

EXECUTIVE OFFICE OF THE PRESIDENT  
THE UNITED STATES TRADE REPRESENTATIVE  
WASHINGTON, D.C. 20508

MAR 04 2008

Chairman Rick Boucher  
Committee on Energy and Commerce  
Subcommittee on Energy and Air Quality  
2125 Rayburn House Office Building  
Washington, DC 20515

Dear Chairman Boucher:

There can be little doubt that climate change is one of the most serious challenges we face as a nation. USTR officials are not the experts on substantive climate change negotiations or policy. But we assure you that we are interested in working with you to advance your goal, as stated in the cover letter to your white paper, "to encourage developing countries to curb their greenhouse gas emissions."

We strongly believe that trade policy can play a positive role in advancing our environmental goals, including in addressing climate change. USTR has sought out and pressed hard for "win-wins" that will leverage trade liberalization to promote good environmental outcomes. Most recently, and most directly relevant to the climate challenge, the United States and the European Union jointly made a groundbreaking proposal in the World Trade Organization (WTO) to remove barriers to trade in a number of environmental technologies that are critically important for mitigating climate change. The proposal calls for early action to remove tariffs and non-tariff barriers on "climate-friendly" technologies that could increase related trade by as much as 14 percent, according to the World Bank, and lays the foundation for a new broader environmental goods and services agreement (EGSA).

In this, and in other areas, we have done much to promote mutually supportive trade and environment policies. Against that background, let me turn to some of the trade-related issues that are now being discussed in connection with proposed climate change legislation.

We have heard a lot about the important role developing countries will need to play in any new international climate change regime, and we agree that their role is important and critical in order to truly address the global nature of climate change. Our overriding goal should be to bring developing countries into a global system in which they do their part to limit greenhouse gas emissions. How best to do that is a complex issue.

For instance, we have serious concerns with some ideas that are currently circulating – particularly the enthusiasm for using import provisions that might be perceived as unilateral trade restrictions directed against other countries to push them to move rapidly to reduce their emissions of greenhouse gases. We believe that this approach could be a blunt and imprecise instrument of fear – rather than one of persuasion – that will take us down a dangerous path and adversely affect U.S. manufacturers, farmers and consumers. It is no accident that trade ministers in Bali unanimously agreed that trade restrictions run the risk of tit-for-tat retaliation and even an all-out trade war where no one wins and everyone loses. My trade counterpart in Europe, Commissioner Peter Mandelson, strongly cautioned against including trade restrictions in the European Commission's recent package of proposals setting out the second phase of its emissions cap-and-trade system – resulting in the omission of these measures.

There are a number of important questions that need to be raised about the implications of utilizing import measures to address competitiveness concerns or perceived failures on the part of other countries to address climate change. I trust that Congress will ensure careful consideration of the implications associated with drafting provisions that would apply with respect to other countries. Unfortunately, I am concerned that the trade issues have been framed far too narrowly – that is, simply in terms of whether particular legislative provisions could be consistent with the rules of the WTO. Of course, WTO consistency is a critical question. The greater risk, however, is that import measures emanating from U.S. legislation could prompt mirror action (or simple trade retaliation) by other countries – with U.S. exports being among the targets. This scenario could unfold long before any potential disputes were concluded in the WTO.

The consequences for global trade could be enormous. Trade sanctions, potentially applied by multiple countries and at cross-purposes, could affect large volumes of economic activity in carbon-intensive industries – sensitive sectors such as steel, cement, aluminum and paper – and affect imports from key players. Imposing import measures on such a large scale could inflict significant economy-wide harms on both the target countries and the countries imposing such measures, and threaten the foundations of the world trading system. This risk is not an illusory one, as several European leaders have already made highly visible comments that a European carbon tax should be applied, for example, to imports from countries that have not adopted mandatory carbon reduction programs, including the United States.

Moreover, the central premise of this type of approach is doubtful – that the threat of import measures will bring key developing countries to the table. In fact, the threat could easily backfire. Developing countries could resent what they perceive to be U.S. strong arm tactics and arguably be less, not more, amenable to work on the hard issues in international climate negotiations. The stick, not the carrot, would set the tone. And other countries could well turn to the stick themselves and develop their own import restrictions, based on their own unilateral definitions of what constitutes adequate action by other countries.

Finally, such trade threats can themselves dramatically unsettle markets. The specter of a shutdown of large sectors of global production would hang like the proverbial “Sword of Damocles” over climate negotiations. Whether the sword drops or not, uncertainty and fear will rule global investments and risk-taking, instead of growth and innovation. We are more likely to achieve global improvements in the environment generally – and in battling the challenge of climate change specifically – if we have a growing world-wide economy. In light of these concerns, USTR is carefully studying the three options laid out in your recent White Paper.

The first option – requiring importers to buy allowances for certain imports from countries with climate regimes that the United States determines are not “comparable” to the U.S. system – seems to raise many of the policy concerns I laid out. This option also underscores the importance of negotiating and establishing a global framework of commitments to reduce greenhouse gas emissions, one in which all major emitters contribute to solutions.

We intend on continuing to study the other two approaches that are considered in the white paper. The second option concerns the development of “carbon-intensity” performance standards or regulations that would apply to both domestic and imported “energy intensive” products. While the use of mandatory standards (“technical regulations,” in WTO parlance) to achieve environmental objectives is not new, one of the unique aspects of the second option is that it appears to focus on how a good is

produced apart from the physical characteristics or end-uses of the final product. Relevant questions regarding trade implications are likely to include the opportunities that foreign and domestic producers and other interested stakeholders have to participate in the development of specific standards and whether compliance with such standards will be mandatory or voluntary under U.S. law. Other questions include whether carbon intensity standards could be based on internationally-developed standards, and what types of procedures are being contemplated for assessing conformity with such standards.

In this regard, I would note that the U.S. standards system, in general, has always been driven largely by the private sector. The U.S. government does not utilize standards as a tool for industrial policy. Rather, we allow markets to determine – based on criteria such as technical merit, consensus, and market relevance – what standard or standards will be utilized in manufacturing supply chains. This position is built on a recognition that a government-run standards development process could never keep up with the pace of technological change in the marketplace, and that a top-down approach could create serious market distortions. The U.S. system creates the conditions for maximizing economic growth, and promotes market dynamism and the harmonization of standards across borders. This long-standing policy was ingrained in U.S. law in 1996 via the National Technology Transfer and Advancement Act (NTTAA). In particular, the NTTAA provides that, when regulating, U.S. regulators need to use technical standards that have been developed or adopted by voluntary consensus standards bodies – rather than developing their own standards – unless the use of such standards would be inconsistent with applicable law or otherwise impractical.

Finally, the third option appears to be the least developed, at least in terms of the description provided in the white paper. Without more information on what is meant by “carbon markets” and “conditions on access,” it is difficult to assess whether there may be any trade implications to this approach.

It is important to keep our eye on the ball – the negotiation of a comprehensive international climate agreement – and press others to do the same. It is important to consider the potentially serious and negative impact that climate change-related trade restrictions, particularly those that affect certain imports, could have in damaging the multilateral trading system and the competitiveness of the U.S. economy. I look forward to working with the Congress to develop approaches that can avoid such implications.

Sincerely,

A handwritten signature in black ink, appearing to read "Susan C. Schwab". The signature is fluid and cursive, with the first name "Susan" being the most prominent part.

Susan C. Schwab

cc: The Honorable John Dingell  
The Honorable Joe Barton  
The Honorable Fred Upton