhouse gas emissions. Of course, the advantage of this leeway would only be seen—if ever—in the resolution of specific disputes that are sure to follow in the wake of any such tax since it is certain to, at one point or another, inadvertently confer a subsidy to domestic products.

The United Kingdom and France indicated a creative solution to this dilemma when they threatened such offsetting measures against the United States. There, the countries proposed to make importers from polluting nations buy into the EU ETS.[131] Under such buy-in requirements, importers would cover the embedded carbon in their products by purchasing emissions credits on the domestic allowance market, and as a result the importers' burden of internalizing the cost of carbon emissions would be automatically matched to that imposed upon domestic producers. This proposal has gained more than a few followers since it was originally proposed.[132]

A similar requirement was installed in the Lieberman-Warner Bill that is currently pending before Congress.[133] While this solves the problem of matching an offset duty to the burden imposed by the market by simply tying the duty to the market directly, it also puts a country in a quandary as to just how to do it and maintain a distinct regulatory regime. Under the Lieberman-Warner approach, the credits purchased by importers would come from a pool distinct from those established to cover domestic emissions.[134] This way, credits flowing to foreign countries trying to sell on the U.S. market would not interfere with the mechanism set up to facilitate the reduction of domestic emissions; were foreign companies to enter into di-

131. *See* Katrin Bennhold, *France and Britain Ready to Lay Out Eco-Friendly Tax Cuts*, INT'L HERALD TRIBUNE, Nov. 1, 2007, available at http://www.iht.com/articles/2007/11/01/business/france.php.

132. Christian Egenhofer, *Beyond the 'Bali Roadmap': The New International Climate Change Agenda Encompasses Trade*, CENTRE FOR EUROPEAN POLICY STUDIES (CEPS) COMMENTARY, Dec. 21, 2007, http://shop.ceps.eu/downfree.php?item_id=1580 ("It is widely expected that the European Commission's proposal for the revised EU emissions trading scheme will foresee the possibility for such border measures to protect EU industries from 'unfair competition.' ").

133. Darren Samuelsohn, *Baucus Seeks Assurances on Global Warming Bill's WTO Prospects*, ENV'T & ENERGY DAILY, Feb. 15, 2008, http://www.eenews.net/EEDaily/2008/02/15 ("As written, the bill, S. 2191, originally from Sens. Joe Lieberman (I-Conn.) and John Warner (R-Va.), would require the world's major emerging economies to set their own stringent climate policies or purchase allowances in the new U.S. carbon market for their exports to the United States.").

134. Lieberman-Warner Bill, S. 2191, 110th Cong. § 6006(a)(2) (2007).

rect competition for the same credits, the original cap which contemplated only domestic emissions would suddenly seem too stringent.

The Lieberman-Warner Bill further provides that, if the Administrator so chooses, these international credits can be made tradable.[135] It is unclear from the statutory text whether they would be tradable only in a market set up specifically for such international credits, or whether they could be transferred to domestic users to cover domestic obligations.[136] If it is the latter, implementation of these credits must guard against the worry that they would provide another source for domestic emitters to find credits to cover their emissions, thus inadvertently relaxing the burden of compliance, which would slow progress on emissions reductions goals. Specifically, such a trading system might inspire the same kind of speculation or manipulation that has been the basis of some complaints against the Clean Development Mechanism of the Kyoto Protocol: foreign companies could inflate their carbon footprints in order to avail themselves of credits through this process and then decide to sell those credits to domestic companies rather than importing goods under them. If, on the other hand, international credits were tradable only amongst international companies, the mechanism would seem to reinforce the discrimination against foreign market participants, resulting in a higher degree of scrutiny from an international trade panel in the event they are challenged.[137] These worries must be addressed in the implementation of such trading regulations.

A. Article XX Concerns with Trade Measures Targeting the Carbon Footprint of Imported Products

Measures requiring importing companies to cover their embedded carbon not covered in their home countries facially violate the most-favored nation principles of the various international free trade agreements by subjecting the imports of some countries to duties, while allowing others—here, those that regulate greenhouse gases comparably to the United States—to hawk their goods without this burden.[138] The question then becomes whether these measures can be excused un-

135. *See id*. § 6006(a)(5).
136. *See id*.
137. *See* discussion *supra* Part III.B.
138. *See supra* notes 47–49 and accompanying text.

der the listed exceptions under Article XX of the GATT. As the Appellate Body in *Retreaded Tires* noted:

> [The] analysis of a measure under Article XX of the GATT 1994 is two-tiered. First, a panel must examine whether the measure falls under at least one of the ten exceptions listed under Article XX. Secondly, the question of whether the measure at issue satisfies the requirements of the chapeau of Article XX must be considered.[139]

As discussed in Part III.A, the two exceptions under Article XX that contemplate environmental policy goals are XX(b)—measures "necessary to protect human, animal or plant life or health,"—and XX(g)—measures "relating to the conservation of exhaustible natural resources" imposed in parallel with restrictions on domestic trade.[140]

The first question is thus whether such measures are provisionally justified under Article XX(b) of the GATT. The threshold determination here is whether the measures are "necessary" as required by the provision.[141] In *Retreaded Tires*, the WTO Appellate Body outlined the jurisprudential framework guiding this decision:

> [T]he fundamental principle is the right that WTO Members have to determine the level of protection that they consider appropriate in a given context. Another key element of the analysis of the necessity of a measure under Article XX(b) is the contribution it brings to the achievement of its objective. A contribution exists when there is a genuine relationship of ends and means between the objective pursued and the measure at issue. To be characterized as necessary, a measure does not have to be indispensable. However, its contribution to the achievement of the objective must be material, not merely marginal or insignificant . . . .[142]

Whether a measure makes a "material contribution" to the achievement of its policy goal is considered in light of possible alternatives to that measure and whether the measure is a "key component" of a comprehensive strategy or regulatory re-

139. *Retreaded Tires*, Appellate Body Report, *supra* note 102, ¶ 139 (citations omitted).

140. *See supra* Part III.A.

141. *See* GATT 1947, *supra* note 9, art. XX(b).

142. *Retreaded Tires*, Appellate Body Report, *supra* note 102, ¶ 210.

gime aimed at the protection of human or environmental health.[143]

In *Retreaded Tires*, the court held that Brazil's ban on imported tires was necessary to curb "the transmission of dengue, yellow fever and malaria through mosquitoes which use tyres as breeding grounds" and minimize human and animal "exposure . . . to toxic emissions caused by tyre fires."[144] In making this determination, the Appellate Body considered (1) the contribution of the import ban to the achievement of its objective,[145] (2) the possible alternatives to the import ban,[146] and (3) the weighing and balancing of relevant factors.[147]

This Comment now turns to buy-in requirements on imports implemented in parallel with an economy-wide cap-and-trade program: considering whether such measures "materially contribute" to the achievement of the policy-goals behind a domestic cap-and-trade scheme such as the Lieberman-Warner Bill puts the United States in a quandary even at this first step of the analysis. If the objective of the cap-and-trade mechanism is to mitigate climate change writ large, then such buy-in measures significantly contribute to the objective by potentially burdening a large number of otherwise unregulated greenhouse gas emitters with internalizing the cost of the emissions resulting from at least some of their production. Of course, this looks dangerously like extra-territorial regulation, disfavored under international trade law jurisprudence.[148] On the other hand, if the objective of the domestic cap-and-trade scheme is to target only domestic greenhouse gas emissions reductions, as might seem natural, it is difficult to cast parallel measures that burden foreign imports as materially contributing to the achievement of the objective. If domestic emissions are the target of the regulatory scheme, as the argument would likely go, only domestic emitters should be burdened by its requirements.

This concern is not without an answer. The United States can point to the so-called concern of "leakage." Essentially, the United States would argue that without provisions to control leakage, there is no way of ensuring "that [U.S.] policies do not

143. *See id.* ¶¶ 155, 210.

144. *Id.* ¶ 119 (quoting *Retreaded Tires*—Panel Report *supra* note 102, ¶¶ 7.109, 7.112).

145. *See Retreaded Tires*, Appellate Body Report, *supra* note 102, ¶¶ 134–55.

146. *See id.* ¶¶ 156–75.

147. *See id.* ¶¶ 176–83.

148. *See* discussion *supra* Part III.B.

merely push emissions from U.S. facilities to overseas plants."[149] This could happen in two ways. First, regulations that entirely ignore the carbon footprints of imports arguably run the risk of encouraging domestic producers to simply set up shop in foreign countries to avoid the costs associated with that regulation. This version of the concern was voiced early during the negotiations of NAFTA, when commenters worried that trade liberalization under NAFTA would spark a race to the bottom of environmental policies in order to keep operating costs low for local production industries.[150] Happily, though, "[studies . . . suggest] that fears that NAFTA would create a pollution haven for dirty industry in Mexico were not justified overall, though the firms that have moved to Mexico have not always followed environmental best practice."[151] Several recent studies indicate that trade liberalization under NAFTA has not sparked a race to the bottom of environmental policies.[152] While the transparency provisions and environmental protections structured under NAFTA may deserve some credit, a principle reason for this "success" is that the worry was bottomed by an inaccurate picture of corporate decision making. Though there is some evidence that companies actually consider the expense of environmental regulations when considering site placements, the costs of these regulations do not approach the levels required for them to be dispositive in the decision-making.[153] Another factor, distance from target mar-

149. *Hearing*, *supra* note 128, at 12 (statement of Jennifer Haverkamp, Senior Counsel, Environmental Defense Fund), available at http://finance.senate.gov/hearings/testimony/2008test/021408jhtest.pdf (citing the USCAP Call for Action). *See also id.* at 3–5 (statement of Ruksana Mirza, Vice President, Environmental and Government Affairs, Holcim Inc.), available at http://finance.senate.gov/ hearings/testimony/2008test/021408rmtest.pdf (discussing the problem of "leak-age").

150. *See, e.g.*, G. Fredriksson & Daniel L. Millimet, *Is There a Race to the Bottom in Environmental Policies? The Effects of NAFTA*, in THE ENVIRONMENTAL EFFECTS OF FREE TRADE: PAPERS PRESENTED AT THE NORTH AMERICAN SYMPOSIUM ON ASSESSING THE LINKAGES BETWEEN TRADE AND ENVIRONMENT (OCTOBER 2000) 241, 245–6 (Commission for the Environmental Cooperation of North America 2002) (discussing the longstanding concern that NAFTA would spur "capital flight," a companion phrase to "leakage" that highlights the loss of jobs and industry rather than the relaxing of environmental protections).

151. Kevin P. Gallagher, *Free Trade and the Environment: Mexico, NAFTA, and Beyond*, AMERICAS PROGRAM, INTERHEMISPHERIC RESOURCE CENTER, Sept. 17, 2004, at 3, *available at* http://americas.irc-online.org/am/1409.

152. *See, e.g.*, Fredriksson & Millimet, *supra* note 150, at 245–46 (summarizing empirical studies concerning environmental policy change—both in stringency and frequency—at regional and national levels before and since the imposition of the NAFTA regime).

153. *See id.* at 245 (citing J.A. List & C.Y. Co., *The Effects of Environmental*

ket, weighs far more heavily on such decisions.[154] As such, the pressure of capital flight has not been felt with such force as to significantly alter the adoption or revision of regional or national environmental policies.[155]

In the context of climate change, and especially when thinking about companies moving from the United States overseas, regulatory costs may continue to be a low priority consideration since the cost of transporting products back to the United States from foreign production facilities may offset the escaped regulatory costs imposed by a U.S. cap-and-trade regime. If this is true, buy-in measures like those proposed in the Lieberman-Warner Bill could not be said to be "materially contributing" to the reduction of domestic GHG emissions as they would not in fact be protecting against leakage.

The second kind of leakage, which is both more likely and more politically contentious, would result from a simple shift in the buying practices of domestic consumers who may prefer the allegedly cheaper, imported products that do not internalize the costs of their related carbon emissions to domestically produced products. Protecting against leakage of this sort puts the United States in the awkward position of blatantly admitting that the buy-in measures are meant to keep U.S. consumers buying from domestic producers, at least to the extent that they were prior to the implementation of the regulation.

The next step in the analysis—whether such measures can be considered a "key component" of a suite of environmentally protective measures—is also a bit complicated.[156] Many of the same considerations will come to the forefront here as did in the "material contribution" prong, though the arguments may fare somewhat better in this context from the United States' perspective. As with the previous discussion, the measures imposing burdens on foreign importers may be argued to be "key components" helping to ensure that emissions are actually reduced rather than simply moved.

Regulations on Foreign Direct Investment, 40 J. ENVTL. ECON. & MGMT 1 (2000)); Gallagher, *supra* note 151, at 2.

154. *See* Gallagher *supra* note 151, at 2 ("Even at the margin, the costs of pollution control are too small to significantly factor into the average firm's location decisions. In addition, many firms are simply too large and cumbersome to move to another location, and they need to stay close to their product markets. The marginal abatement costs are small relative to the transaction costs of decommissioning and actually moving to another country.").

155. *See id.* at 246.

156. *See* discussion *supra* Part III.B.

As an initial matter, the provisions can be asserted to be strictly necessary to the success of the domestic regulatory scheme.[157] This argument, like the proposed argument to show material contribution, relies on the threat of leakage for its degree of persuasion. The same arguments that may serve to discount the threat of leakage there would work here as well, with perhaps the addition of one: The rhetoric surrounding buy-in measures often justifies their imposition in order to put domestic businesses on a "level playing field" with international competitors.[158] As this reasoning highlights a discrimination between foreign and domestic businesses, it undercuts efforts to establish the measures as providing a key contribution.

Perhaps providing another pathway to show "key contribution," WTO jurisprudence holds that the United States has the "right . . . to determine the level of protection [it] consider[s] appropriate."[159] This fundamental right would give a country some flexibility in the imposition of such measures, allowing the United States to protect the effect of its regulatory endeavors; a Panel or the Appellate Body would likely give a country a good deal of deference on the matter of whether the measures were "key" to the overall regulatory regime.[160] This context is unique, however, as the environmental and human health goal of the policies is not one enjoyed only—or even mostly—by the citizens of the country imposing the measures. Where Brazil imposed the import ban on tires to protect its citizens from disease and toxic fumes, the United States in this case would be imposing import duties benefitting all the world's citizens by leveraging greenhouse gas emissions reductions. This point may well skew the analysis somewhat because it once again colors the measures as blatantly attempting to regulate beyond its borders.

157. *See Hearing*, *supra* note 128, at 12 (testimony of Jennifer Haverkamp) (arguing the central importance of competitiveness provisions "to ensure that America's climate protection efforts are not undermined by other nations' inaction"); *id. supra* note 128, at 2 (testimony of Sen. Arlen Specter) ("Those who suggest some 'protectionist' motive to competitiveness provisions could not be further off the mark. This is about fairness and about whether unilateral, domestic climate provisions can actually work absent binding international agreements.").

158. *Hearing*, *supra* note 128, at 2, 20 (testimony of Jennifer Haverkamp); *Hearing*, *supra* note 128, at 5 (testimony of Ruksana Mirza).

159. *Retreaded Tires*, Appellate Body Report, *supra* note 102, ¶ 210.

160. *See supra* note 143 and surrounding text.

Even if measures requiring importers to cover—in one way or another—the embedded carbon in their products were considered "necessary," there is another hurdle to provisional justification under Article XX(b). Recall that the *Tuna/Dolphin* holdings prohibit the discrimination between like products based on the methods by which they were produced.[161] This issue may rear its head in two ways. To illustrate, consider three imported dress shirts: one from China, one from India, and one from Italy. Say the Chinese and Italian manufacturers run their machinery by tapping in to electric power provided by a traditional coal-fired power plant while the Indian manufacturer is supplied with energy from a newly constructed plant employing carbon capture and sequestration technology recently transferred to the country from the United States. Assuming the three shirts are physically identical, each shirt is nonetheless subjected to different duties upon importation. As the Indian shirt is produced using relatively efficient technology, the importer will have to buy fewer carbon credits to cover her imported products. The Chinese importer would thus legitimately complain that the buy-in requirements discriminated between products based solely on their production methods.[162] Further, the Italian importer, who operates in the shadow of the EU ETS, would not have to cover embedded carbon products upon import since the price of embedded carbon would have already been internalized under the EU trading regime. Both the Indian and the Chinese importers might then object that the buy-in requirements discriminate between like products based on whether or not production is burdened by domestic regulations in their origin country, an arguably procedural distinction.[163]

Daunted by the hurdles to provisional justification under Article XX(b) and hoping to capitalize on some of the rhetoric relaxing condemnation of "extraterritorial regulation" in the

161. *See Tuna/Dolphin I*, *supra* note 78, at 1622.

162. *See Hearing*, *supra* note 128, at 14 (testimony of Jennifer Haverkamp) (implying that the Lieberman-Warner Bill's buy-in provisions do not "suffer[ ] from . . . being a process based regulation").

163. The product/process distinction haunts the imposition of a carbon tax as well as requirements that importers from unregulated countries buy into the emissions credit market. See Green & Epps, *supra* note 130, at 292–93 (noting that some authors argue that a carbon tax would be a permissible discrimination between distinct products (an indirect tax), while others assert that it would be an impermissible discrimination between producers employing different production methods (a direct tax)).

Shrimp/Turtle cases, the United States likely would turn to justifying the buy-in measures under Article XX(g) of the GATT. This approach presents the initial concern of whether a cap-and-trade system for greenhouse gas emissions and parallel market restrictions relate to the "conservation of [an] exhaustible natural resource[ ]."[164]

Such an argument is not without helpful precedent. The Panel sitting on the *Reformulated Gasoline* case held that clean air was an exhaustible resource.[165] As the complaining parties did not raise the issue upon appeal, the Appellate Body declined to consider the question.[166] The key here is the difference between climate writ large and a stable climate. While the former is inexhaustible because the world will never lack a climate in one form or another, the latter is clearly threatened by the continued growth of greenhouse gas emissions.[167] The number of businesses that rely upon a stable climate for their profitability is readily apparent in the preambles of those legislatures that have acted on the issue. For example, in passing the historic Global Warming Solutions Act of 2006, the California legislature found that "[g]lobal warming will have detrimental effects on some of California's largest industries, including agriculture, wine, tourism, skiing, recreational and commercial fishing, and forestry. It will also increase the strain on electricity supplies necessary to meet the demand for summer air-conditioning in the hottest parts of the state."[168]

Another prominent illustration of the business risk tied to climate change is the recent petition to the Securities and Exchange Commission ("SEC") urging the SEC to clarify that existing disclosure laws require the contemplation of climate change risks.[169] The petition spells out a remarkable number of ways in which a business's profitability might be tied to the changing climate (or the changing regulatory landscape).[170] The very fact that there are business risks associated with the

164. GATT 1947, *supra* note 9, art. XX(g).

165. *Reformulated Gasoline*, Appellate Body Report, *supra* note 82, at 612, ¶ vi.

166. *Id.* at 613–14.

167. *See, e.g.*, IPCC, *supra* note 31.

168. Assem. B. No. 32, 2006 Leg., 2005–2006 Sess. § 38501(b) (Cal. 2006), *available at* http://www.arb.ca.gov/cc/docs/ab32text.pdf.

169. *See* Cal. Pub. Employees' Ret. Sys. et al., Petition for Interpretive Guidance on Climate Risk Disclosure 2 (Sep. 18, 2007), *available at* http://www.sec.gov/rules/petitions/2007/petn4-547.pdf.

170. *See id.* at 21–34.

end of the climate system as we know it militates in favor of conceptualizing it as an exhaustible resource.

The two principle requirements of measures seeking justification under XX(g)—combination with domestic regulations and "evenhandedness" in coverage—are readily met by such import restrictions.[171] The buy-in requirements or import duties would only be constructed in parallel with a domestic cap-and-trade regime, and would be part of a comprehensive regulatory effort to affect an environmental policy goal. Further, the buy-in requirement—unlike a fixed import tax—treats foreign products evenhandedly vis-à-vis domestic products because it subjects them to the same regulatory requirements.

However, it is important to keep in mind that, prior to its unilateral imposition of such duties on importers (or restrictions on foreign participation in the domestic emissions credit market), the United States would have a duty to attempt to work something out with the affected nations.[172] The United States may be able to call to the forefront the long history of debate and negotiation under the UNFCCC, which failed to satisfy its own priorities, as evidenced by the nation's refusal to ratify the Kyoto Protocol.[173] If the United States were to take steps now to help ensure that it fulfilled this consultation duty, the restrictive measures aimed at closing the competition gap opened by any national cap-and-trade programs could be provisionally justified under Article XX(g).

Of course, a provisional success means only that the measures reach scrutiny under Article XX's chapeau, which allows measures to be excused under its provisions only if they do not "constitute a means of arbitrary or unjustifiable discrimination."[174] This is a tall order since buy-in requirements or similar measures would be, fundamentally, an attempt to protect domestic production against competitive disadvantage. The inquiry here will be especially sensitive to the *implementation* of the restrictions in light of the purpose of the measures.[175]

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171. *See supra* notes 87–91 and accompanying text.

172. *See supra* note 93 and accompanying text. *See also Hearing*, *supra* note 128, at 13 (Havercamp Testimony) ("If Congress were to adopt it, a [Lieberman-Warner] Title VI-type provision would serve as a backstop—there if we need it (that is, if negotiations or national actions don't lead to serious emissions limits for other major emitters), but ideally, never invoked.").

173. *See, e.g.,* Byrd-Hagel Resolution, S. Res. 98, 105th Cong. (1997).

174. GATT 1947, *supra* note 9, art. XX.

175. *See supra* note 85 and accompanying text.

Some general observations are nonetheless informative. Unlike the import restriction at issue in *Retreaded Tires*, a restriction that requires some importing companies and not others to buy emissions credits to cover the carbon footprint of their products comports with the policy goal of the measures—reducing greenhouse gas emissions through market mechanisms that force internalization of emissions consequences. Where Brazil's exception to its import ban on retreaded tires seemed merely to be playing favorites, importer exemptions to coverage under the cap-and-trade schemes would be available only to those importers who have already covered their greenhouse gas emission under regulations in their home countries.[176] The buy-in provisions thus appear far from "arbitrary or unjustifiable."

Nevertheless, such measures may find themselves in something of a no-man's-land of WTO jurisprudence. Recent testimony before the Senate Finance Committee by environmental groups, market aficionados, and industry interests repeatedly cast the Lieberman-Warner Bill's requirements on importing countries and provisions like them as "encouraging" developing country trade partners to join in the efforts to reduce global greenhouse gas emissions.[177] In *Tuna/Dolphin II*, the WTO Appellate Body expressly held that unilateral measures attempting to influence policy changes in foreign jurisdictions were impermissible under the GATT/WTO.[178] However, "the Appellate Body reviewing the *Shrimp/Turtle* case recognized that unilateral sanctions are inherently designed to influence policy changes in nonconforming nations" and may in some circumstances be justified.[179] Insofar as the latter repre-

176. Under the Lieberman-Warner Bill, for example, an importing company's products could be exempted if the foreign country had taken "comparable action to limit the greenhouse gas emissions of the foreign country." S. 1291, 110th Cong. § 6006(c)(4)(B)(i) (2007) *available at* http://frwebgate.access.gpo.gov/cgibin/getdoc.cgi?dbname=110_cong_bills&docid=f:s2191is.txt.pdf.

177. *See, e.g.*, *Hearing*, *supra* note 128, at 12 (Havercamp Testimony) (noting that "a provision along the lines of Title VI of Lieberman-Warner will need to be integrated into [a domestic cap-and-trade] regime . . . [that] *induces* other nations to join that program") (emphasis added).

178. Sikina Jinnah, Note, *Emissions Trading Under the Kyoto Protocol: NAFTA and WTO Concerns*, 15 GEO. INT'L ENVTL. L. REV. 709, 736–37 (2002–2003) (citing *Tuna/Dolphin II*, *supra* note 79, at 865).

179. *Id.* at 737. Indeed, the Appellate Body noted:

> Conditioning access to a Member's domestic market on whether exporting Members comply with, or adopt, a policy or policies unilaterally prescribed by the importing Member may, to some degree, be a common aspect of measures falling within the scope of one or another of the

sents the more recent and better reasoned conclusion of the Appellate Body,[180] it seems buy-in requirements such as those threatened by the EU or included in the Lieberman-Warner Bill may have a fighting chance under the chapeau analysis. It is difficult to muster much optimism, though, as the history of WTO consideration of trade barriers in the context of environmental protection is a history of disappointment for environmentalists.[181]

These concerns are far from academic. In November, 2007, France and the United Kingdom proposed an array of tax incentives for low carbon products attended by measures to impose carbon taxes on imports from polluting nations.[182] Katrin Bennhold reported that the proposal "could set the scene for a major confrontation between wealthy regions like Europe and the United States and emerging powers like China, India and Brazil, which have less stringent environmental standards."[183] Paolo Mesquita, a Brazilian ambassador to the World Trade Organization, was quoted as saying, "[i]t's not clear how they can do this in compliance with the WTO rules."[184] The legal hurdles to justifying measures aimed at closing any competitive gap created by the imposition of a national cap-and-trade scheme, combined with the apparent willingness of the developing countries to challenge such measures, strongly militates in favor of a proactive effort to address these issues through some sort of international agreement.

B. The Principle of Common but Differentiated Responsibilities as a Limitation on Price-Matching

For many, the Article XX concerns noted above seem to mark the conclusion of the analysis.[185] What's more, those fo-

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exceptions [listed under] Article XX.

Id. (quoting *Shrimp/Turtle*, *supra* note 86, at 38).

180. I say better reasoned here since, as the Appellate Body in *Shrimp/Turtle* noted, construing the Article XX chapeau so as to exclude all unilateral measures targeting foreign policy change would effectively rob the exceptions listed under that provision of any meaning. *See* Jinnah, *supra* note 178, at 737.

181. *See* discussion *supra* Part III.B.

182. Bennhold, *supra* note 131.

183. *Id.*

184. *Id.*

185. *See, e.g., Hearing*, *supra* note 128, at 3 (testimony of Sen. Arlen Spector) (outlining a two-step analysis which first considers the competitiveness provisions under national treatment principles and then turns to the likelihood of an Article XX exemption for those provisions).

cusing on national treatment requirements as they relate to competitiveness provisions conclude that the goal of domestic greenhouse gas reduction policy should be to regulate even-handedly across domestic and importing companies.[186] However, even if buy-in requirements such as those included in the Lieberman-Warner Bill were excused under Article XX of the GATT, it is not clear that such measures could place imported goods on equal competitive footing with their domestic counterparts. As discussed in Part III.C, the United States has consented to the application of the principle of common but differentiated responsibilities in the context of climate change policies.[187] Further, the WTO Appellate Body in *Reformulated Gasoline* indicated that such parallel agreements and other aspects of public international law may be relevant to the determination of trade disputes.[188] In light of the United States' agreement that countries such as China and India should bear a lower burden in tackling a changing climate, so the argument would go, the United States cannot impose an equal burden on importing companies from those countries as it does on its domestic companies. Under this view, the United States would only be able to require importing companies from developing countries to cover *some* but not their entire carbon footprint.

There are several arguments that the United States might put forward to justify buy-in provisions requiring importing companies to fully cover their carbon footprints. First, the United States might point out that, since only the emissions associated with those products imported into the United States would have to be covered under these buy-in requirements, foreign countries subject to these requirements were *de facto* held to a less burdensome standard because the buy-in requirements only cover a portion of the exporting country's greenhouse gas emissions.[189] Furthermore, the United States might argue that its efforts to transfer green technology to developing

186. *See id*. at 4 ("The touchstone will be to ensure that imports are treated no better or worse than domestic products, and that the additional regulatory costs created by this legislation favor neither foreign or domestic production."); *see also id*. at 7 (Mirza Testimony) ("To ensure that leakage protection measures are compatible with WTO rules and the United Nations Framework Convention on Climate Change, this should be implemented through a system of equal rights and equal obligations among domestic producers and importers.").

187. *See supra* note 116 and accompanying text.

188. *See supra* note 83 and accompanying text.

189. Of course, it is fair to ask how true this is, if at all.

countries (if any) take the edge off the imposed measures and differentiate the trade burdens.

Finally, there may be arguments that arise from the details of the imposed scheme. The Lieberman-Warner Bill, for example, sets the price of international reserve credits to never exceed the most recent auction of domestic credits.[190] Thus, if the market functions properly, foreign buyers should be paying the lowest prices to cover their imbedded carbon. The question is whether this price is low enough.

A panel charged with the resolution of a dispute implicating this issue would likely be loath to determine just how differentiated the burdens must be in order to be proper under the UNFCCC. Future action under the UNFCCC may have something to say about this and may guide later decisions on the matter. The Bali Roadmap, agreed to by the Thirteenth Conference of the Parties, laid out a plan to develop the world's next comprehensive and coordinated effort to address the issues posed by a warming climate.[191] Such a set of agreements likely gives more substance to the principle of common but differentiated responsibilities, implementing discrete rights and obligations that flesh out just how differentiated the responsibilities need to be.

V. NATIONAL TREATMENT REQUIREMENTS AND THE EMISSIONS CREDIT AS A COMMODITY

As noted earlier, Marisa Martin has already undertaken to show that brokerage firms may be able to successfully challenge cap-and-trade programs excluding all foreign participation in a carbon allowance market.[192] While this conclusion illustrates how carbon markets intended to be distinct may begin to blur at the edges as allowances are held—at least for a while—by entities beyond the scope of the program, it by no means sounds the death knell of independent regulatory structures. Indeed, despite the EU ETS's exclusion, there is little reason for policy makers to impose such restrictions on who can handle allowances; the participation of foreign brokerage firms

190. S. 1291, 110th Cong. § 6006(a)(3)(B) (2007), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_bills&docid= f:s2191is.txt.pdf.

191. *See* Rachmat Witoelar, President, UN Climate Change Conference, Address to Closing Plenary: The Bali Roadmap (Dec. 15, 2007), http://unfccc.int/files/meetings/cop_13/application/pdf/close_stat_cop13_president. pdf.

192. *See* Martin, *supra* note 13.

does not necessarily frustrate the environmental policy goal of reducing greenhouse gas emissions, though it may complicate emissions tallying or inadvertently increase the likelihood of accidental non-compliance.[193]

There is some dispute as to just how to perceive emissions allowances under the WTO regime, but most of those who have examined the issue declined to call emissions allocations "products" for international trade purposes under the WTO regime.[194] Martin summarizes some of these investigations as follows:

> [Annie Petsonk] argues that emissions allowances as a means of meeting a party's Kyoto obligations likely would be considered a "form of legal tender in satisfaction of sovereign obligations" and not considered a "product." [Jacob] Werksman categorizes emissions credits as "licenses or permits issued by a government authority" and neither a "product" nor a "service." In this sense, licenses to emit carbon could be treated similarly to the transboundary sale of domestic licenses, patents, sovereign debt, or land titles, none of which are covered by WTO rules.[195]

As Martin herself points out, however, WTO jurisprudence is constantly evolving, and it may be unwise to consider this matter decided until the dispute settlement bodies of the WTO face it directly.[196] The argument that foreign carbon emissions allowances are products and thus should be afforded national treatment under domestic cap-and-trade schemes is colorable, if not rock solid, as discussed below in Part V.B.

However, NAFTA adds another dimension to this discussion. While Werksman correctly noted that land titles and the like are not contemplated by WTO rules, recall that NAFTA's Chapter 11 provisions regarding investment *do* contemplate

193. *See* Bluemel, *supra* note 18, at 2032

194. Martin, *supra* note 13, at 446–47. *See also* Steve Charnovitz, *Trade and Climate: Potential Conflicts and Synergies*, *in* BEYOND KYOTO: ADVANCING THE INTERNATIONAL EFFORT AGAINST CLIMATE CHANGE 141, 152 (Pew Center on Global Climate Change 2003), *available at* http://www.pewclimate.org/docUploads/Beyond%20Kyoto.pdf.

195. Martin, *supra* note 13, at 447 (citations omitted).

196. *See id.* at 448 ("While emissions allowances may not fit comfortably into the current conception of 'goods' under the GATT, this should not entirely eliminate the possibility that the notion of 'products' can include something like an emissions allowance. Most WTO provisions are considered 'continuing' ones to be interpreted in an evolutionary manner.").

"property, tangible and intangible."[197] If NAFTA requires that carbon credits be transferrable between Canadian and U.S. emissions credit markets, and the Canadian market is subsequently integrated with the EU ETS, the U.S. system will be vicariously integrated with much larger international efforts. Though many of the details were ignored, the beginnings of these concerns bubbled to the surface when Canada ratified the Kyoto Protocol and first contemplated implementing an emissions trading scheme while the United States stubbornly refused to make headway on global warming policy.

A. The Early Conversations and the Modern Dilemma

NAFTA's Chapter 11 national treatment requirements raised some eyebrows among international trade lawyers when Canada ratified the Kyoto Protocol in December of 2002.[198] In concert with ratification of the treaty, the Canadian government published its Climate Change Plan.[199] The Plan provided for, *inter alia*, the development of an emissions trading system targeting industrial emissions tied to the international emissions trade contemplated by Kyoto.[200]

With Kyoto's ratification supplying the backdrop for investigation, Professor Forcese determined that "[n]ational treatment [has] to be applied in establishing emissions permits and trading systems to reduce emissions by industrial emitters."[201] There was some concern among members of Canada's trade bar that the national treatment provisions might spark trade disputes if Canada set up a trading regime that excluded U.S. companies from participation.[202] In other words, there was some worry that U.S. companies could legitimately complain if they were disallowed from trading on the Canadian market. After all, to disallow U.S. companies from the Canadian market would seem to be to treat foreign investors in like circum-

197. NAFTA Parts IV–VII, *supra* note 8, art. 1139.

198. *See* Craig Forcese, *The Kyoto Rift: Trade Law Implications of Canada's Kyoto Implementation Strategy in an Era of Canadian-U.S. Environmental Divergence, in* THE FIRST DECADE OF NAFTA: THE FUTURE OF FREE TRADE IN NORTH AMERICA 393, 393–94, 417–20 (Kevin C. Kennedy ed., 2004).

199. *See id.* at 397–98.

200. *See id.*

201. *Id.* at 421.

202. *See id.* at 412, 417.

stances less favorably than investors at home by restricting foreign investors' opportunities.[203]

This entire hypothetical, however, was quickly dismissed.[204] First of all, it was unlikely that too many companies would be chomping at the bit to enter such a market voluntarily. Further, even if a company determined that the benefit of being green outweighed the disadvantages of committing itself to regulation—either in the public eye or under a profitability analysis focused on the long term—it is unlikely that the company would feel so compelled to choose Canadian carbon markets as the means to bring a private complaint under NAFTA provisions.

It is worth noting that the set of industrial emitters does not span the space of all companies that might possibly be interested in participating in a newly established carbon market. The regulation of such a common compound as CO_2 inevitably means a lot of business for some companies.[205] Brokerage

203. It is assumed here that competing companies facing one another across the border would be considered to be operating under "like circumstances" within the language of the provision despite the obvious difference that, in this hypothetical, the Canadian companies would be regulated and the U.S. companies would not. Underlying this assumption is the notion that regulation itself cannot be enough to distinguish two groups of investors since NAFTA concerns itself with regulatory asymmetries. A regulatory distinction without something else, the reasoning goes, is not enough.

204. *See, e.g.*, Forcese, *supra* note 198, at 417 (stating that "some members of Canada's trade bar . . . speculated that to the extent emissions trading systems under the Kyoto implementation Plan [might be made] available only to Canadian participants, Chapter 11 national treatment requirements would be violated," but reasoning that, since "[n]othing in Kyoto exempts emissions made by foreign investors in the calculation of a country's emissions reduction requirements," "there [would be] little reason to imagine that the Canadian government would implement an emissions trading system that excluded non-Canadian owned companies"). *But see,* Mark Sills & Ron Ezekiel, *Meeting Canada's Kyoto Commitments: Trade Disputes Ahead?*, ENVTL. FIN., June 2003, at 27 (suggesting that Canada's ratification of the Kyoto Protocol might spur trade disputes or complications with the U.S.). These assessments did not take into account—though probably rightly so—the signing of a non-binding "precedent-setting agreement" by the three NAFTA Parties' Environment Ministers that stated the nations would cooperate in their efforts to reduce North America's greenhouse gas emissions. *See* Press Release, Commission for Environmental Cooperation, NAFTA Environment Ministers Sign Climate Change Agreement (Oct. 13, 1995), *available at* http://www.cec.org/news/ details/index.cfm?varlan=ENGLISH&ID=2389.

205. *See* Elias Leake Quinn, *Market Convergence Through the Back Door: Inadvertent Integration of the World's Carbon Markets under NAFTA*, 2 CARBON & CLIMATE L. REV. 181, 185 (2008); *see also* Sue Asci, *Carbon Trading Set to Expand in U.S.*, INVESTMENT NEWS, Sept. 1, 2008, http://www.investmentnews.com/apps/pbcs.dll/article?AID=/20080901/REG/309019983 ("With a shot at becoming a $1 trillion market in little more than a decade, carbon trading is poised to take a major step forward in the United States.")

firms and the like are perhaps the more likely candidates for challenging their bar from the national market.[206] Indeed, the directive establishing the EU ETS that was organized by the EU to accomplish its collective Kyoto requirements excludes all U.S. companies, including those providing trading services to such brokerage firms.[207] From a regulator's standpoint, though, there is little reason that these companies should be prohibited, as their participation does not interfere with emissions tallies or the environmental goal of industrial emissions reductions.[208]

Another reason that the hypothetical dispute was given short shrift was that there seemed to be no reason for Canada to implement exclusive markets; Canada's motive was compliance with Kyoto obligations, which do not differentiate on just where emissions reductions are affected.[209] The emissions reductions of foreign investors under Canada's market could be calculated toward Canada's obligations, the argument went, so their exclusion would have made little sense.[210]

Thus far, these predictions have proven academic. Canada has yet to structure or implement a domestic emissions trading scheme.[211] The issues sounded anew, though, with the recent release of Canada's new plan to reduce the nation's greenhouse

206. *See*, *e.g.*, Martin, *supra* note 13.

207. *See id.* at 439.

208. *See* Forcese, *supra* note 198, at 417.

209. *See id.*

210. *See id.* This point somewhat belies the complexity of the issues. Allowing foreign investors to purchase emissions credits on a domestic market is not so easily transferred into calculable emissions reductions. Cap-and-trade systems work to reduce emissions through a framework of "carrots and sticks." They provide flexibility for covered emitters to extend their compliance horizons, but closely oversee just how this flexibility is employed to ensure that the emissions reduction goals are not frustrated. Allowing the voluntary participation of companies beyond the reach of enforcement measures or other regulatory "sticks" frustrates the correlation of market participation to emissions reductions. This point, however, was swallowed by the small likelihood that foreign companies would pursue participation in the first place.

211. In fact, Canada has been sued for not complying with its own climate change law—the Kyoto Protocol Implementation Act—which requires that the government publish a climate change action plan and erect substantive regulations on a certain time-table to ensure that the country's Kyoto obligations are met. *See* Press Release, Friends of the Earth Canada, Friends of the Earth takes Federal Government to Court over Kyoto Failure, (June 18, 2008), *available at* http://www.foecanada.org/index.php?option=content&task=view&id=364&Itemid=2.

gas emissions, once again including plans for the development of a cap-and-trade system.[212]

However successful, the former arguments can also be applied to the case where the United States adopts a domestic greenhouse gas trading scheme. There is, however, one significant wrinkle in the analogy. It seems unlikely that the U.S. program will be erected under the auspices of Kyoto or any other international agreement. Instead, the program would likely contemplate only domestic emissions, focusing on a national change rather than leveraging international emissions reduction projects. Even if the scheme allowed companies to earn credits through activities beyond the nation's borders—a domestic Clean Development Mechanism if you will—its cap-and-trade system is likely to be tuned to regulate the U.S. emissions alone, absent a consented-to agreement between the United States and the rest of the world.

The presence of two, side-by-side carbon trading regimes will encourage regulated companies and brokerage firms to push to open opportunities in both markets in pursuit of the best deal, thus increasing the likelihood of disputes. Indeed, U.S. companies have already shown increasing interest in participating in foreign greenhouse gas markets.[213]

If a regulatory dam is broken and, say, the U.S. market is flooded with foreign credits, the policy goal of effecting greenhouse gas emissions reductions may be greatly frustrated. The U.S. market, if set up to be insulated from markets abroad, will be tuned to its industries and its perceived ability to pay. The availability of outside credits will affect an over-allocation of emissions allowances, flooring the price of the credits and so possibly making it less expensive to pay to emit carbon than to increase efficiency or otherwise cut emissions.[214]

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212. *See* News Release, ecoAction, Canada's New Government Announces Targets to Tackle Climate Change and Reduce Air Pollution, (Apr. 26, 2007), *available at* http://www.ecoaction.gc.ca/news-nouvelles/20070426-10-eng.cfm.

213. *See* Martin, *supra* note 13, at 438 (citing Gary C. Bryner, *Carbon Markets: Reducing Greenhouse Gas Emissions Through Emissions Trading*, 17 TUL. ENVTL. L.J. 267, 268 (2004); Michael Northrup, *Leading By Example: Profitable Corporate Strategies and Successful Public Policies for Reducing Greenhouse Gas Emissions*, 14 WIDENER L.J. REV. 21, 29–31 (2004)); Asci, *supra* note 205.

214. The over-allocation worry found flesh, as it were, in the downward price spike and high price volatility in the EU ETS market in April of 2006. There, inadequate emissions inventories led to the inadvertent over-allocation of allowances as policy-makers were forced to guess at actual emissions. *See* International Emissions Trading Association, Position Paper on EU ETS Market Functioning, Oct. 2006, http://www.ieta.org/ieta/www/pages/download.php?docID=

Arguments abound on both sides of the argument as to whether the United States should structure its scheme to insulate itself from other emissions credit markets. Eric Bluemel nicely summarized a number of those factors militating in favor of integration:

> Different liability rules, procedures, and enforcement mechanisms across elemental regimes within a regime complex create opportunities for accidental and intentional noncompliance that are not present in a harmonized global regime. Although ever present, incentives to shirk are heightened in a global warming regime complex where different regimes may be designed to increase wealth transfer or to advance protectionist goals. The reduced transparency and increased complexity of trading across elemental regimes within the global warming regime complex also increase the likelihood of noncompliance by making it more difficult for countries to determine the compliance status of other countries or even their own status.[215]

On the other hand, market fluctuations in foreign regimes may cause U.S. policy makers to hesitate before tying the nation to other systems.[216] After all, the United States has more experience managing cap-and-trade regimes than any other country in the world. If the nation is now going to impose the burden of internalizing greenhouse gas emissions across the economy, why not, say the cautious, keep control over the implementation completely with us here at home? Pragmatic environmentalists, seeing the political difficulty posed by tying domestic emissions reduction schemes with international efforts, urge that the United States should at least get the process started since time is of the essence with climate change mitigation efforts. Act domestically now, they say, and worry about the rest of the international landscape later.

1926.

215. Bluemel, *supra* note 18, at 2032 (citing *inter alia* Brett Frischmann, *Using the Multi-Layered Nature of International Emissions Trading and of International-Domestic Legal Systems To Escape a Multi-State Compliance Dilemma*, 13 GEO. INT'L ENVTL. L. REV. 463, 491–506 (2001)).

216. *See, e.g.*, International Emissions Trading Association, *supra* note 214 and accompanying text.

B. "Product" and "Likeness" Determinations

The central question then becomes whether emissions allocations are "products" for the purposes of the GATT or NAFTA, and, if so, are foreign emissions allowances so alike to domestic ones that (if they existed) they would demand national treatment? While much of this analysis depends upon the characteristics of a specific regime's credits as compared to another's, some broad-strokes observations will be informative.

Turning then to the WTO's perception of emissions credits. Much of the language dealing with products, and many of the opinions construing that language, refer to physical characteristics of the items of concern and generally require physical descriptions of the products. Initially, product-conception of an emissions credit seems unlikely as the emissions allowances are not products in the normal touch-and-feel sense but are instead wholly legal animals, creatures of regulation. However, were a tribunal convinced to peak behind the curtain of the rigorously "thing-a-fying" construction of "product," emissions credits arguably have at least enough product-like qualities to determine whether they are alike or dislike under WTO jurisprudence. Were a reviewing tribunal to find that emissions credits from distinct regulatory regimes were alike for national treatment purposes, it may backfill the product requirement as having been met.

The criteria for analyzing likeness in products consist of: (1) the "properties, nature and quality of the products;" (2) the use to which the products are put; (3) consumer perception of the products; and (4) the international tariff classification of the products.[217]

The "property, nature and quality" of a carbon emissions credit likely consists of its granularity or resolution—the amount of carbon one credit allows you to emit—and its associated registration and authentication procedures. Policymakers and regulatory agencies are loath to reinvent the wheel, so we are likely to see a procedural convergence relating to the registration of emissions and the authentication of emissions credits. The regulatory rigor with which all of these

217. GOYAL, *supra* note 87, at 99 (citing *EEC—Measures on Animal Feed Proteins*, GATT Doc. L/4599- 25S/49, adopted Mar. 14, 1978, § (sic) 4.2). *See also Asbestos*, Appellate Body Report, *supra* note 97, § 101 (indicating that four criteria for analysis correspond to four categories of possibly shared product characteristics).

processes are attended will also factor into the calculus and will be affected by relative funding and administrative prioritization. Credit coverage of carbon emissions in one-ton increments is already an industry standard.[218] All likelihood points to emissions credits of distinct regimes being exceedingly similar in their "properties, nature and quality." In addition, the Appellate Body in the *Asbestos Case* indicated its willingness to contemplate the environmental and health effects of the products before them when making a likeness determination.[219] Since the policy goals behind the allowances are identical and their use would have similar environmental impacts since carbon emission is a global problem, the environmental impact analysis would militate in favor of a likeness decree.

The consumer perception of the products presents an interesting challenge in the context of emissions credits. On the one hand, one could argue that consumers of emissions credits would perceive domestic and foreign credits in much the same way, that is, as methods for covering emissions allocations and reducing compliance costs with implemented legislation. Global climate change and the problem of greenhouse gas emissions is, after all, a global issue, and the regulated gasses are only harmful in the global aggregate.

On the other hand, perception is likely tied to usability. If one regime bans the use of foreign credits to cover domestic obligations, consumers of emissions credits are likely to perceive a difference in the products. In a sense, restrictive regulation may become a self-fulfilling prophesy. Foreign credits will not be treated like products and so are restricted from use, consumers perceive a distinct difference between foreign and domestic credits due to their usefulness under one regime or another, and thus the credits could be held to be distinct products that do not implicate the GATT's national treatment requirements.

The final consideration for likeness under the WTO, the international tariff classification of the product, is probably the greatest obstacle to the assessment of emissions credits as

218. *See, e.g.,* ICECAP, *European Emissions Trading*, http://www.icecapltd.com/ (follow "Our Markets" hyperlink, then follow "European Emissions Trading" hyperlink) (last visited Oct. 18, 2008) (Each allowance represents one unit of carbon dioxide emitted or 1 tonne CO2e—this is called an EU allowance (EUA).); Carbon Planet, Carbon Credits, http://www.carbonplanet.com/carbon_credits (last visited Oct. 18, 2008) ("Each carbon credit is associated with a single tonne of carbon dioxide.").

219. *See Asbestos Case*, Appellate Body Report, *supra* note 97, ¶¶ 114–15.

products, because it would require the affirmative act of adding such objects to the annexes listing the various classifications within the treaty provisions. Were an effort to amend the agreements undertaken, it should be used to cement international consensus on the issue of whether emissions credits are in fact products rather than simply defining their tariff status.

As for the conception of an emissions credit under the NAFTA regime, the question of concern is whether an emissions credit constitutes "property, tangible or intangible."[220] In the first instance, emissions credits permit the immediate actual release of greenhouse gasses into the atmosphere. Their durability is tied to the structure of the regime and the likelihood that a legislature would, after distributing the allowances and setting up the market, regulate the allocations out of existence again. Most cap-and-trade structures will include banking provisions for a term of years, allowing companies to hold on to excess emissions credits for future years in order to extend their compliance horizons under a falling cap.[221] These long-term provisions indicate a durability of the credit and so again urge that the credit be construed as "property."

The classical depiction of property as a right to "use, enjoy and dispose" of something—the definition discussed by the NAFTA Arbitral Panel in *Pope & Talbot*[222]—melds with the emissions allowances in two ways. First, the credit itself can be used, enjoyed, and disposed of in the process of trading it or surrendering it to cover emissions. While the three aspects may seem conflated somewhat in this context, consider a bottle rocket, the undeniable property of my niece: the use, enjoyment, and disposal of the bottle rocket converge in the single event of lighting a fuse.

This definition of property also fits when describing the relationship of the emissions credit to an industrial investment.[223] The right to emit CO_2, one of the most common byproducts of production, is deeply tied to the management and operation of a production facility. Denial of this right affects an owner's right to use, enjoy, and dispose of the production facility itself. Where in *Pope & Talbot* the dispute concerned the license to sell wood beyond a border,[224] here the issue would be

220. *See* NAFTA, *supra* note 8 and accompanying text.
221. *See, e.g.,* Lieberman-Warner Bill, S. 2191, 105th Cong. §§ 2201–02.
222. *See* Lévesque, *supra* note 109, at 313.
223. *See id*.
224. *Id*. at 312 (quoting *Pope & Talbot*, *supra* note 111, ¶ 98).

the right to emit one of the most common side-products of production. The concerns surrounding the effects on installation management and day-to-day operations are obvious in the event that a foreign party involved in an investment could not acquire or transfer emissions credits. Viewed in this light, such a denial might become the province of the expropriation provisions of NAFTA under Chapter 11.

Article 1114 of NAFTA's investment chapter requires that it not be "construed to prevent a Party from adopting, *maintaining or enforcing any measure otherwise consistent with* [Chapter 11] *that it considers appropriate* to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns."[225] Furthermore, the Lieberman-Warner Bill, like the Clean Air Act before it,[226] unequivocally states that "[a]n emission allowance shall not be a property right."[227] Though likely a determinative statement foreclosing any domestic takings claims, this section may not decide the matter with respect to NAFTA provisions. In a strikingly analogous situation in *Pope & Talbot*, the Arbitral Panel had this to say: "While Canada suggests that the ability to sell softwood lumber from British Columbia to the U.S. is an abstraction, it is, in fact, a very important part of the 'business' of the Investment."[228] Under this line of reasoning, a panel might be convinced that the provisions explicitly withholding the "property" descriptor from emissions credits were intended solely to address takings claims brought by companies pinched by the downward ratcheting of the emissions cap and subsequent reduction in available credits.[229]

C. Excusing Restrictions on Foreign Credits and Foreign Participation

In order to stand despite their facial violation of national treatment principles, measures that restrict the transfer and use of like emissions credits from foreign trading schemes will be examined in much the same way as measures adopted to

225. NAFTA, *supra* note 8, at 642 (emphasis in original).

226. *See* Clean Air Act § 403(f), 42 U.S.C. § 7651b(f) (2006) (discussing the nature of allowances allocated under Title IV of the Clean Air Act and stating that "[s]uch allowance does not constitute a property right").

227. Lieberman-Warner Bill, S. 2191, 105th Cong., § 1201(c)(1).

228. Lévesque, *supra* note 109, at 312 (quoting *Pope & Talbot*, *supra* note 111, ¶ 98).

229. This argument is developed further in Quinn, *supra* note 205, at 186–89.

close the competition gap discussed in Part IV.A. There will first be an inquiry into whether or not such measures are provisionally justified under Article XX(b) or (g), and then whether they survive scrutiny under Article XX's chapeau.[230] Many of the same arguments made in the context of product-specific measures will apply with equal force to the context of credit transfer restrictions, with a few noteworthy exceptions.

The restrictions on the use of foreign credits will likely have an easier time meeting the requirements under XX(b).[231] As it is not a restriction on the process of production but on the product itself, the analysis will not be mired by the *Tuna/Dolphin* cases and their progeny.[232] Moreover, in order to pursue a distinct policy goal, a nation must be able confine the number of credits on its emissions trading market to its own emissions reduction goal. To that end, the restrictions make a material contribution to the achievement of the environmental policy goal and are likely to be understood as "necessary" for the protection of human health and welfare.[233]

However, credit transfer restrictions may have an even more difficult time with the chapeau test. Such measures are baldly constructed to protect the vitality of the domestic trading market. It is easy to imagine countries challenging the measures—and, for that matter, a panel charged with resolving the dispute—urging simply that credits are credits, and so long as parties are buying them up to cover their emitting activities, the purpose of the system to facilitate emissions reductions is not being frustrated, at least not on the global scale. It may well be that such foreign participation hampers U.S. bookkeepers, and muddies the tallying of just where the offsets are being counted, frustrating efforts to protect against double-counting. But then, "difficulties related to anticipated administrative problems"[234] were not sufficient to excuse the blanket require-

230. *Retreaded Tires*, Appellate Body Report, *supra* note 102, ¶ 139.

231. *See* GATT 1947, *supra* note 9, art. XX(b).

232. *See Tuna/Dolphin I*, *supra* note 78 and Green & Epps, *supra* note 130 and accompanying text. There may be an argument that allowing the transfer of credits between some markets and not others as may occur under the Lieberman-Warner Bill, § 2501–02, might be construed as the discrimination of carbon credits based on their "methods of production"—here the attendant verification and enforcement provisions. Even if such an analogy were put forward, though, the restrictions would probably be defensible as the differences would be substantial enough to argue that the credits were not "like products," and so the regulatory distinction would be wholly justified.

233. GATT 1947, *supra* note 9, art. XX(b). *See also* discussion *supra* Part IV.A.

234. *Reformulated Gasoline*, Appellate Body Report, *supra* note 82, at 629.

ments the United States pressed in *Reformulated Gasoline*.[235] As such, administrative difficulties are not likely to justify the imposition of buy-in transfer restrictions.

The Lieberman-Warner Bill allows for companies to cover up to fifteen percent of their domestic obligations with credits issued under the auspices of those foreign emissions trading systems that have been certified by the Administrator of the EPA.[236] While a system which limits but does not wholly prohibit the transfer of foreign credits is somewhat less suspect under Article XX, the provision may nonetheless be construed as a quantitative restriction on the import of foreign allowances.[237] To a certain extent, certifying foreign emissions trading markets as compatible for transfer—presumably the result of an inquiry into the validation and enforcement protocols of those credit systems—looks a lot like a concession that credits from those markets are in fact "like" those allocated under the domestic program. It begs the question (one sure to be asked by more than a few companies depending on which market has the cheaper credit prices): why only fifteen percent? Allowing any transfer of credits between markets will require tracking of credits and management of the market, if only to ensure traded credits are fungible. If the purpose of the system is to bring market forces to bear on the emission of greenhouse gases, so the argument would go, why not open the doors and really let the market do its job?

The United States can respond to these concerns by noting its significant domestic interests in requiring the lion's share of greenhouse gas emissions reductions achieved by its countries' investments be within its territory. After all, those sources that emit greenhouse gases are also often responsible for the emission of a number of other regulated pollutants.[238] Of

235. *Id*. at 629–31.

236. *See* Lieberman-Warner Bill, S. 2191, 105th Cong., §§ 2501–02.

237. *See* GATT 1947, *supra* note 9, art. XI (prohibiting quantitative import and export restrictions).

238. *Compare* EPA, *Inventory of U.S. Greenhouse Gas Emissions and Sinks: 1990–2006,* Executive Summary at 23, *available at* http://www.epa.gov/ climatechange/emissions/downloads/08_ES.pdf, (listing a number of sources of greenhouse gas emissions including coal-fired electricity generation, motor vehicle emissions, and a number of other industrial sources), *with* EPA, *Mercury: Basic Information*, http://www.epa.gov/mercury/about.htm (last visited Mar. 12, 2008) (noting that "[c]oal-burning power plants are the largest human-caused source of mercury emissions to the air in the United States"); EPA, *SO_2: What Is It? Where Does It Come From*, http://www.epa.gov/air/urbanair/so2/what1.html (last visited Sept. 16, 2008) (noting that fuel combustion electricity generation accounts for a

course, the United States regulates those other compounds separately, and it is unlikely that discriminatory measures would be upheld in order to protect secondary benefits directly under the control of other regulatory programs.

VI. CONCLUSION

In the final analysis, these intersections of international trade law and greenhouse emissions trading schemes by no means doom domestic attempts to implement global warming policies. Rather, they militate in favor of attempting to deliberately place these policies in the international law landscape through the pursuit of parallel international agreements. The inclusion of emissions credits to the list of products or services exempted from national treatment and most-favored nation principles under NAFTA would prevent the inadvertent integration of a U.S. scheme with foreign systems in the event that Canada set up its own cap-and-trade program under Kyoto and tied it to, for example, the EU ETS. Agreements establishing emissions reduction obligations for those countries upon which the United States would impose import duties or carbon-market buy-in requirements would solve the open question of just how the principle of common-but-differentiated responsibilities should be fleshed out in practice.[239] While these international efforts ought not be lost in the process of setting up a domestic regulatory—indeed, they play may an integral part in ensuring such a program's success—there is also no reason to further delay domestic action.

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majority of domestic SO_2 emissions); EPA, *Ground-level Ozone*, http://www.epa.gov/air/ozonepollution/index.html (last visited Nov. 3, 2008) ("Motor vehicle exhaust and industrial emissions . . . emit NOx and VOC that help form ozone.").

239. It is important to keep in mind that the United States must at least attempt to do this if it wants to be able to argue that such measures are excused under Article XX(g) of the GATT. *See* SANDS, *supra* note 77, at 971–72.