THE *KYOTO PROTOCOL* AND EARLY ACTION

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I INTRODUCTION

In early June of this year, an Australian forestry company, Australian Plantation Timber ('APT') sold a AUD$1 million option to purchase the carbon sequestrated from 5 092 hectares of its plantations in Western Australia to Cosmo, one of Japan's major oil companies. If Cosmo exercises its option between now and 2012, APT may earn up to an additional AUD$35 million.[1] At the formal signing ceremony of the transaction, Gwen Andrews, Chief Executive Officer of the Australian Greenhouse Office and representative of the Australian Government, acknowledged the Government's strong support for the transaction and the important role of the private sector in helping to implement the principles of the *Kyoto Protocol to the United Nations Framework Convention on Climate Change* ('*Kyoto Protocol*').[2]

The APT-Cosmo deal is the latest example of the willingness of private companies to implement measures that are clearly consistent with the fundamental principles of the *United Nations Framework Convention on Climate Change* ('*UNFCCC*')[3] and the *Kyoto Protocol* through utilising the marketplace mechanisms that these instruments formally create. Despite the current positioning of the Bush Administration, the uncertainty over the *Kyoto Protocol* and even the occasional lingering challenges to the science of climate change, there is an ever-increasing willingness on the part of many corporations to take early action to reduce the levels of their greenhouse gas emissions.

This is not to say that all companies are of like mind. In fact, some continue to oppose the *Kyoto Protocol*, others take no action at all, and those who choose to do something often do so only on a token basis. However, for corporations such as Cosmo and APT, BP Amoco ('BP'), Shell, Ontario Power, DuPont, General Motors Holden, Toyota and Ford, the development of regulatory frameworks to reduce global levels of greenhouse gas emissions has not only encouraged early

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1 Australian Plantation Timber, *Australian Company Pioneers International Carbon Trading Market*, Press Release (6 June 2001).

2 Opened for signature 16 March 1998, 37 ILM 22.

3 Opened for signature 4 June 1992, 31 ILM 849 (entered into force 21 March 1994).

action to deal with future potential business risks and liabilities, but has also presented significant opportunities. As a consequence and perhaps for the first time in the development of international environmental law, companies and countries are taking action to implement the general principles of the *Kyoto Protocol* despite the absence of any concluded legally binding regime.

II CORPORATE ENGAGEMENT IN THE DEVELOPMENT OF INTERNATIONAL REGIMES

Climate change has clearly been recognised as a global issue, the impacts of which cross national boundaries. Solutions must come through the international cooperation of sovereign states to regulate the activities of those private nationals and corporations that are primarily responsible for greenhouse gas emissions and are engaged in business within their jurisdictions. The negotiation of the *Kyoto Protocol* as an instrument of international law attempts to engage both states and private corporations in developing global climate change solutions.

The evolution and development of public international law has traditionally taken place in the absence of private sector participation. Sovereign states enact international treaties and create state practice. They negotiate sovereign obligations with little or no private sector involvement in the design of international regimes. It has only been when states develop domestic implementing legislation that the real involvement of the private sector begins.

However, over the last decade, the involvement of the private sector in many international issues has increased significantly, especially in the intersection between trade and the environment. Reasons for this include:

(1) the increasing impact of global corporations on the environment, especially in terms of cross-border pollution;
(2) the increasing ability of global corporations to influence global environmental policies and outcomes;
(3) the growing willingness of international civil society to challenge the actions of multinational corporations;
(4) the growing corporate recognition of the sector's responsibility for environmental issues;
(5) the use of market-based mechanisms to influence corporate behaviour; and
(6) the movement towards framework agreements that provide broad principles for dealing with global environmental issues, which principles are then developed through ongoing negotiation.

The increasing private sector involvement in the international negotiation process provides the opportunity for corporations, non-government organisations and communities to become engaged in issues as they are developing. It has also led to a bridging of the traditional gap between private sector governance and the development of international environmental law regimes.

III EARLY CORPORATE ACTION TO IMPLEMENT THE PRINCIPLES OF THE *KYOTO PROTOCOL*

The international participation of the private sector is most obvious in the area of climate change, where the fulfillment of states' binding treaty obligations to reduce levels of greenhouse gas emissions is almost entirely dependant upon those obligations being passed on to private corporations. Effectively this means that we are seeing the development of international legal rules that directly regulate corporations, ensuring a far greater corporate interest in their development.

As the international community continues to negotiate the international climate change regime, the corporate sector has been actively engaged in the design process through the active lobbying of governments. There is little doubt that the current position of the Bush Administration reflects the attitudes of those key oil companies involved in the Bush election campaign. These attitudes are to be compared to those held by other companies in the United States ('US') which encouraged the Clinton Administration to endorse the *Kyoto Protocol*.

In addition to their participation in international negotiations, many corporations have already taken significant voluntary early action by taking steps to reduce greenhouse gas emissions, by pursuing emission reduction projects, and by developing legal precedents and rules in the hope that these will be adopted by states as international and domestic regimes are developed. These corporations are effectively implementing the general objectives of the *Kyoto Protocol*. This is most obvious in areas where market-based incentives offer real opportunities for the private sector.

The *Kyoto Protocol* allows for the creation of 'carbon credits' from emission reduction or removal projects – including forestry operations – and from Clean Development Mechanism ('CDM') and Joint Implementation ('JI') projects. Already we have seen Australian companies such as APT and State Forests of New South Wales enter into carbon trades with Japanese buyers, while others such as Orbital Engine Corporation and AGL have been actively pursuing clean development projects in China and South America respectively, with a clear aim of selling the emission reductions. These activities and trades are taking place despite the fact that the carbon trading, CDM and JI market mechanisms of the *Kyoto Protocol* are not yet in force.

Furthermore, we have seen the emergence of a range of private global emissions trading companies such as CO2e.com and Natsource, which aim to facilitate global carbon trading as envisaged under art 17 of the *Kyoto Protocol*. The establishment of the Green Electricity Market in Australia to facilitate implementation of the Federal Government's renewable energy legislation is another example of a private 'market maker' at work.

Obviously, for many of these companies the *Kyoto Protocol* and the regimes being developed under it provide significant opportunities. For forestry companies, the ability to trade carbon from their plantations under the *Kyoto Protocol* principles provides an additional source of revenue. This also applies to companies with cleaner and renewable technologies.

While the emerging regimes provide clear market incentives for these new environmental products, there has also been a rapid emergence of carbon finance from both governments and the private sector to support the development of new technology. The Australian Government's Greenhouse Gas Abatement Program specifically funds projects that reduce greenhouse emissions. In the private sector, there has been an emergence of private investment funds focused solely on emission reduction projects and new energy technology. Merrill Lynch's new Energy Technology Investment Trust, which is traded on the London Stock Exchange, is one example of a fund specifically designed to take advantage of the global investment opportunities in the alternative energy and energy technology sectors.

It is not only companies that grow trees or produce more energy efficient products that are pursuing initiatives under the *Kyoto Protocol*. The key players to date have included General Motors, Ford, Shell and perhaps most notably BP. For companies such as General Motors and Ford, climate change presents an opportunity to gain advantages over their less technologically sophisticated rivals. By investing in cars that run on a combination of fuel and battery power or fuel cells which do not produce carbon dioxide, these companies have an opportunity to dominate the new market and squeeze out smaller competitors for whom the required investments would be too great.

In the case of Shell, its significant investment in new divisions including Shell Renewables, Shell Hydrogen and Shell Forestry all demonstrate a diversification of the corporate portfolio in a way that is specifically linked to the *Kyoto Protocol*. This is further reinforced by Shell's decision to review every new project in terms of its potential carbon liabilities, and by its announcement a few weeks ago confirming that it will invest between US$500 million and US$1 billion on developing new energy businesses over the next five years.

Like Shell, BP has been the other – perhaps the most prominent – corporate leader in the climate change area. Having recently changed its image to 'Beyond Petroleum', BP has marketed itself as a global energy company with a specific emphasis on dealing with climate change. Over the last few years it has announced voluntary cut backs in its own carbon dioxide output, promising that its emissions of greenhouse gases in 2010 will be 10 per cent below its 1990 levels, even though the company expects its output and sales to be roughly 50 per cent greater in 2010 than they were in 1990. To help reach the announced goals, BP has established an in-house carbon dioxide trading program that requires business units to buy and sell credits in order to meet their allowed emission levels. In Australia, BP is also the first participant in the 'greenhouse friendly – greenhouse free' initiative in which revenues from sales of its cleaner fuel are specifically directed by the Commonwealth Bank into cleaner energy projects.

While the Chief Executive Officer of BP, John Brown, and other executives do not necessarily expect customers to switch their business from other oil companies (at least in the short term), they admit that they do not know exactly what the carbon dioxide reductions will cost the company. Nonetheless, they have stated publicly that they are confident that their commitment is sensible and that they believe that taking a leadership position on climate change gives the company a distinctive edge in the eyes of government officials, scientists and environmental groups. It is also believed that such a commitment may give BP better access to government-controlled oil deposits and more operating flexibility. By experimenting with emissions trading, BP is also likely to have more clout at the negotiating table when international regulatory frameworks are being devised, as was the case with the United Kingdom's emissions trading scheme.[4]

Significantly, such initiatives have not been limited to the private sector alone. Perhaps the two greatest participants in early carbon trading have been the World Bank and the Dutch Government. Through its Prototype Carbon Fund – in which a number of major companies including Deutsche Bank, Mitsubishi, Tokyo Electric Power, BP, Chubo Electric Power, Electrabel, and Gazdde France have invested – the World Bank acquires emission reductions from approved projects in developing countries. At a domestic level, the Dutch Government's Emission Reduction Unit Procurement Tender ('Eru-PT') Fund has already concluded contracts to purchase around 4.2 million tonnes worth of greenhouse gas emission reductions from projects in Eastern European countries for an amount of US$31.6 million.

It is clear that the significant actions being taken by many private companies – either directly or in association with multi-lateral agencies and domestic governments – are well ahead of the political negotiations designed to finalise the *Kyoto Protocol.* While for some companies early action has already provided significant revenue flows through the sale of emission reductions, many others hope that early action will allow them to influence the way in which the rules are developed, to increase public confidence in their companies and to escape what may otherwise be more onerous obligations in the future.

Even in the US, where the Bush Administration continues to oppose *Kyoto Protocol*, many US corporations continue to undertake action to reduce levels of greenhouse gas emissions. For example, a coalition of energy companies including Enron, El Paso, Calpine, Trigen and Nisource have all recently come out against the Bush Administration's rejection of the *Kyoto Protocol* and have instead endorsed a program to reduce the levels of their carbon dioxide emissions. The even more recent launching of a voluntary pilot emissions trading program for the Mid-West US, which involves many of the major energy utilities, further demonstrates the intention of many companies to continue to act in accordance with the principles and objectives of the climate change negotiations, despite the position of their own National Government.

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4 See Kimberley O'Neill Packard and Forest Reinhardt, 'What Every Executive Needs to Know about Global Warming' (2000) July-August *Harvard Business Review*, 133.

IV CONCLUSION

Irrespective of the way in which the international negotiations over the *Kyoto Protocol* evolve, it is clear that a significant shift is taking place in the behaviour of many corporations, which either see new opportunities or wish to limit the liabilities which may arise under the *UNFCCC* and the *Kyoto Protocol*. In many cases, the corporations who are taking action are 'making the market' by establishing early precedents and placing themselves in an excellent position to influence policy debate in a way not previously possible in the context of international negotiations. As scientific and public opinion continues to harden we are likely to see increasing pressure placed on corporations to take action and the emergence of a variety of reward systems for early movers. The recent boycott by both Greenpeace and other companies of Exxon-Mobil in Europe for its failure to address climate change issues may well be indicative of future trends.

It is perhaps somewhat ironic that one of the Bush Administration's key reasons for rejecting the *Kyoto Protocol* is that it would cause serious harm to the US and the global economy. As Jan Pronk, Chairman of the Sixth Conference of the Parties to the *UNFCCC* recently noted, 'there is wide agreement that the necessary technology to address climate change is available already. It doesn't have to be invented, it only has to be applied'.[5] Calculations from the international scientific and economic community show that the costs involved in meeting climate change are affordable, that the short-term retrogression of economic growth will be minimal, and that addressing climate change will ensure that long-term economic growth is sustainable. As Pronk notes, the costs of non-action are much greater.[6] The economic damage from climate change through related natural disasters is already tremendous and will mount further. Some countries may be able to protect themselves against such consequences but run the risk of slowing down their long-run economic growth. In effect, acting on climate change does not threaten global or domestic economies; it simply guarantees growth for future generations. Despite the criticisms by some that companies taking early action are little more than opportunistic, it is clear that their actions are a critical part of the international effort to reduce global greenhouse emissions and assist in changing corporate attitudes.

5 Jan Pronk, (Speech presented at the Equity and Global Climate Change Conference, Washington DC, 17 April 2001) <http://www.pewclimate.org/events/pronk.cfm> at 3 June 2001.

6 Ibid.