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NAFTA shadow hangs over Kyoto

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Canada's new Kyoto strategy is a positive step to encourage business participation in reducing greenhouse gases. However, it does not address the fact that Kyoto and NAFTA are on an ideological and legal collision course.

Kyoto's provision of credits for emissions reductions are market- and trade-based, and, as such, will be accountable under NAFTA guidelines. This opens the door for countless legal challenges that can potentially undermine Kyoto. It is critical the government take preventive steps now before Canada's long-term trade and environmental objectives are compromised.

Kyoto and NAFTA are classic examples of international agreements that seek to encourage participation by giving signatories a competitive advantage through economic incentives.

Canada and Mexico are parties to both agreements, but the United States has not agreed to sign on to Kyoto. The U.S. position against Kyoto leaves open the potential for NAFTA to be used as a tool to prevent Kyoto's implementation.

As well, there are contradictions between NAFTA and Kyoto that open the possibilities of legal challenges to the accord.

NAFTA guarantees foreign investors equivalent status for investment and trade: No individual investor can have a competitive advantage over another unless explicitly stated in the agreements. As a result, the special-trade status guaranteed among the three NAFTA countries may conflict with the privileged position of Mexico and Canada through Kyoto.

For example, a U.S. investor could use a section of the NAFTA agreement known as Chapter 11, to argue that investment conditions in either Canada or Mexico as a result of Kyoto effectively discriminate against free trade. A legal challenge could be launched under NAFTA's arbitration process that would threaten to undermine the whole purpose of the Kyoto Protocol.

Fundamental to Kyoto is the successful integration of trade with heightened protection of the environment. NAFTA holds similar aspirations, but specifies that any environmental measure must be consistent with Chapter 11 rules.

For example, foreign investors cannot be discriminated against solely for environmental reasons unless a direct link with human, animal or plant health is established. This link must be reinforced by hard science.

While greenhouse gases have been shown to impact health and climate, there is still debate over whether society is producing dangerous enough levels to warrant action.

To facilitate the gradual reduction in greenhouse gas emissions and the associated costs, Kyoto proposes a complex series of credits that can be exchanged between investors and countries in an effort to promote trade and environmental protection. It is these credits that will be awarded by Kyoto that could be viewed as an unfair competitive advantage through Chapter 11 and trigger a legal challenge.

Under Kyoto, American investors can only receive credit for emissions reduction activities and investments in Canada or Mexico.

They could argue that they are being required to use or give a preference to goods produced or services provided in Mexico or Canada. Americans could seek compensation from Ottawa for imposing a performance requirement and taking measures "tantamount to expropriation."

There is evidence that companies will resort to such legal recourse.

S.D. Myers, an American company, successfully challenged Ottawa over conditions on PCB exports. They used the same clause in Chapter 11 to prosecute for equitable rights for goods and services in the two countries.

Unless the Canadian government accepts the potential of these challenges, the very substance of Kyoto is at risk.

Canada could broker a NAFTA exemption of the Kyoto Protocol. This has already been done for other agreements.

The federal government has also been delinquent on another count: So far the government has not specified how American investors might participate in emissions reduction activities and receive credit through the national emissions credit registry.

If Ottawa does not allow American investors to hold an account or participate in this way, it would be a further violation of Chapter 11 clauses that ensure equitable treatment and bring forth a challenge on different grounds.

If the Canadian government is serious about Kyoto, then it has to make Kyoto and NAFTA consistent rather than let the debate focus on secondary matters such as meeting emission targets.

The time to act is now. Turning a blind eye to these problems will almost certainly ensure that Canada will fail to live up to the spirit of both NAFTA and Kyoto.

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