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Winning the Greenhouse Gas Game

by Andrew Hoffman

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Greenhouse gas regulation may seem like a distant threat, but corporations are already maneuvering to make sure that the rules, when they come, will fall in their favor. Nearly 60 companies, including DuPont, Shell, Alcoa, Weyerhaeuser, BP, Motorola, and American Electric Power, are pursuing voluntary emissions targets. In the process, some of these companies—a group whose combined net sales top $1.5 trillion—are gaining expertise that will help them win advisory roles in policy development and give them negotiating clout as governments shape the rules. (See the sidebar "The Road to Regulation.")

Crucially, these companies are becoming savvy emissions traders. Emissions trading, employing so-called "cap and trade" schemes, is a technique for playing in what amount to commodity markets for buying and selling the right to generate pollutants. This practice is certain to be an important component of emerging greenhouse gas policies. If regulators put a ceiling on the allowed emissions of, say, methane, and your company produces more than that amount, you'll be able to buy credits from a company that emits less than the permitted maximum. Conversely, if you reduce emissions below the regulated limit, you can be the one to sell credits. Companies that know how to play the emissions trading game will be well positioned to influence policy as it develops and react to it once it's in place.

BP, for example, already has five years of experience in emissions trading, having launched an experimental intracompany market in 1998 that allows business units to buy and sell cred-

The Road to Regulation

Although the Kyoto Protocol, the global treaty that would limit greenhouse gas emissions, has yet to be ratified, some form of regulation seems inevitable. Internationally, the Kyoto Protocol must be ratified by at least 55 countries, including those responsible for 55% of the world's emissions, before it can go into effect. The first part of that requirement has already been met—120 nations have ratified the treaty. The second awaits a decision from Russia, which produces 17.4% of global greenhouse emissions. At present, only two developed countries, Australia and the United States, have opted not to participate. But regardless of the fate of the Kyoto Protocol, participating countries and regions, including the European Union, Britain, Canada, Denmark, and even China, have already started developing their own regulatory programs to control emissions of these gases.

Though the current U.S. administration is unenthusiastic about greenhouse gas regulation, momentum is building for a federal program. Nearly 45 relevant bills have been put forward in Congress; most recently, a bill proposed by Senators John McCain and Joe Lieberman reached a vote in the Senate. Although the bill was defeated, the vote approached an even split: 55–43 against adoption. When the Senate last voted on the Kyoto Protocol, in 1997, the tally was 95–0 against. Bills proposing regulatory schemes are clearly evolving in ways that are satisfying policy makers.

Even without Congressional consensus, many U.S. states have pressed on with initiatives of their own. California created the nation's first bill to regulate carbon dioxide emissions from automobiles by the 2008 model year. Ten northeastern states announced their intention to come to an agreement by April 2005 on a plan for a regional system that would limit carbon dioxide emissions from power plants. The New England states and eastern Canadian provinces have adopted a plan to reduce their greenhouse gas emissions to 1990 levels by 2010 and even lower levels later, and Maine has put this goal into law. New Jersey has pledged to reduce statewide emissions by 3.5% from 1990 levels by 2005 and has signed agreements with its biggest utility and 56 colleges and universities to reduce emissions to below 1990 levels. And the state of Washington has recently announced its intent to join Oregon and California in pursuing greenhouse gas reductions.

its among themselves (see the article "Bringing the Market Inside" by Thomas W. Malone in this issue). BP's expertise in cap and trade earned the company an advisory role in designing the British greenhouse gas Emissions Trading System. And Shell's experience with its own emissions trading landed it an advisory role in developing the EU's Emissions Trading Directive, due to go into effect in 2005.

If your company hasn't yet formulated a greenhouse gas strategy, consider the following questions:

- What is the energy efficiency of your operations, and can you improve it?
- Do you know how to measure your company's production of carbon dioxide and other greenhouse gases (methane, nitrous oxide, hydrofluorocarbons, perfluorocarbons, and sulfur hexafluoride)? If so, how much greenhouse gas does your company produce in processes and products, and what are the sources?
- Do you know the available technologies or alternatives for reducing emissions or for improving energy efficiency? Do you know the cost/benefit trade-offs associated with each?
- Do you know how to conduct commodity trading of greenhouse gas emissions?
- How will any new facilities you build accommodate future greenhouse gas regulation?
- How will you assess the greenhouse gas liability of any capital assets you intend to buy or sell?
- How will you monitor and forecast the development of greenhouse gas regulations?
- What will be the impact on your business if greenhouse gas limits are imposed?

If you can't readily answer these questions, your company is in a risky position. Finding the answers is a good way to start shaping a sound strategy.

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